

Bankruptcy



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Introduction

Service members having problems with paying their bills are often faced with garnishment or repossession and consider bankruptcy as a solution to their problems. This article provides guidance on the basics of bankruptcy law.

What is Bankruptcy?

Bankruptcy provides a method to temporarily suspend the need to pay certain debts during the course of the proceeding (through the "automatic stay"). If the proceeding is successful, certain debts are discharged and are no longer owed. The goal of bankruptcy law is to give the debtor a fresh start financially for those who qualify. Bankruptcy law is primarily federal law, with state law providing certain "exemptions" such as how much money and/or property you can keep and not have to give to the US Trustee.

Automatic Stay

Once one files for bankruptcy, an "automatic stay" is put in place that prevents creditors from attempting to collect on any debts incurred before filing. Creditors may petition the court for relief from the automatic stay and permission to continue.

Discharge

After the bankruptcy proceedings are complete, a finding that a person is "bankrupt" results in a discharge of the personal debts. The discharge acts as a forgiveness of personal liability for certain debts incurred prior to filing for bankruptcy. In most instances, creditors are prohibited from suing or attempting to collect debts that have been discharged.

A debtor can be denied a discharge for certain "bad acts" such as concealing or fraudulently transferring assets prior to filing. Even if a discharge is granted, certain debts can never be discharged, such as:

- alimony and child support;
- student loans (unless a hardship exists);
- recent taxes;
- any debt incurred through the debtor's fraud; and
- certain other uncommon and specific debts (such as certain condo association fees).

Your Options

Individuals may choose several different types of bankruptcy based upon the amount and nature of the debts, the exemptions available, and the types of assets owned by the debtor. The different bankruptcies are named after a corresponding chapter in the code.

Chapter 7

Filing a Ch. 7 is the cheapest and quickest route of each of the bankruptcy options. Chapter 7 is referred to as "straight" or "liquidation bankruptcy." In a liquidation, the debtor discloses all of his or her assets to a trustee who then sells any non-exempt assets and distributes the proceeds to the debtor's creditors. Every state allows a debtor, even in a liquidation, to keep some amount of property (based on federal or state exemption laws).

An individual is then discharged of all debts. Creditors must look solely to the assets held by the trustee for payment. Creditors are thereafter prohibited from attempting to collect their claims from the discharged debtor. A debtor can receive a Chapter 7 discharge once every eight years.

A person must qualify in order to use Ch. 7. Eligibility for and individual is determined through a specified formula called the "means test" that calculates your income. If you don't qualify under the means test, you must file under Ch. 13.

Chapter 13

Filing a Chapter 13 is more expensive than filing a Chapter 7, but you are able to keep much, if not all, of your property. Chapter 13 debtors pay their debts through future income rather than liquidation or foreclosure of present assets. This option is generally chosen by those with a regular income.

Under Chapter 13, the debtor presents a plan for repayment, which is reviewed by the trustee, the creditors, and the Bankruptcy Court. Over time, the plan must provide creditors with an amount at least equal to what they would receive under a Chapter 7 and must be feasible in light of the debtor's income. If the plan is approved, then the debtor makes payments to the trustee who in turn pays the creditors. Plans usually run at least three years and cannot run longer than five.

Co-Debtors

A bankruptcy filing often involves others (i.e., a spouse) who have cosigned notes or mortgages with the debtor. The filing of a Chapter 13 plan can be used to stop all creditor actions against certain co-debtors. This is true even if the co-debtors are solvent and don't join the Chapter 13 petition. This protection can become permanent if the plan provides for payment of the cosigned debt in full and is fully performed.

Sources:

<http://www.uscourts.gov/bankruptcycourts.html>;
<http://www.cob.uscourts.gov/>;
11 U.S.C. § 707;
<http://www.usdoj.gov/ust>.

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