

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 gives a person a method to temporarily suspend or discard debt that has become too burdensome for them to repay. The goal of bankruptcy law is to give the debtor a fresh start financially for those who qualify. All bankruptcy cases are handled in federal courts under rules outlined in the U.S. Bankruptcy code.

Automatic Stay

When a person 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" often leads to 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;
- certain educational benefits or loans;
- certain taxes;
- any debt incurred through the debtor's fraud;
- debts for death and personal injury;

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. The Bankruptcy Code will allow the debtor to keep certain "exempt" property; but the trustee will liquidate the debtor's remaining assets.

Although an individual who files for Chapter 7 bankruptcy will usually receive a discharge of debts, the right to a discharge is not absolute because some types of debts are not discharged such as a lien on a property. Nevertheless, individual debtors receive a discharge in 99% of chapter 7 cases. A debtor can receive a Chapter 7 discharge once every eight years.

A person must qualify in order to use Ch. 7. Eligibility for an 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 bankruptcy is designed for individual debtors with regular source of income.

Under Chapter 13, the debtor presents a three to five year 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. Chapter 13 is very different from Chapter 7 since debtors get to retain ownership of their assets, but debtor must complete the payment plan before the debts are discharged. Chapter 13 discharges are also broader than Chapter 7, and the debtor is protected from garnishments and lawsuits while the payment plan is ongoing.

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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