

Title:

Bankruptcy-Chapter 13 Or Chapter 7?

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Summary:

The main purpose of bankruptcy laws is to give people hopelessly overburdened with debt a financial fresh start. Bankruptcy filings are public records. However, under normal circumstances, no one will know about the bankruptcy. Credit Bureaus will maintain a record of the bankruptcy and it will remain on the credit record for 10 years.

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Article Body:

The main purpose of bankruptcy laws is to give people hopelessly overburdened with debt a financial fresh start. Bankruptcy filings are public records. However, under normal circumstances, no one will know about the bankruptcy. Credit Bureaus will maintain a record of the bankruptcy and it will remain on the credit record for 10 years.

The most common reasons for bankruptcy filings are unemployment, large medical expenses; seriously overextended credit; marital problems, and other large unexpected expenses.

There are two ways a debtor can go bankrupt. The first and most common way is for an individual to file a voluntary petition asking the Court to allow bankruptcy. The second, and rarely used way, is for creditors to ask the Court to make an Order that a person is bankrupt. In this way, a creditor can gain payment, at least in part, for debts a debtor is refusing to pay. In both these cases a Bankruptcy Trustee is required to administer the bankruptcy.

There are two different types of legal bankruptcy proceedings.

Chapter 7, also called a straight bankruptcy, is a liquidation proceeding. The debtor gives all non-exempt property to a bankruptcy trustee who then converts

it to cash for distribution to creditors. The debtor is freed from all dischargeable debts, usually within 4 months. Chapter 7 is filed in cases where the debtor has few assets to lose, so this option gives a relatively quick release from debts. A debtor can file Chapter 7 again if more than 8 years have passed since discharge of a previous Chapter 7 bankruptcy.

Chapter 13 bankruptcy is also called a reorganization bankruptcy. It is filed by individuals who wish to pay off their debts in 3 to 5 years. This type of proceeding is suited for individuals with non-exempt property they wish to keep. It is only an option for individuals who have predictable income and whose income is sufficient to pay their reasonable expenses with some amount left over to pay off their debts.

Under the new Bankruptcy Law which took effect on October 17, 2005, individuals who can afford to make some repayment of their debts must file Chapter 13. Only debtors who meet strict financial requirements are allowed to erase their debts completely through Chapter 7. Debtors must take an approved Financial Counseling Course within 6 months of filing. Then, their income is assessed according to the formula (monthly income-expenses) X 60. If the result is \$6,000 or less, and unsecured debts are less than 25%, Chapter 7 is allowed. If income is greater than \$10,000 or unsecured debts are greater than 25%, the debtor must file Chapter 13.

Once bankruptcy is filed, creditors are forbidden from harassing the debtor. By law, creditors cannot initiate or continue any lawsuits, wage garnishees, or even make telephone calls demanding payments. Secured creditors such as banks holding, for example, a lien on a car, will get the stay lifted if the debtor cannot make payments.

Spouses are legally unaffected by a debtor's bankruptcy if they are not responsible (did not sign an agreement or contract) for any of the debt. If they have a supplemental credit card they are probably responsible for that debt. However, in community property states, either spouse can contract for a debt without the other spouse's signature on anything, and the spouse will still be obligated to pay. There are some exceptions to this rule, such as the purchase or sale of real estate; those few exceptions do require the signature of both spouses on the contract for both to be liable. But mundane purchases, such as credit cards, do not require both spouses to have signed. Community property states are: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington and Wisconsin.

Declaring bankruptcy does not mean that an individual's subsequent access to credit is cut off. Whether a debtor is allowed to keep credit cards after filing

bankruptcy is up to the credit card company. If the bankruptcy involves discharging a credit card, the card company will cancel the card unless the debtor reaffirms the debt. Even if the card has a zero balance the credit card company might still cancel the card.

A number of banks now offer "secured" credit cards, for which the debtor puts up a certain amount of money (as little as \$200) in an account at the bank to guarantee payment. Initially the credit limit is equal to the security given and is increased as the debtor demonstrates ability to pay the debt.

Two years after a bankruptcy discharge, debtors are eligible for mortgage loans on par with applicants of the same financial profile who have not filed bankruptcy. Income stability and the size of the down payment are seen as more relevant than a past bankruptcy filing. Though bankruptcy stays on a credit report for 10 years, it becomes less significant as time passes. People who have filed for bankruptcy are often better credit risks than people who have not, and are struggling to pay multiple accumulated debts.

Debtors filing for bankruptcy are allowed to keep certain assets. The exemption for a homestead is limited to \$125,000 if the property was acquired within the previous 1215 days (3.3 years). The cap is not applicable to any interest transferred from a debtor's previous principal residence which was acquired prior to the beginning of the 1215-day period. The value of the state homestead exemption is reduced by any addition to the value brought about on account of a sale of nonexempt property made by the debtor with the intent to evade or defraud creditors during the 10 years before the bankruptcy filing.

An absolute \$125,000 homestead cap applies if either the court determines that the debtor has been convicted of a felony demonstrating that the filing of the case was an abuse of the provisions of the Bankruptcy Code, or the debtor owes money due to criminal acts. This limitation is not applied if the homestead property is "reasonably necessary for the support of the debtor and any dependent of the debtor."

Some laws relating to bankruptcy vary from state to state. Legal residency is determined by which state the debtor lived in the 730 days (2 years) before filing; or if the debtor did not live in a single state in the previous 2 years, the state of residence where the debtor spent the majority of the 180 period preceding the 2 years. If this leaves the debtor ineligible for any exemptions then the debtor is allowed use federal exemption laws.

In some cases of Chapter 7 bankruptcy, tax debts are also wiped out, but only if stringent conditions are met: the IRS does not have a tax lien against the

debtor's property; no fraudulent tax returns have been filed; tax liability is due for a tax return filed at least 2 years before the bankruptcy filing; the tax return was due at least 3 years ago, and the taxes were assessed at least 8 months before filing for bankruptcy.

Student loans from government and private organizations are usually not wiped out, unless repayment would cause undue hardship to the debtor.

All non-exempt property, such as real estate, cars and motorcycles will then be liquidated by the trustee.

There is no legal requirement to use a lawyer to file for bankruptcy, and debtors can do so themselves for about \$300; however, it is strongly advised the use the services of a specialized bankruptcy lawyer as bankruptcy law is complex. A bankruptcy lawyer is well worth the cost, which is usually only \$1,600 to \$2,000. Debtors will recoup the legal fees many times over through peace of mind and avoidance of stress in addition to actual money saved by following the bankruptcy attorney's advice.