Bankruptcy

SPACE BASE DELTA 1 LEGAL OFFICE

135 DOVER STREET, BLDG 350, SUITE 2068
PETERSON SFB, CO 80914-1148
(719) 556-4871
DSN 834-4871

210 FALCON PARKWAY, SUITE 2104
SCHRIEVER SFB, CO 80912-2104
(719) 567-5050
DSN 560-5050

The information provided in this document is meant for the sole use of Active Duty service members, retirees, their families, and other personnel eligible for legal assistance from the Space Base Delta 1 Legal Office. The information is general in nature and meant only to provide a brief overview of various legal matters. Rights and responsibilities vary widely according to the particular set of circumstances in each case. Laws can vary across states, services, and civilian jurisdictions and laws changes from time to time. <u>Do not rely upon the general restatements of background information presented here without discussing your specific situation with a legal professional.</u>

Current as of June 2021

BANKRUPTCY

Introduction

Service members who have problems 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 should always be the method of last resort for resolving your financial situation. While bankruptcy has its advantages, it also has huge ramifications on your credit history and can negatively affect your career and livelihood. Bankruptcy provides a means to temporarily suspend the need to pay certain debts during the course of the proceeding. If the proceeding is successful, creditors can no longer collect on those debts. The purpose of filing for bankruptcy is to give the debtor a fresh start financially; however, declaring bankruptcy will make it more difficult to obtain mortgages and car loans and can affect security clearances.

Bankruptcy cases cannot be filed in state courts because they are governed by federal law. These procedures are covered under Title 11 of the United States Code (the Bankruptcy Code). The vast majority of cases are filed under the three main chapters of the Bankruptcy Code: Chapter 7, Chapter 11, and Chapter 13.

Automatic Stay

Once a person files for bankruptcy, an "automatic stay" is enacted that prevents creditors from attempting to collect on any debts incurred before filing. Creditors may, however, petition the court for relief from the automatic stay and request permission to continue attempting to collect the debt. Often, creditors whose loans are secured by a pledge of property (a lien) are permitted to take possession of that property.

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 all debts incurred prior to filing for bankruptcy. In most but not all instances, creditors are prohibited from suing or attempting to collect debts that have been discharged. Once discharge is granted, former creditors also have no claim on a person's future income.

It is important to list all your property and debts in your bankruptcy schedules. If you do not list a debt, for example, it is possible the debt will not be discharged. The judge can also deny your discharge for certain "bad acts" such as concealing or fraudulently transferring assets prior to filing. Even if the discharge is granted, certain debts can never be discharged, such as:

- alimony and child support
- student loans
- most taxes

- any debt incurred through the debtor's fraud or theft
- court fines and criminal restitution
- certain other uncommon and specific debts (e.g., certain condo association fees)

Your Options

Individuals may choose several different types of bankruptcy depending on the amount and nature of the debts, the exemptions available, and the types of assets owned by the debtor. The different types of bankruptcies are named after their corresponding chapter in the Code. In 2005, the Bankruptcy Code was amended to require that most individual debtors complete credit counseling with an approved counseling agency at least 6 months before filing for bankruptcy. A list of approved agencies can be found at https://www.justice.gov/ust/list-credit-counseling-agencies-approved-pursuant-11-usc-111.

Chapter 7

Chapter 7 is referred to as "straight" or "liquidation bankruptcy" and individuals, corporations, partnerships and other business entities are eligible to file. In liquidation, the debtor turns all of his or her assets over to a trustee who then sells all the assets and distributes the proceeds to the debtor's creditors.

An individual is then discharged of all debts (partnerships and corporations are not). 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.

Every state allows a debtor, even in a liquidation, to keep some small amount of property.

Under the bankruptcy law, a person must qualify in order to use Chapter 7. Eligibility for an individual is determined through a specified formula called the "means test." For more information on the means test, visit http://www.justice.gov/ust/eo/bapcpa/meanstesting.htm. Persons not qualifying under the means test for Chapter 7 protection must file under Chapter 13.

Chapter 13

Chapter 13 debtors pay their debts through future income rather than liquidation or foreclosure of present assets. This option is generally chosen by individuals with regular income. As of 2020, this Chapter allows the debtor to keep much of his or her property and is available to debtors with unsecured debts (often credit card debts) less than $394,725 and secured debts less than $1,184,200 (home mortgages and car loans).

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.

While a debtor under Chapter 13 gets to keep much of his or her property, there are certain disadvantages such as:

- Debtors remain under court supervision for the life of the plan (up to five years) and are forbidden from making new debts or selling assets without court permission.
- Debtors who propose less than full payment to unsecured debtors will be forced to live on a budget for the life of the plan and pay all excess income to the creditors.
- Even if the debtor pays all of the creditors in full, the bankruptcy will still appear on the debtor's credit record.

If the debtor is unable to complete the plan payments, then any creditor may petition to have the court convert the case to a Chapter 7 liquidation.

Chapter 11

Chapter 11 is a reorganization proceeding, usually involving corporate debtors but it is also available to individuals who have engaged in commercial enterprise. This Chapter is used when the owner desires to stay in business, restructure existing debts, retain assets, and/or attempt to reorganize under court supervision.

Taxes

Filing bankruptcy under either Chapter 7 or Chapter 11 will stop all IRS or state tax collection activities. However if a Chapter 7 is filed, the tax collection activities resume shortly after filing because the tax obligation cannot be discharged in bankruptcy. Furthermore, interest and penalties continue to accrue. Under Chapter 13, filing halts the accumulation of interest and penalties, and taxes may be paid over the life of the plan.

Co-Debtors

A bankruptcy filing often involves other persons (such as the debtor's 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 do not 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.

Conclusion

Your individual financial situation may alter the generalities and conclusions set forth in this article. For your specific situation, you should seek counsel from an attorney before filing for bankruptcy relief.