K.2 Answers to Common Bankruptcy Questions

A decision to file for bankruptcy should be made only after determining that bankruptcy is the best way to deal with your financial problems. This brochure can not explain every aspect of the bankruptcy process. If you still have questions after reading it, you should speak with an attorney familiar with bankruptcy.

There have been many news reports suggesting that changes to the bankruptcy law passed by Congress in 2005 prevent many individuals from filing bankruptcy. It is true that these changes have made the process more complicated. But the basic right to file bankruptcy and most of the benefits of bankruptcy remain the same for most individuals.

What Is Bankruptcy?

Bankruptcy is a legal proceeding in which a person who can not pay his or her bills can get a fresh financial start. The right to file for bankruptcy is provided by federal law, and all bankruptcy cases are handled in federal court. Filing bankruptcy immediately stops all of your creditors from seeking to collect debts from you, at least until your debts are sorted out according to the law.

What Can Bankruptcy Do for Me?

Bankruptcy may make it possible for you to:

* Eliminate the legal obligation to pay most or all of your debts. This is called a "discharge" of debts. It is designed to give you a fresh financial start.

* Stop foreclosure on your house or manufactured home and allow you an opportunity to catch up on missed payments. (Bankruptcy does not, however, automatically eliminate mortgages and other liens on your property without payment.)

* Prevent repossession of a car or other property, or force the creditor to return property even after it has been repossessed.

* Stop wage garnishment, debt collection harassment, and similar creditor actions to collect a debt.

* Restore or prevent termination of utility service.

* Allow you to challenge the claims of creditors who have committed fraud or who are otherwise trying to collect more than you really owe.

What Bankruptcy Can Not Do

Bankruptcy can not, however, cure every financial problem. Nor is it the right step for every individual. In bankruptcy, it is usually *not* possible to:

* Eliminate certain rights of "secured" creditors. A creditor is "secured" if it has taken a mortgage or other lien on property as collateral for a loan. Common examples are car loans and home mortgages. You *can* force secured creditors to take payments over time in the bankruptcy process and bankruptcy *can* eliminate your obligation to pay any additional money on the debt if you decide to give back the property. But you generally can not keep secured property unless you continue to pay the debt.

* Discharge types of debts singled out by the bankruptcy law for special treatment, such as child support, alimony, most student loans, court restitution orders, criminal fines, and most taxes.

* Protect cosigners on your debts. When a relative or friend has cosigned a loan, and the consumer discharges the loan in bankruptcy, the cosigner may still have to repay all or part of the loan.

* Discharge debts that arise after bankruptcy has been filed.

What Different Types of Bankruptcy Cases Should I Consider?

There are four types of bankruptcy cases provided under the law:

* *Chapter* 7 is known as "straight" bankruptcy or "liquidation." It requires an individual to give up property which is not "exempt" under the law, so the property can be sold to pay creditors. Generally, those who file chapter 7 keep all of their property except property which is very valuable or which is subject to a lien which they can not avoid or afford to pay.

* *Chapter 11*, known as "reorganization," is used by businesses and a few individuals whose debts are very large.

* *Chapter 12* is reserved for family farmers and fishermen.

* *Chapter 13* is a type of "reorganization" used by individuals to pay all or a portion of their debts over a period of years using their current income.

Most people filing bankruptcy will want to file under either chapter 7 or chapter 13. Either type of case may be filed individually or by a married couple filing jointly.

Chapter 7 (Straight Bankruptcy)

In a bankruptcy case under chapter 7, you file a petition asking the court to discharge your debts. The basic idea in a chapter 7 bankruptcy is to wipe out (discharge) your debts in exchange for your giving up property, except for "exempt" property which the law allows you to keep. In most cases, all of your property will be exempt. But property which is not exempt is sold, with the money distributed to creditors.

If you want to keep property like a home or a car and are behind on the mortgage or car loan payments, a chapter 7 case probably will not be the right choice for you. That is because chapter 7 bankruptcy does not eliminate the right of mortgage holders or car loan creditors to take your property to cover your debt.

If your income is above the median family income in your state, you may have to file a chapter 13 case. Median family income is different in each state. For example, in 2009, the median income for a family of four ranged from a low of just under $60,000 in Oklahoma to almost $100,000 in Maryland. Other states fall in between. Higher-income consumers must fill out "means test" forms requiring detailed information about their income and expenses. If the forms show, based on standards in the law, that they have a certain amount left over that could be paid to unsecured creditors, the bankruptcy court may decide that they can not file a chapter 7 case, unless there are special extenuating circumstances.

Chapter 13 (Reorganization)

In a chapter 13 case you file a "plan" showing how you will pay off some of your past-due and current debts over three to five years. The most important thing about a chapter 13 case is that it will allow you to keep valuable property--especially your home and car--which might otherwise be lost, if you can make the payments which the bankruptcy law requires to be made to your creditors. In most cases, these payments will be at least as much as your regular monthly payments on your mortgage or car loan, with some extra payment to get caught up on the amount you have fallen behind.

You should consider filing a chapter 13 plan if you:

* Own your home and are in danger of losing it because of money problems;

* Are behind on debt payments, but can catch up if given some time;

* Have valuable property which is not exempt, but you can afford to pay creditors from your income over time.

You will need to have enough income during your chapter 13 case to pay for your necessities and to keep up with the required payments as they come due.

What Does It Cost to File for Bankruptcy?

It now costs $299 to file for bankruptcy under chapter 7 and $274 to file for bankruptcy under chapter 13, whether for one person or a married couple. The court may allow you to pay this filing fee in installments if you can not pay it all at once. If you hire an attorney you will also have to pay the attorney fees you agree to.

If you are unable to pay the filing fee in installments in a chapter 7 case, and your household income is less than 150 percent of the official poverty guidelines (for example, the figures for 2009 are $21,855 for a family of two and $33,075 for a family of four), you may request that the court waive the chapter 7 filing fee. The filing fee can not be waived in a chapter 13 case, but it can be paid in installments.

What Must I Do Before Filing Bankruptcy?

You must receive budget and credit counseling from an approved credit counseling agency within 180 days **before** your bankruptcy case is filed. The agency will review possible options available to you in credit counseling and assist you in reviewing your budget. Different agencies provide the counseling in-person, by telephone, or over the Internet. If you decide to file bankruptcy, you must have a certificate from the agency showing that you received the counseling before your bankruptcy case was filed.

Most approved agencies charge between $30/-/$50 for the pre-filing counseling. However, the law requires approved agencies to provide bankruptcy counseling and the necessary certificates without considering an individual's ability to pay. If you can not afford the fee, you should ask the agency to provide the counseling free of charge or at a reduced fee.

If you decide to go ahead with bankruptcy, you should be very careful in choosing an agency for the required counseling. It is extremely difficult to sort out the good counseling agencies from the bad ones. Many agencies are legitimate, but many are simply rip-offs. And being an "approved" agency for bankruptcy counseling is no guarantee that the agency is good. It is also important to understand that even good agencies won't be able to help you much if you're already too deep in financial trouble.

Some of the approved agencies offer debt management plans (also called DMPs). A DMP is a plan to repay some or all of your debts in which you send the counseling agency a monthly payment that it then distributes to your creditors. Debt management plans can be helpful for some consumers. For others, they are a terrible idea. The problem is that many counseling agencies will pressure you into a debt management plan as a way of avoiding bankruptcy whether it makes sense for you or not. You should not consider a debt management plan if making the monthly plan payment will mean you will not have money to pay your rent, mortgage, utilities, food, prescriptions, and other necessities. It is important to keep in mind these important points:

* Bankruptcy is not necessarily to be avoided at all costs. In many cases, bankruptcy may actually be the best choice for you.

* If you sign up for a debt management plan that you can't afford, you may end up in bankruptcy anyway (and a copy of the plan must also be filed in your bankruptcy case).

* There are approved agencies for bankruptcy counseling that do not offer debt management plans.