

A GUIDE TO FILING FOR BANKRUPTCY

PROTECTION UNDER CHAPTER 7

OF THE BANKRUPTCY CODE

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GUIDE TO OBTAINING A “FRESH START”

UNDER THE BANKRUPTCY CODE

Introduction:

Any type of legal action takes planning. The decision to file for bankruptcy protection is no different. Through planning, personal property, cash and even real property may be saved. For this reason you should consider hiring an attorney, not a paralegal to prepare your papers. Remember, an attorney is able give legal advice on a multitude of subjects. A paralegal is only permitted to type what you tell them and if you don't know the questions, then you can't find out the answers.

Types of Bankruptcies:

There are three principle types of bankruptcies, Chapters 7, 11 and 13. This article is only concerned with a Chapter 7 filing, which refers to the terms liquidation and “fresh start.” Liquidation is simple. It means all the assets of the person owing the money (called the debtor) are collected by a neutral person (called a trustee), sold and the money given (disbursed) to the people to whom money is owed (creditors). However, there are many exceptions to this rule (called exemptions) allowing you to keep most of your personal property and a large amount of cash. (Fed. B.C. § 101.) The policy behind a Chapter 7 filing is to give the debtor a “fresh start.” In many cases all the assets are exempt and there is no distribution to the creditors.

Once all the property is disposed of, or found to be exempt, and any remaining money is disbursed, the debtor is no longer legally responsible for any of the debts incurred before the bankruptcy petition has been filed. This means the debts have been discharged and legally excused. A debtor may only receive a Chapter 7 discharge once every 8 years. (Fed. B.C. § 109; 28 U.S.C. § 1409.)

Discharge and Non-Dischargeable Debts:

The terms “discharge” and “non-dischargeable debts” have legal significance. A discharge is a court order that excuses the debtor from all debts listed in the bankruptcy petition, except those found to be non-dischargeable.

The Federal Bankruptcy Code lists specific items that cannot be discharged in a bankruptcy proceeding. In legal jargon these are non-dischargeable debts:

1. Certain Taxes, if due within the last three years.
2. Money, property, services or credit obtained by fraud including false financial statements. This also includes certain debts incurred in the 60-day period prior to the filing of the bankruptcy petition.
3. Money obtained by fraud, embezzlement or theft and debts incurred for an intentional or malicious injury to the person or property of another.
4. Alimony, maintenance and support, with very limited exceptions.
5. Government fines or penalties including criminal restitution.
6. Money obtained for educational benefits and student loans except in limited circumstances.
7. Liability for death or personal injury caused by drunk driving.
8. Debts that were or could have been listed in a previous bankruptcy case where the debtor did not receive a discharge.

Exemptions:

The Bankruptcy Code provides for exemptions for certain property. (Fed. B.C. § 522(b).) If all of the property falls into the exemption then the case is called a no asset case and the creditors get nothing. Property falling into one of the exemptions may be kept by the debtor both during the proceeding and after the case is discharged. Property that may not be exempt may be converted to exempt property before any petition is filed. The value of the property is the value on the date of filing. (Fed. B.C. § 522(a)(2).)

California has chosen to opt out of the Federal Bankruptcy exemptions. (Cal. Code Civ. Proc. § 703.130.) This means the debtor may chose between two different sets of

exemptions under state law. (Cal. Code Civ. Proc. §; 703.140(b); 704.010 et seq.) Each of these sections are more liberal in favor of the debtor than the federal exemptions. Also there is a third section for those who want to avoid the court system and proceed under an Assignment for the Benefit of Creditors. (Cal. Code Civ. Proc. § 1801 et seq.)

Types of Creditors:

There are two types of creditors, secured and unsecured. A secured creditor is one that retains some rights as to the property of the debtor, such as a car lease, your mortgage company, etc. An unsecured creditor is someone with no lien or mortgage against the property. An example of this is medical bills, credit cards, personal loans, etc.

Concerning a secured creditor, the debtor has three choices:

1. Reaffirm: This is an agreement (a reaffirmation) between the creditor and the debtor that the debtor will continue to make payments on the debt. The creditor cannot repossess the property as long as payments are made. The court must approve any agreement between the creditor and debtor for it to be binding on the creditor. While a debtor is free to repay any debt the debtor chooses, without any obligation to another creditor, this defeats the purpose of a “fresh start.”
2. Redeem: The debtor has the option of purchasing the property, usually for a one-time cash payment.
3. Release: The debtor may simply give the property back and the debt will be discharged. If the value of the property is less than what is owed, the additional sum is still discharged.

Concerning unsecured creditors, the court will notify them if there are any assets. If so they are entitled to file a claim. If there are no assets the unsecured creditor’s claim will be discharged even if that creditor was not listed in the petition. However, the better practice is to list all the creditors.

Concerning utility companies, if you furnish the company with a deposit or other security within 20 days of filing the petition, to make sure future services are covered, they cannot discriminate against you. (Fed. B.C. § 366(b).) However, the better practice would be to pay the bills before filing so they are not considered a creditor.

Finally, after discharge a creditor cannot attempt to collect any pre-petition debt that has been discharged. The remedy for any attempt is a contempt order from the court. Any attempts at collection should be reported to your attorney who will provide the creditor with a copy of the discharge. If the creditor continues to try to collect the debt, an action may be brought in the bankruptcy court for the violation.

Who Can File:

Anyone who resides in, does business in, or has property in the United States may file under a Chapter 7 proceeding except the following:

1. Any person involved in a previous bankruptcy case that was dismissed within the last 180 days and is under a court order prohibiting the filing of another case;
2. Any person who has been granted a discharge under Chapter 7 within the last 8 years. (Fed. B.C. § 109; 28 U.S.C. § 1409.)

Fees and Costs:

Attorney's fees will be discussed individually but they include consultation, preparation of the petition, and pre and post-petition negotiation with creditors. You can also expect \$450.00 in costs including the court filing fee, credit report, asset report and photocopying, postage, certified mailings and other administrative matters.

Generally the husband and wife filing jointly may keep the costs to a minimum. With a joint filing only one petition is prepared and filed and one fee is paid. Since California is a community property state debts incurred during the marriage by one spouse are attributable to both and are jointly and severally liable. There may be some

very limited exceptions to this. The same is true for a discharge. Once the debts are discharged as to one spouse, they are discharged as to the other as well but only as to community property funds. If separate property funds are obtained, these can be reached by the creditor.

If it can be proven that the debts were incurred prior to marriage, and were never made part of the community, then the spouse who did not incur the debts may not be liable for them. However, the longer the marriage the less likely the debt will be found to be separate from the community.

When Should You File A Chapter 7:

A determination of whether or not you should file bankruptcy depends on both a common sense and legal analysis of all of the following items. This is perhaps the key reason why you should consult with an attorney instead of a paralegal. Factors an attorney will look at are:

1. The type of debt you have, dischargeable v. non-dischargeable.
2. The extent of your debt and whether there are other alternatives.
3. Your income and whether you have the ability to repay part or all of your debt over time.
4. What exemptions may be claimed.
5. Have all debts been incurred and have nonexempt assets been converted to exempt assets.
6. Has all non-exempt property been received.
7. An analysis of all trusts, life insurance policies, divorces within 180 days, pending foreclosures, and cash advances.

The Means Test:

Another factor in determining if you qualify for a Chapter 7 filing is what is being referred to as the “Means Test.” This is actually very simple. The Census Bureau has established the median income for each state depending on the size of the household. If

your income is under the median then you are not affected by the new law, except to the extent you have to produce documents and undergo credit counseling.

If your income is over the median, then there is a formula for determining whether you qualify for a Chapter 7 filing. Only an attorney can do the analysis as each step of the process involves legal advice. Being over the median does not mean that you cannot file a Chapter 7 but we won't know until the entire analysis is completed. It is possible that at the end of the analysis you will have to file a Chapter 13 and repay part of the debt.

Credit Counseling/Debt Education:

One of the new requirements to filing is that you must undergo two sessions of credit counseling. The first session is called Credit Counseling and the second Debt Education. These sessions are accomplished on the internet through private companies. There seems to be a range of prices with the average being \$50.00 for the Credit Counseling and \$25.00 for the Debt Education. You must complete the Credit Counseling no more than 180 days before filing and complete the Debt Education within two weeks of filing. If you fail to complete either session you will not receive a discharge.

Documents:

The new law also contains a provision for producing a series of documents. The list is very extensive but not all of the documents will apply to you. This list will be discussed individually with you during your interview however, you should be aware that one of the prerequisites to filing is that you must be current on filing your tax returns. If you have not filed for a few years, or even last year, you cannot file a bankruptcy until the returns have been filed.

Some of the documents have to be filed with the petition. Others can be filed later. However, to avoid any possibility that your bankruptcy will be dismissed, our office requires all of the documents to be produced prior to filing so that we can deliver them to the trustee immediately upon filing.

What Happens When The Petition Is Filed:

Once the petition is filed, all collection efforts, including legal proceedings, by the creditors must stop. This is called an automatic stay. (Fed. B.C. § 362(a).) The court puts the creditors on notice that they must not make any effort at all to contact you concerning the debt. If the creditor violates the stay, the creditor may be liable for damages. (Fed. B.C. § 362(h).) The stay is only terminated if the creditor files a motion (a request) to the court to lift the stay and the court grants the request. (Fed. B.C. § 362(d).) This usually only involves problems with real property, an automobile or pending litigation.

There are very limited exceptions to the stay. Criminal proceedings and any civil actions to establish paternity, or to collect alimony, maintenance, child support or tax audits are not stayed. (Fed. B.C. § 362(b).)

Bankruptcy Procedures:

After the petition is filed, and the creditors notified of the filing, the court will schedule a meeting of creditors before an individual trustee. (Fed. B.C. § 341(a).) This hearing usually takes place about 20 to 40 days after the petition is filed and is probably the only hearing you will have to attend. (Fed. Rules Bankr. Proc. Rule 2003(a).) Creditors are notified but rarely attend. If they do, the trustee may allow them to ask you some limited questions but will not permit them to treat you in a disrespectful manner. You will be placed under oath at the hearing, which means you must tell the truth. Part of the attorney's job is to prepare you for that meeting.

After the meeting there are two time periods to keep in mind.

1. There is a 30-day period wherein the trustee may object to exemptions you have claimed (Fed. Rules Bankr. Proc. Rule 4003(b));
2. There is a 60-day period where in creditors may file a complaint concerning the dischargeability of their debt. (Fed. Rules Bankr. Proc. Rule 4007(c).)

After these time periods you simply wait for the discharge through the mail from the court. You must always keep the court informed of your current address until the case

is over. This usually happens about four months from the date the petition is filed or shortly after the time for objections has passed. The discharge eliminates all personal responsibility for the debts that have been discharged. (Fed. B.C. § 524(a).) After the discharge, in a no asset case, meaning all the property is exempt, a notice is sent to the creditors telling them there are no assets and the trustee closes the case. The discharge also acts as a permanent injunction against future collection efforts. (Fed. B.C. § 524(c)(d).)

Who Is The Trustee and What Is Your Role:

The trustee is a lawyer or accountant who is a member of a panel appointed to review bankruptcy filings. (Fed. B.C. § 701.) The Trustee reviews the petition, gathers the nonexempt property, attempts to convert it to cash and pay dividends to the creditors. They are paid about \$75.00 a case plus a percentage of the amount distributed to the creditors. You must cooperate with the trustee. If you don't comply with the requests of the trustee your case may be dismissed and you will be denied a discharge.

What About Your Credit After Filing:

Any bankruptcy filing remains on your credit for report for 10 years. While this may seem burdensome, it is a trade off for being able to discharge all your debts, protect your remaining assets and for saving your home. In short, it's a trade off for getting a fresh start.

You are not precluded from purchasing a home after a bankruptcy however you can expect the following:

1. Some lenders only working with "A" or "B" credit will deny you a loan.
2. Some may require a higher down payment.
3. Some will charge you additional points
4. Some will charge you a higher interest rate and higher points.

As to credit cards, again the rules are similar. There are some credit card companies that will send you a credit card almost immediately when you send them proof

of your discharge. However, the fees will be exorbitant and the credit limits very low, at least for the first year.

As to vehicles, this is something to talk to your attorney prior to filing the bankruptcy. Your attorney will advise you how to obtain a vehicle that will remain in good condition until you rebuild your credit.

There is always some embarrassment associated with filing for bankruptcy. There should not be. This is a legitimate legal tool to safeguard your assets and your future. Do not let any creditor give you a different impression.

Public Disclosure:

The filing of the bankruptcy petition causes the case to become a public record. Credit agencies are notified of the filing, as are your creditors. While business filings may be published, usually individual filings are not, unless they involve some person who is famous before the filing.

Employers are not notified of the filing and they cannot fire you because you filed for bankruptcy protection. The filing of the petition is not a criminal proceeding. Employers and governmental agencies cannot discriminate against any person who files for bankruptcy protection. This includes the fact you cannot be denied any kind of a license because of the filing.