

A GUIDE TO FILING FOR BANKRUPTCY

PROTECTION AND REORGANIZATION UNDER CHAPTER 13

OF THE BANKRUPTCY CODE

Michael R. Totaro
Totaro & Shanahan
P.O. Box 789
Pacific Palisades, CA 90272
310 573 0276 (v)
310 496 1260 (f)
Mtotaro@aol.com

GUIDE TO OBTAINING A REORGANIZATION
UNDER CHAPTER 13 OF 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 won'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 13 filing. The policy behind a Chapter 13 is to reorganize the debtor's finances so that the debtor may repay at least a portion of the unsecured debts and the arrearage on any secured debt the debtor intends to keep. The amount of debt to be repaid depends on what property the debtor has that is not exempt and what disposable income the debtor has after deducting allowable expenses. The debtor must repay debts to the extent there is disposable income or equity in assets that are not protected (exempted).

The Procedure:

Prior to filing the bankruptcy petition, the debtor and attorney work out a plan that they feel will be acceptable to the creditor, the Chapter 13 trustee and the court. Since the Chapter 13 trustee makes 10% of the monthly payment, there is an incentive for the trustee to look at the debtor's budget very carefully to determine if the budget includes items the trustee does not feel are appropriate to someone seeking bankruptcy protection.

Once the Petition and Plan are filed with the court, the court schedules a meeting of creditors under 11 U.S.C. §341 of the Bankruptcy Code (called a 341 hearing) and also a date for confirmation of the plan. In some areas the two hearings are held on the same

day but in most jurisdictions there is a substantial amount of time between the 341 hearing and the confirmation hearing.

Each jurisdiction handles the period of time between filing and confirmation differently. In all jurisdictions any mortgage payment that comes due must be sent to our office in the form of a cashier's check so that we may place it in the mail and verify it has been paid. As to the plan payment, some trustees want the payment brought to the 341 hearing and others want it paid on the anniversary date of the bankruptcy filing to a specified lockbox. We will advise you of what your trustee wants you to do. Generally in San Bernardino, Riverside and Orange Counties the check is brought to the 341 hearing. This also applies to any matter in front of the court in Woodland Hills. However if your case is assigned to downtown LA, one trustee wants the check brought to the hearing and one wants it mailed to the lockbox. We will let you know what to do.

Once your plan is confirmed, you resume making your normal monthly payments on your secured debt. These payments are now due on the due date with no grace period. So if your mortgage is due on the 1st it must be paid on the 1st. Your plan payment will always be due on the same day of the month as your petition was filed. So if you filed on the 11th the plan payment is due on the 11th.

The Chapter 13 Plan:

As part of the reorganization process, the debtor presents a plan to the Chapter 13 trustee and offers to pay back a portion of the unsecured debt and also any arrearage on the secured debt. The amount to be repaid is established in part by negotiation and in part by the Means Test which deducts allowable expenses from one's gross income. This is where it gets tricky. The debtor may have many expenses that are not allowable but necessary to the family. For example, the debtor cannot provide support for an adult child, meaning any child over the age of 18. This means you cannot pay for the college tuition for an 18 year old or any of their expenses if they are out of high school. This is just one example.

The plan gives the debtor a number of options. If the debtor is under the median income the payments may be made over 3 years. However, sometimes the arrearage on a home would result in too high of a payment if the term was 3 years and therefore 5 years would be better. In other cases 5 years may be chosen to keep the payment lower but the debtor may be entitled to pay it off earlier, but only if 100% of the unsecured creditors are being paid in full.

Once the plan is confirmed, the debtor simply continues to make payments under the plan for the plan period, whatever that may be. As noted the length of the plan is determined by the debtor's income level and the percentage of debt being repaid. The plan must be approved by the court and once approved it is binding on all listed creditors.

Upon completion of the plan payments, and the plan period, the debtor is entitled to a discharge. All listed debts are discharged even if only paid a fraction of what is owed. (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 choose 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. Surrender: 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 placed into the unsecured portion of the plan.

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, during the process and 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:

A company cannot file a Chapter 13. However, any individual who resides in, does business in, or has property in the United States may file under a Chapter 13 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 4 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 \$50.00 in costs including the court filing fee, a 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 even if only one spouse's name is on the debt. 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. However if only one spouse has filed the non-filing spouse will only have a discharge 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 13:

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.

In addition there are times when a Chapter 13 (or Chapter 11) is mandatory.

1. Too much unprotected equity in real or personal property:

Sometimes all of the equity in property cannot be protected. In a Chapter 7 the trustee would take the property and sell it. In a Chapter 13 you would not lose the property but would have to pay an amount equal to the unprotected equity to the unsecured creditors.

2. Too high of income:

If your income is just too high you would not qualify for a Chapter 7. The United States Trustee would demand you file a Chapter 13 and repay some of your debt.

3. Behind on Mortgage Payments or Wanting to Strip a Second:

If you are behind on mortgage payments on a home you want to keep, you must file a Chapter 13. If you file a Chapter 7 this is an indication you are giving up the home and the lender will move to lift the stay to foreclose. Also, if you want to strip a second mortgage or HELOC, this can only be accomplished in a Chapter 13 or Chapter 11. The court has no power to do this in a Chapter 7.

The Means Test:

Another factor in determining the amount of money you will have to repay is 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, undergo credit counseling and pay back only what is disposable from your actual income and expenses over a span of 3 years.

If your income is over the median, then there is a formula for determining how much you will have to pay back over 5 years. The people most affected by this formula are single people, with no children and no real property. Whatever income that is determine to be disposable goes to the unsecured creditors. The debtor would have to pay that in addition to any arrearage on second 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 \$25.00 for the Credit Counseling and \$15.00 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 requires the production of documents. The list is very extensive but not all of the document 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. Generally the documents are as follows:

1. Last two to four years federal taxes depending on the trustee;
2. Last six months pay stubs
3. The declarations page of your vehicle insurance
4. Mortgage Statements for first and second loans

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:

As discussed briefly above 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 and after the plan is confirmed, you simply make your payments for the plan period. At the end of this plan period the Court, upon motion, will

award a discharge. The discharge eliminates all personal responsibility for the debts that have been discharged. (Fed. B.C. § 524(a).) After the discharge 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 private lawyer appointed by the United States Trustee. The trustee's sole function is to make sure you are paying a fair share of your debts. The trustee collects the payments from you and disburses the funds to your 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. This trustee does not sell assets, but instead charges you with the unexempt portion of your assets in a like dollar amount to pay creditors. For example if the trustee says you have \$10,000 in non-exempt assets, you would have to pay \$10,000 of your debt over 3 to 5 years.

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.