

Bankruptcy

What is Bankruptcy?

Bankruptcy is a legal action in which one who cannot pay his or her bills can get a fresh financial start. Bankruptcy also benefits creditors by allowing them an opportunity to possibly collect a portion of the debtor's debt once bankruptcy is filed. The right to file for bankruptcy is provided for by federal law, and all bankruptcy cases are handled in federal court.

What is a Discharge?

A discharge is when the debtor's debts are expunged at the conclusion of the bankruptcy case. In essence, Discharge excuses you from paying your debts. In addition, the discharge order forbids creditors from collecting a debt that was included in the bankruptcy petition.

Will Bankruptcy Wipe Out All My Debts?

Personal bankruptcy usually does not erase child support, alimony, fines, taxes, and some student loan obligations. Also, unless you have an acceptable plan to catch up on your debt under Chapter 13, bankruptcy usually does not allow you to keep property when your creditor has an unpaid mortgage or lien on it (this is called a *secured debt*).

How Does Bankruptcy Protect Me?

Bankruptcy protects you and your property from certain actions by creditors **after** a bankruptcy petition is filed. When you file for bankruptcy, the court issues an *automatic stay*, a court order that prohibits:

(1) lawsuits against you to recover debts that occurred before you filed for bankruptcy; (2) enforcement of any legal judgment against you or against property of your estate; (3) any act to obtain possession of estate property or property in your estate's possession; (4) any act designed to create or enforce a lien against your property, such as a mortgage foreclosure; (5) the commencement or continuation of a case in the US Tax Court is specifically stayed, and (6) creditors may not bother, intimidate or harass you about repayment of obligations from before you filed for bankruptcy.

The automatic stay does NOT prohibit any of the following actions:

- (1) criminal proceedings,
- (2) alimony and/or child support,
- (3) modification orders to spousal or child support and/or paternity suits,
- (4) enforcement of judgments by governmental units, and
- (5) mortgage foreclosures where the mortgage is secured by the Housing and Urban Development agency. There are other exceptions that are rare and usually do not concern service members, retirees and their families.

What are the Types of Bankruptcy?

There are two primary types of personal bankruptcy: **Chapter 13 and Chapter 7**. Both types of bankruptcy may get rid of unsecured debts and stop foreclosures, repossessions, garnishments, utility shut-offs, and debt collection activities. Both also provide exemptions that allow you to keep certain assets, although exemption amounts vary.

Chapter 7, known as straight bankruptcy, involves liquidating all non-exempt assets. Exempt property may include cars, work-related tools and basic household furnishings. For most soldiers, all of their property will probably be exempt, and they won't actually have to give up anything at all. Property which is not exempt is sold, and the proceeds of sale are used to pay off creditors as much as possible. After the proceeds of sale are exhausted, any debts still remaining are discharged. You can receive a discharge of your debts under Chapter 7 only once every six years.

Chapter 13 allows you to keep property, such as a mortgaged house or car, that you otherwise might lose. However, you have to have a regular income and limited debt to file for Chapter 13 bankruptcy. In Chapter 13 bankruptcy you file a repayment plan in court showing how you will pay off your debts over the next three to five years. The big benefit to Chapter 13 is that it prevents your creditors from harassing you and allows you to keep property subject to a security interest, as long as you make the payments required under your repayment plan.

Who is Eligible to File for Bankruptcy?

Chapter 7 bankruptcy is available to any person, partnership or corporation that resides or has a domicile, a place of business or property in the United States.

Chapter 13 bankruptcy is available to anyone

- (1) who has regular income,
- (2) whose unsecured debts total less than \$250,000, and
- (3) whose secured debts total less than \$750,000.

The amount of the debt is determined at the time of the filing of the petition. There are a few exceptions to eligibility that usually are not relevant to service members, retirees and their families.

Will I Have to go to Court?

In most bankruptcy cases, you only have to go to a proceeding called the “meeting of creditors” to meet with the bankruptcy trustee and any creditor who chooses to attend. This occurs between 20-50 days after the order of relief is issued by the Bankruptcy Court. Creditors and the trustee use this meeting to question you regarding information in the bankruptcy petition.

How Will Bankruptcy Affect My Credit?

There is no clear answer to this question. If you are already so far behind on your bills that you are contemplating bankruptcy, then your credit is probably pretty bad already, and actually filing for bankruptcy may not make things a lot worse. However, bad debts usually only stay on your record for seven years; bankruptcy stays on your credit report for 10 years, making it difficult to acquire credit, buy a home, get life insurance, or sometimes get a job. Since bankruptcy wipes out your old debts, you are likely to be in a better position to pay new bills and may actually have better credit immediately after the bankruptcy than immediately before the bankruptcy. Bankruptcy has significant consequences, and you should think carefully and seek advice from your legal assistance office before deciding to file for bankruptcy.

Can Bankruptcy Affect My Security Clearance?

Your security clearance can be affected by bankruptcy. Some criteria factored in to security clearance eligibility include “excessive indebtedness, recurring financial difficulties, or unexplained affluence.” Therefore, filing for bankruptcy may prevent you from keeping or obtaining a security clearance. The security section will weigh whether the bankruptcy was caused primarily by an unexpected event, such as medical bills following a serious accident, or by financial irresponsibility. The security section may also consider the recommendations and comments of your chain of command and co-workers. The amount of your unpaid debts, by itself, may jeopardize your clearance, even if you don't file bankruptcy.

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