



FACTS

FOR OLDER CONSUMERS

National Consumer Law Center®

What You Should Know About Bankruptcy

What Is Bankruptcy?

Bankruptcy is a process under federal law designed to help people and businesses get protection from their creditors. An important goal of bankruptcy is to give individuals with debt problems a chance for a fresh financial start. For some elders, bankruptcy does this by eliminating the legal obligation to pay debts. Others gain an opportunity to get current on mortgages and car loans or to pay off debts at a reduced amount. Filing bankruptcy also immediately stops most creditors from seeking to collect debts, at least until things are sorted out in the bankruptcy process.

Things to Think About Before Deciding Whether to File

A decision to file bankruptcy should be made only after determining that bankruptcy is the best way to deal with your financial problems. Other options to deal with unmanageable debt usually should be considered first.

- **Credit Counseling**

When done well, credit counseling can be very helpful for consumers in financial distress. Unfortunately, there are many people who offer counseling and credit repair in order to rip you off. You should be careful to avoid scams and offers of costly debt consolidation plans as a way out of debt. Most of these deals will only make your situation worse.

If you decide to go ahead with bankruptcy, the law requires that you meet with an approved credit counseling agency first to consider your options in credit counseling. 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 will not be able to help much if you’re already too deep in financial trouble.

Many credit counselors, including some of the approved bankruptcy agencies, offer debt management plans (also called DMPs). This is a plan to repay some or all of your debts in which you send the counseling agency a monthly payment that it

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then distributes to your creditors. Debt management plans can be helpful for some seniors. For others, they are a terrible idea. The problem is that counseling agencies may 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.

• Consolidation Loans and Reverse Mortgages

It is almost never a good idea to mortgage your home to pay off credit card and other unsecured debt. By trading in credit card debt for a mortgage loan, you risk the loss of your home if you continue to have financial problems. Refinancing an existing mortgage may make sense, but generally only if you are having difficulty with the current mortgage payment and the new mortgage will provide a lower payment and better terms.

A reverse mortgage lets older homeowners borrow on the equity in their homes, but is different than a traditional mortgage. Unlike a traditional home equity loan, repayment is not required until you sell your home, move out permanently, or die. The amount of money you owe increases over time because you do not make payments. The lender pays you the money you borrow either in a lump sum, in monthly installments, or as a line-of-credit. Reverse mortgage options may be confusing and there are many things to consider before deciding it can help. Before applying for a reverse mortgage, you should get counseling from an impartial housing counselor.

• Protections from Debt Collection Harassment

If your main reason for considering bankruptcy is that you are receiving calls from collectors, you may want to consider whether the collector has the legal right to take any action against you and whether you can take steps to stop the calls. Although constant harassing calls and letters from collection agencies can be annoying and at times intimidating, if you are "judgment proof," you may have nothing to fear. You are "judgment proof" if all of your assets and income are protected by law from a creditor trying to collect on a debt or enforce a court judgment. If explaining your situation doesn't stop collection efforts, the simplest way to stop collection harassment is to write the collector a cease letter. Federal law requires collection agencies to stop their collection efforts after they receive a written request to stop. Sometimes simply being prepared to assert your legal rights can be the best way to deal with debts you can not pay.

Is It True That Changes in the Bankruptcy Law Will Prevent Me From Filing Bankruptcy?

There were many changes made to bankruptcy by a law passed by Congress in 2005. Some news reports had suggested that these changes would prevent many individuals from filing bankruptcy. It is true that the changes have made the process more complicated. But the basic right to file bankruptcy still exists and most of the benefits of bankruptcy remain available for most individuals.

Is Bankruptcy the Right Choice for You?

Bankruptcy can be the right choice if you have no better way to deal with your debts. It may make it possible for you to:

- Eliminate the legal obligation to pay most or all of your debts. This benefit comes from the bankruptcy “discharge” that you get for successfully completing a bankruptcy case.
- Stop almost all creditors from taking any steps against you except through the bankruptcy process. This is provided by the “automatic stay” that goes into effect as soon as you file the necessary paperwork at the beginning of a bankruptcy case. Foreclosures, tax sales, repossessions, utility shut-offs, lawsuits, and other creditor actions will be immediately (but perhaps only temporarily) stopped.
- Catch up on missed payments on home mortgages, property taxes, auto loans and other debts secured by property you wish to keep. Bankruptcy does not, however, automatically eliminate mortgages and other liens on your property without payment.
- Stop debt collection harassment, wage garnishment, and similar creditor actions to collect a debt.
- Lower the monthly payments on some debts, including some secured debts such as car loans.
- Prevent termination of utility service or restore service if it has already been terminated.
- Allow you to challenge the claims of creditors who have committed fraud or who are otherwise trying to collect more than you really owe.

Bankruptcy can not, however, cure every financial problem and it is not 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 co-signed 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. Because of this, you may wish to delay a bankruptcy filing until you are reasonably sure that you will not incur new major debts.

What Different Types of Bankruptcy Cases Should I Consider?

There are four types of bankruptcy cases provided under the law that an individual may file. However, most seniors 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**

Chapter 7 is known as “straight” bankruptcy or “liquidation.” 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.

- **Chapter 13**

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. In a chapter 13 case you file a “plan” showing how you will pay off some of your past-due and current debts over a three to five year period. 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. 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 will need to have enough income in chapter 13 to pay for your necessities and to keep up with the required payments as they come due.

Is My Income Too High to File a Chapter 7?

Most older consumers who are considering bankruptcy should be able to file under chapter 7. However, if your income is above the median family income in your state, you may have to file a chapter 13 case (the national median family income for a family of 4 in 2011 ranged from a low of just over \$53,000 in New Mexico to almost \$103,500 in Maryland). Higher-income seniors must fill out a full set of “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.

What Does It Cost to File for Bankruptcy?

It now costs \$299 to file for bankruptcy under chapter 7 and \$274 to file 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 all at once. 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 2011 are \$16,535 for a single person and \$22,065 for a family of 2), 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.

If you hire an attorney you will also have to pay the attorney's fees you agree to. You may be eligible for free representation through the legal services or volunteer attorney program in your area.

What Must I Do Before Filing Bankruptcy?

You must receive a briefing 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 \$20-\$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 cannot afford the fee, you should ask the agency to provide the counseling free of charge or at a reduced fee.

It is usually a good idea for you to meet with an attorney before you receive the required credit counseling. Unlike a credit counselor, who can not give legal advice, an attorney can provide counseling on whether bankruptcy is the best option. If bankruptcy is not the right answer for you, a good attorney will offer a range of other suggestions. The attorney can also provide you with a list of approved credit counseling agencies, or you can check the website for the United States Trustee Program office at www.usdoj.gov/ust.

Can I Own Anything After Bankruptcy?

Yes! Many people believe they can not own anything for a period of time after filing for bankruptcy. This is not true. You can keep your exempt property and anything you obtain after the bankruptcy is filed. It is important to check the exemptions that are available in the state where you live. (If you moved to your current state from a different state within two years of your bankruptcy filing, you may be required to use the exemptions from the state where you lived just before the two-year period.). In some states, you are given a choice when you file bankruptcy between using either the state exemptions or using the federal bankruptcy exemptions. If your state has “opted” out of the federal bankruptcy exemptions, you will be required to choose exemptions mostly under your state law. However, even in an “opt-out” state, you may use a special federal bankruptcy exemption that protects retirement funds in pension plans and IRAs.

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 come. Most of the time, this meeting will be a short and simple procedure where you are asked a few questions about your bankruptcy forms and your financial situation. In a chapter 13 case, you may have to appear at a hearing when the judge decides whether your plan should be approved. Occasionally, if complications arise, or if you choose to dispute a debt, you may also have to go to court.

What Else Must I Do to Complete My Case?

After your case is filed, you must complete an approved course in personal finances. This course will take approximately two hours to complete. Many of the course providers give you a choice to take the course in-person at a designated location, over the Internet usually by watching a video, or over the telephone. Your attorney can give you a list of organizations that provide approved courses, or you can check the website for the United States Trustee office at www.usdoj.gov/ust/. If you can not afford the fee, you should ask the agency to provide the course free of charge or at a reduced fee. In a chapter 7 case, you should sign up for the course soon after your case is filed. If you file a chapter 13 case, you should ask your attorney when to take the course.

After you have filed all the necessary documents, attended the meeting of creditors, and taken the finance course, your case will be completed and you will receive a document from the court noting that your debts have been discharged. In most chapter 7 cases, this will be sent you approximately three months after the case is filed. The discharge in a chapter 13 case is not sent until the plan is completed, which is usually about 3 to 5 years after the case is filed.

Will Bankruptcy Affect My Credit?

There is no clear answer to this question. Unfortunately, if you are behind on your bills, your credit may already be bad. Bankruptcy will probably not make things any worse. The fact that you’ve filed a bankruptcy can appear on your credit record for ten years from

the date your case was filed. But because bankruptcy wipes out your old debts, you may be in a better position to pay your current bills, and you may be able to get new credit.

If you decide to file bankruptcy, remember that debts discharged in your bankruptcy should be listed on your report as having a zero balance, meaning you do not owe anything on the debt. Debts incorrectly reported as having a balance owed will negatively affect your credit score and make it more difficult or costly to get credit. You should check your credit report after your bankruptcy discharge and file a dispute with credit reporting agencies if this information is not correct.

For More Information

More detailed information on refinancing and other consumer credit issues is contained in *Surviving Debt: A Guide for Consumers*. The handbook is available from the National Consumer Law Center®, 7 Winthrop Square, Boston, MA 02110 (617/542-8010). You can also order NCLC® publications at www.consumerlaw.org.



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