Bankruptcy

If you are like most people, when you borrow money, you have every intention of paying it back. When something unexpected happens, such as a serious illness or loss of job, you may find yourself unable to keep up with your payments. Bankruptcy may be an option available to help you eliminate your debt.

While declaring bankruptcy might seem like the perfect solution, bankruptcy ruins credit, makes it difficult to keep bank accounts and credit cards, can cause the loss of valuable possessions and makes it difficult to get on with the necessities of life, such as buying or renting a home or car, getting insurance or finding a job. In fact, most financial advisors look at bankruptcy as a last resort — one that should only be carried out with the counsel of an experienced bankruptcy attorney — and only when budgeting, credit counseling or other efforts have failed.

If you plan to file for bankruptcy protection, you are required to take a credit counseling class from a government-approved organization within 180 days before you file. You also have to complete a debtor education course before your debts can be discharged. For more information on these courses and to verify if the course is government-approved, please visit the United States Courts website at http://www.uscourts.gov/services-forms/bankruptcy/credit-counseling-and-debtor-education-courses.

Generally, bankruptcies can be divided into two types: liquidation (Chapter 7) and reorganization (Chapter 13). These types are explained below.

Chapter 7 Bankruptcy

Chapter 7 bankruptcy comes under the liquidation category. It's called liquidation because the bankruptcy trustee may take and sell ("liquidate") some of your property to pay back some of your debt. However, you may keep property that is protected (also called "exempt") under state law. Not everyone can file for Chapter 7 bankruptcy. For example, if your disposable income is sufficient to fund a Chapter 13 repayment plan, after subtracting certain allowed expenses and monthly payments for certain debts, you won't be allowed to use Chapter 7 bankruptcy. However, if you do file Chapter 7 it typically lasts three to six months.

In Chapter 7 bankruptcy, some of your property may be sold to pay down your debt. In return, most or all of your unsecured debts (that is, debts for which collateral has not been pledged) will be erased. You get to keep any property that is classified as exempt under the state or federal laws available to you (such as your clothes, car, and household furnishings). Many debtors who file for Chapter 7 bankruptcy are pleased to learn that they can keep some of their personal property.

If you owe money on a secured debt (for example, a car loan for which the car is pledged as a guarantee of payment) you have a choice of allowing the creditor to repossess the property, continuing your payments on the property under the contract (if the lender agrees), or paying the creditor a lump sum amount equal to the current replacement value of the property. Some types of secured debts can be eliminated in Chapter 7 bankruptcy.

Chapter 13 Bankruptcy

There are several types of reorganization bankruptcies, but Chapter 13 is the most common type for consumers. In Chapter 13 bankruptcy you keep all of your property, but must make monthly payments over three to five years to repay all or some of your debt.

In Chapter 13 bankruptcy you must have a reliable source of income that you can use to repay some portion of your debt in order to file for Chapter 13. When you file for Chapter 13 bankruptcy, you must propose a repayment plan that details how you are going to pay back your debts over the next three to five years. The minimum amount you'll have to repay depends on how much you earn, how much you owe, and how much your unsecured creditors would have received if you'd filed for Chapter 7 bankruptcy. Your debts must be within limits set by the federal government. If you have secured debts, Chapter 13 gives you an option to make up missed payments to avoid repossession or foreclosure. You can include these past due amounts in your repayment plan and make them up over time.

Both Chapter 7 and Chapter 13 bankruptcy have many rules, and exceptions to those rules, regarding which debts are covered, who can file, and what property you can and cannot keep. Though bankruptcy can eliminate many kinds of debts, such as credit card debt, medical bills, and unsecured loans, there are many types of debts, including child support and spousal support obligations and most tax debts, that cannot be wiped out in bankruptcy. You may want to consult with an attorney if you have questions regarding the types of bankruptcy and whether it is a good option for you.