Bankruptcy – Is it the right choice?

Texas Legal Services Center

Information Not Legal Advice
This pamphlet is for information only and is not a substitute for the advice of an attorney.

What is a bankruptcy and is it the right choice for me?

Bankruptcy is a kind of court case where a person asks a federal court to discharge (wipe out) debts. If the judge grants the discharge, it is permanent and creditors cannot make any effort to collect the debts.

While every effort has been made to make sure the information in this publication is accurate, it is only general information about bankruptcy. The laws related to bankruptcy are very complicated, particularly when it involves Chapter 13. For answers to specific questions about bankruptcy, you should talk to a lawyer.

What is the difference between a Chapter 7 and a Chapter 13 bankruptcy?

Bankruptcy is a legal way to give a person in financial trouble a "fresh start." There are different kinds of bankruptcy. Most people use either a Chapter 7 or Chapter 13 bankruptcy. Chapter 7 is a liquidation bankruptcy. In a Chapter 7 bankruptcy, the court makes an order saying that certain debts do not have to be paid back. Chapter 13 is a reorganization bankruptcy. It allows a person to make a plan to pay some debts over a period of time. When the payment plan is completed, the remaining debts are discharged.

What should I know about a Chapter 7 bankruptcy?

In a Chapter 7 bankruptcy, the debtor gives up (liquidates) all his or her non-exempt property. The non-exempt property is sold and the money received is divided among the creditors, (the people to whom the debtor owes money).

The remaining debts are discharged. In other words, the court releases the debtor from paying the remaining debts, and creditors cannot try to collect any debt that was discharged by the bankruptcy court.

Many people only have property that is exempt. When that happens, the debtor keeps all his or her property, and the debts are discharged.

What is exempt and non-exempt property?

"Exempt" property are the things that cannot be taken away from the debtor to pay back the money owed. "Non-exempt" property are the things that can be taken away from the debtor to pay back money owed. There are lists saying what things are exempt and what are non-exempt under both federal law and Texas law.

In Texas, a person who files a Chapter 7 bankruptcy can choose to use either the Texas or federal exemptions. Texas and federal property exemptions are different. Before choosing which exemptions to use, a debtor has to compare the property he owns to the federal exemption list and the Texas exemption list to see which is better.

What happens in a bankruptcy case?

First, the debtor has to get credit counseling and then file papers in the federal court asking the court to discharge the debts. The basic steps of a bankruptcy are:

- ***Counseling and Education:*** The debtor must go to an approved credit counseling agency within 180 days before filing for bankruptcy. After the filing, the debtor must also attend approved debtor education within 45 days of the "creditors meeting."
- ***Filing:*** The debtor must file papers with the bankruptcy court. Things that have to be filed with the court:
    - List of creditors (the people or companies you owe money to);
    - Schedule of assets and liabilities (what you owned and what you have to pay);
    - Statement of Income and Expenses;
    - Statement of Intentions (who you can pay and who you cannot);
    - Statement of Financial Affairs (what money you have and what money you do not have);
    - Copies of all pay stubs for the 60 days before you filed for bankruptcy;
    - Statement of your total monthly income;
    - Statement of any changes in your income that you think might happen in the next 12 months;
    - Most recent income tax return.
- If you do not file all the required papers within a certain time, the court can dismiss your case.
- ***Creditors Meeting***: You must attend a meeting which may be attended by representatives of the persons and businesses to whom you owe money. The bankruptcy trustee or a court official presides at the meeting.
- ***Discharge:*** The court orders that the debts be discharged.

This is a very basic explanation of what happens in a bankruptcy case. Each case is different, and many bankruptcy cases are very complicated.

What is the "means" test?

The "means test," is a way to force you to pay some of your debts through Chapter 13, rather than wiping out the debts entirely under Chapter 7. The means test is a way of figuring out if a person should be able to pay back some debts. The means test looks at a debtor's income and property. If the debtor's income and property are too high, the person cannot file a Chapter 7 bankruptcy. If a person whose property and income are too high files for Chapter 7 bankruptcy, the court can dismiss the bankruptcy case or convert it to Chapter 13.

Many Texas seniors qualify for Chapter 7 relief, despite the means test especially if their only source of income is from Social Security. Benefits from the Social Security Administration are *not* included in the means test calculation.

What are non-dischargeable debts?

Some debts cannot be wiped out in bankruptcy. That is, they are non-dischargeable. Tax debts, for example, cannot usually be discharged in bankruptcy. The following is a general list of non-dischargeable debts. This list is not specific to your fact situation, and there are some exceptions. To find out whether an item is dischargeable in a particular case, consult with a lawyer. The following may not be dischargeable:

- Debts for "luxury goods" and services owed to a single creditor totaling more than $500 made within 60 days of filing;
- Cash advances in excess of $750 made within 70 days of filing;
- Debts that require timely request for a court's opinion if a creditor has not been given time to make such a request;
- Debts related to death or injury caused while the debtor was intoxicated;
- Some student loans;
- Debts incurred to pay state and local taxes;
- Debts incurred to pay fines and penalties;
- Unpaid child support or spousal support;
- Homeowner association, condominium, and cooperative fees;
- Fees on prisoners; and
- Pension, profit sharing debts.

What about a Chapter 13?

If the debtor has regular income, it may make sense to think about a bankruptcy under Chapter 13. A bankruptcy under Chapter 13 allows the debtor to make a plan to pay certain debts. If the debtor successfully completes the plan, some unsecured debts can be discharged. Chapter 13 payment plans are typically three to five years long, and creditors cannot try to collect the debt during the plan period. The plan must either pay unsecured claims in full (with interest) or provide that all of the debtor's disposable income will be paid to the plan. Disposable income is income, except child support, minus living expenses. There are rules that govern what income counts and what expenses are deducted to figure disposable income. A bankruptcy trustee oversees the plan.

For more information…

The federal courts and the Federal Trade Commission have useful information about bankruptcy. Go to http://www.uscourts.gov/bankruptcycourts/bankruptcybasics.html and

http://www.consumer.ftc.gov/articles/0224-filing-bankruptcy-what-know.

Texas Law Help has useful information on many areas of the law. Go to *www.texaslawhelp.org*.

Legal Hotline for Texans: (800) 622-2520
Call our attorney-staffed legal hotline. Advice is free for Texans 60 and over or for anyone eligible for Medicare.

This publication was made possible through grants from the State Bar of Texas Real Estate, Probate, & Trust Law Section and the Litigation Section.