

A Chapter 7 Bankruptcy Overview

Copyright 2010 Nolo

How Chapter 7 bankruptcy works.

Chapter 7 bankruptcy is sometimes called "liquidation" bankruptcy -- it cancels your debts, but you might have to let the bankruptcy court liquidate (sell) some of your property for the benefit of your creditors. ("Chapter 7" refers to the chapter of the federal Bankruptcy Code that contains the bankruptcy law.)

Chapter 7 Bankruptcy Costs in Time and Money

The whole Chapter 7 bankruptcy process takes about four to six months, costs \$299 in filing and administrative fees, and commonly requires only one trip to the courthouse.

You must also complete credit counseling with an agency approved by the United States Trustee. (For a list of approved agencies in each state, go to the Trustee's website, www.usdoj.gov/ust, and click "Credit Counseling and Debtor Education.")

Who Can File

You won't be able to use Chapter 7 bankruptcy if you already received a bankruptcy discharge in the last six to eight years (depending which type of bankruptcy you filed) or if, based on your income, expenses, and debt burden, you could feasibly complete a Chapter 13 repayment plan. (For more information on these eligibility requirements, see Chapter 7 Bankruptcy -- Who Can File?)

Bankruptcy Forms

To file for Chapter 7 bankruptcy, you fill out a petition and a number of other forms and file them with the bankruptcy court in your area. Basically, the forms ask you to describe:

- your property
- your current income and monthly living expenses
- your debts
- property you claim the law allows you to keep through the Chapter 7 bankruptcy process (called "exempt property") -- most states let you keep some equity in your home, clothing, household furnishings, Social Security payments you haven't spent, and other necessities such as a car and the tools of your trade.
- property you owned and money you spent during the previous two years, and
- property you sold or gave away during the previous two years.

You'll find step-by-step instructions for filling out all of the required forms in *How to File for Chapter 7 Bankruptcy*, by Stephen Elias, Albin Renauer, and Robin Leonard (Nolo).

Bankruptcy's Magic Wand -- The Automatic Stay

Filing for Chapter 7 bankruptcy puts into effect an "Order for Relief" -- known informally as the "automatic stay." The automatic stay immediately stops most creditors from trying to collect what you owe them. So, at least temporarily, creditors cannot legally grab ("garnish") your wages, empty your bank account, go after your car, house, or other property, or cut off your utility service or welfare benefits. For more information, see *How Bankruptcy Stops Your Creditors: The Automatic Stay*.

Bankruptcy Court's Control Over Your Financial Affairs

By filing for Chapter 7 bankruptcy, you are technically placing the property you own and the debts you owe in the hands of the bankruptcy court. You can't sell or give away any of the property you own when you file, or pay off your pre-filing debts, without the court's consent. However, with a few exceptions, you can do what you wish with property you acquire and income you earn after you file for bankruptcy.

The Bankruptcy Trustee for Chapter 7 Bankruptcy

The court exercises its control through a court-appointed person called a "bankruptcy trustee." The trustee's primary duty is to see that your creditors are paid as much as possible on what you owe them. And the more assets the trustee recovers for creditors, the more the trustee is paid.

The trustee (or the trustee's staff) will examine your papers to make sure they are complete and to look for nonexempt property to sell for the benefit of creditors. The trustee will also look at your financial transactions during the previous year to see if any can be undone to free up assets to distribute to your creditors. In most Chapter 7 bankruptcy cases, the trustee finds nothing of value to sell.

The Creditors Meeting

A week or two after you file, you (and all the creditors you list in your bankruptcy papers) will receive a notice that a "creditors meeting" has been scheduled. The bankruptcy trustee runs the meeting and, after swearing you in, may ask you questions about your bankruptcy and the papers you filed. In the vast majority of Chapter 7 bankruptcies, this is the debtor's only visit to the courthouse.

What Happens to Your Property

If, after the creditors meeting, the trustee determines that you have some nonexempt property, you may be required to either surrender that property or provide the trustee with its equivalent value in cash. If the property isn't worth very much or would be cumbersome for the trustee to sell, the trustee may "abandon" the property -- which means that you get to keep it, even though

it is nonexempt. (For information on which types of property are typically exempt, see *When Chapter 7 Bankruptcy Isn't the Right Choice*. However, which property is exempt varies by state -- you can find complete lists of exempt property for every state in *How to File for Chapter 7 Bankruptcy*, by Stephen Elias, Albin Renauer, and Robin Leonard (Nolo).)

Most property owned by Chapter 7 debtors is either exempt or is essentially worthless for purposes of raising money for the creditors. As a result, few debtors end up having to surrender any property, unless it is collateral for a secured debt (see below).

How Your Secured Debts Are Treated

If you've pledged property as collateral for a loan, the loan is called a secured debt. The most common examples of collateral are houses and automobiles. If you're behind on your payments, the creditor can ask to have the automatic stay lifted in order to repossess or foreclose on the property. However, if you are current on your payments, you can keep the property and keep making payments as before -- unless you have enough equity in the property to justify its sale by the trustee.

If a creditor has recorded a lien against your property because of a debt you haven't paid (for example, because the creditor obtained a court judgment against you), that debt is also secured. You may be able to wipe out the lien in Chapter 7 bankruptcy.

The Chapter 7 Bankruptcy Discharge

At the end of the bankruptcy process, all of your debts are wiped out (discharged) by the court, except:

- debts that automatically survive bankruptcy, such as child support, most tax debts, and student loans, unless the court rules otherwise, and
- debts that the court has declared nondischargeable because the creditor objected (for example, debts incurred by your fraud or malicious acts).

For more information and step-by-step help filing for Chapter 7 bankruptcy, see *How to File for Chapter 7 Bankruptcy*, by Stephen Elias, Albin Renauer, and Robin Leonard (Nolo).