

Oceana's Law for the Layperson

**INDIVIDUAL BANKRUPTCY
AND RESTRUCTURING**

Second Edition

Revised and Updated by

Margaret C. Jasper

Legal Almanac Series

Oceana Publications

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Library of Congress Control Number: 2006922575

ISBN 0-19-532156-1

ISBN 978-0-19-532156-2

Oceana's Legal Almanac Series: Law for the Layperson

ISSN 1075-7376

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Manufactured in the United States of America on acid-free paper.

To My Husband Chris

Your love and support
are my motivation and inspiration

-and-

In memory of my son, Jimmy

ABOUT THE AUTHOR

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- AIDS Law
- The Americans with Disabilities Act
- Animal Rights Law
- The Law of Attachment and Garnishment
- Auto Leasing
- Bankruptcy Law for the Individual Debtor

Individual Bankruptcy and Restructuring
Banks and their Customers
Becoming a Citizen
Buying and Selling Your Home
The Law of Buying and Selling
The Law of Capital Punishment
The Law of Child Custody
Your Rights in a Class Action Suit
Commercial Law
Consumer Rights Law
The Law of Contracts
Co-ops and Condominiums: Your Rights and Obligations As Owner
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The Law of Debt Collection
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Lemon Laws
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Marriage and Divorce
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Motor Vehicle Law
The Law of No-Fault Insurance
Nursing Home Negligence
The Law of Obscenity and Pornography
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Privacy and the Internet: Your Rights and Expectations Under the Law
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The Law of Product Liability
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Religion and the Law
Retirement Planning
The Right to Die
Rights of Single Parents
Law for the Small Business Owner
Small Claims Court
Social Security Law
Special Education Law
The Law of Speech and the First Amendment
Teenagers and Substance Abuse
Trademark Law
Victim's Rights Law
The Law of Violence Against Women
Welfare: Your Rights and the Law
Your Rights Under the Family and Medical Leave Act
You've Been Fired: Your Rights and Remedies
What if it Happened to You: Violent Crimes and Victims' Rights
What if the Product Doesn't Work: Warranties & Guarantees
Workers' Compensation Law
and Your Child's Legal Rights: An Overview.

INTRODUCTION

"[Bankruptcy] gives to the honest but unfortunate debtor . . . a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt." Local Loan v. Hunt, 292 U.S. 234, 244 (1934).

This legal almanac discusses the law of bankruptcy as it relates to the individual. In 2005, individual debtors filed 2,039,214 non-business bankruptcy petitions compared to 874,642 filings ten years earlier in 1995. This figure represents 98.11% of all bankruptcy filings, business and non-business. These statistics demonstrate the growing financial problems facing many Americans today.

Bankruptcy is a legal method under federal law by which an individual may resolve or restructure their financial affairs when they are faced with debt problems. This almanac presents an overview of bankruptcy law and the bankruptcy court system, with a focus on the remedies available to the individual faced with personal indebtedness. The procedural steps the individual debtor must take in order to obtain debt relief and restructure his or her finances are also explored.

This almanac also explains the various documents which must be filed, the automatic stay protection, the exemptions available to the debtor, the difference between dischargeable and non-dischargeable debts, the bankruptcy chapters under which an individual debtor generally files his or her case, and the role of the trustee during the process.

The Appendix provides resource directories, sample forms, applicable statutes, and other pertinent information and data. The Glossary contains definitions of many of the terms used throughout the almanac.

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CHAPTER 1:

OVERVIEW OF BANKRUPTCY LAW

THE ORIGINS OF BANKRUPTCY LAW

The origin of the word “bankruptcy” can be traced back to Italy during the Medieval Period. When a businessman was unable to pay his debts, the practice at that time was to destroy his trading bench. From the term “broken bench” or “banca rotta” comes the word “bankruptcy.” In that period, tradesmen unable to repay their debts were dealt with harshly. Protecting the interests of the creditors was of paramount concern. The primary focus in that period was on recovering the interests of the creditors.

In England, the first official laws concerning bankruptcy were passed in 1542, under Henry VIII. A bankrupt individual was considered a criminal and was subject to criminal punishment. Penalties were severe and ranged from imprisonment to the death penalty.

In the United States, prior to the enactment of the bankruptcy laws, individuals risked being sent to a debtors’ prison if they were unable to pay their debts. The focus was still on protecting the creditor and failure to pay a debt was looked upon as a very serious offense. This mindset began to change in the late 1800s when laws were enacted to assist persons who found themselves in financial trouble.

THE EMERGENCE OF BANKRUPTCY LEGISLATION

Article I, Section 8, of the United States Constitution authorizes Congress to enact “uniform Laws on the subject of Bankruptcies,” however, the early federal bankruptcy laws were temporary responses to bad economic conditions. The first official bankruptcy law was enacted in 1800 in response to land speculation and was repealed in 1803.

In 1841, in response to the panic of 1837, the second bankruptcy law was passed but was soon repealed in 1843. In response to the financial

crises caused by the Civil War, Congress passed another bankruptcy law in 1867, which was subsequently repealed in 1878.

The economic upheaval of the Great Depression led to the enactment of the Bankruptcy Act of 1933 and the Bankruptcy Act of 1934. This legislation culminated with the Chandler Act of 1938, which included substantial provisions for reorganization of businesses.

GOVERNING LAW

In 1978, Congress enacted the “Bankruptcy Code,” which is the uniform federal law that governs all bankruptcy cases. The Bankruptcy Code is codified as Title 11 of the United States Code. The Bankruptcy Code made it easier for both businesses and individuals to file for bankruptcy protection and reorganize their debts.

The primary goal of the federal bankruptcy laws is to give debtors a fresh start by releasing the debtors from personal liability for certain debts. This release is known as a bankruptcy discharge. The discharge prohibits creditors from taking any further action against the debtor to collect on those debts.

The procedural aspects of the bankruptcy process are governed by the Federal Rules of Bankruptcy Procedure (the “Bankruptcy Rules”) and local rules of each bankruptcy court. The Bankruptcy Rules contain a set of official forms for use in bankruptcy cases.

The Bankruptcy Code, Bankruptcy Rules, and local rules set forth the formal legal procedures for dealing with the debt problems of individuals and businesses. A record number of business and individual bankruptcies were filed in the 1980s and early 1990s.

Before filing for bankruptcy, one must research the law and procedure in his or her own jurisdiction. Bankruptcy law was federally enacted, and was intended to be uniform across the country. However, when conflicts arise in a particular case, a decision is made by the bankruptcy court in which the case is pending.

Unless an appeal is taken to the federal level, or the legislature intervenes to establish a uniform ruling, the various local decisions would be the law in that jurisdiction until statutorily changed or overruled at the appellate level.

Therefore, the reader is advised to check the law and practice of their own jurisdiction before filing a bankruptcy petition. Further, if the debtor’s financial situation is particularly complex, it is advisable to consult a lawyer before proceeding.

The Bankruptcy Code has been amended several times since its enactment.

The Bankruptcy Reform Act of 1994

On October 22, 1994, the Bankruptcy Reform Act of 1994 was signed into law. The 1994 Act contained many provisions for both business and consumer bankruptcy, including:

- (i) Provisions to expedite bankruptcy proceedings;
- (ii) Provisions to encourage individual debtors to use Chapter 13 to reschedule their debts rather than use Chapter 7 to liquidate;
- (iii) provisions to aid creditors in recovering claims against bankrupt estates; and
- (iv) the creation of a National Bankruptcy Commission.

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 became effective on October 17, 2005. The Act contains the most comprehensive changes in bankruptcy law in over two decades. This almanac sets forth bankruptcy law and procedures under the amended Bankruptcy Act. Some of the major changes include:

- (i) A provision under which the bankruptcy attorney must make a reasonable inquiry to verify that the information contained in the debtor's petition and schedules is well-grounded in fact. The attorney's signature on the petition serves as certification that the information contained in the schedules is correct;
- (ii) A "means test" for Chapter 7 eligibility, under which a creditor or the trustee can bring a motion to dismiss the debtor's case if it is determined that the debtor's income is greater than the state median income. If the debtor's current monthly income exceeds a certain standard, abuse is presumed and the debtor may be placed in a 5-year repayment plan under Chapter 13.
- (iii) A 5-year plan duration for a Chapter 13 debtor whose income exceeds the state median income.
- (iv) A mandatory credit counseling provision under which a prospective debtor must undergo credit counseling from an approved, non-profit credit counseling agency within the 180 day-period prior to filing. The credit counseling must be provided by a nonprofit budget and credit counseling agency approved by the U.S. trustee or bankruptcy administrator. There is an exception to this requirement in case of emergency. In addition, after filing a bankruptcy case, an in-