

## ADJUSTMENT OF DEBTS UNDER CHAPTER 13

### QUESTIONS AND ANSWERS ABOUT CHAPTER 13 BANKRUPTCIES

#### **What is a Chapter 13 bankruptcy case and how does it work?**

A chapter 13 bankruptcy case is a proceeding under federal law in which the debtor seeks relief under chapter 13 of the Bankruptcy Code. Chapter 13 is the chapter of the Bankruptcy Code which allows a person to repay all or a portion of his or her debts under the supervision and protection of the bankruptcy court. The Bankruptcy Court is the federal law that deals with bankruptcy. A person who files a Chapter 13 is called a debtor. In a Chapter 13 case, the debtor must submit to the court a plan for the repayment of all or a portion of his or her debts. The plan must be approved by the court to become effective. If the court approves the debtor's plan, most creditors will be prohibited from collecting their claims from the debtor. The debtor must make regular payments to a person called the chapter 13 trustee, who collects the money paid by the debtor and disburses it to creditors in the manner called for in the plan. Upon completion of the payments called for in the plan, the debtor is released from liability for the remainder of his or her dischargeable debts.

#### **How does a Chapter 13 differ from a Chapter 7 case?**

The basic difference between a Chapter 7 case and a Chapter 13 case is that in a Chapter 7 case the Debtor's non-exempt property (if any exists) is liquidated to pay as much as possible of the Debtor's debts, while in a Chapter 13 cases a portion of the Debtor's future income is used to pay as much of the Debtor's debts as is feasible under the Debtor's circumstances. As a practical matter, in a Chapter 7 case the Debtor loses all or most of his or her non-exempt property and receives a Chapter 7 discharge, which releases the Debtor from liability for most debts. In a Chapter 13 case, the Debtor usually retains his or her non-exempt property, but must pay off as much of his or her debts as the court deems feasible and receives a Chapter 13 discharge, which is slightly broader than a Chapter 7 discharge and releases the Debtor from liability for a few types of debts that are not dischargeable under Chapter 7. However, a Chapter 13 case normally lasts much longer than a Chapter 7 case and is usually more expensive for the Debtor.

#### **When is a Chapter 13 case preferable to a Chapter 7 case?**

Chapter 13 is usually preferable for a person who – (1) wishes to repay all or most of his or her unsecured debts and has the income with which to do so within a reasonable time, (2) has valuable non-exempt property or has valuable exempt property securing debts, either of which would be lost in a

Chapter 7 case, (3) is not eligible under means testing to maintain a Chapter 7 case, (4) is not eligible for a Chapter 7 discharge, (5) has one or more substantial debts that are dischargeable under Chapter 13 but not under Chapter 7, or (6) has sufficient assets with which to repay most of his or her debts, but needs temporary relief from creditors in order to do so.

### **How does a Chapter 13 case differ from a private debt consolidation service?**

In a Chapter 13 case, the bankruptcy court can provide relief to the debtor that a private debt consolidation service cannot provide. For example, the Court has the authority to prohibit creditors from attaching or foreclosing on the Debtor's property, to force unsecured creditors to accept a Chapter 13 Plan that pays only a portion of their claims, and to discharge a Debtor from unpaid portions of debts. Private debt consolidation services have none of these powers.

### **What is a Chapter 13 discharge?**

It is a Court Order releasing a Debtor from all of his or her dischargeable debts and ordering creditors not to collect them from the Debtor. A debt that is discharged is one that the Debtor is released from and does not have to pay. There are two types of Chapter 13 discharges: (1) a full or successful plan discharge, which is granted to a Debtor who completes all payments called for in the plan, and (2) a partial or unsuccessful Plan discharge, which is granted to a Debtor who is unable to complete the payments called for in the Plan due to circumstances for which the Debtor should not be held accountable. A full Chapter 13 discharge discharges a few more debts than a Chapter 7 discharge, while a partial Chapter 13 discharge is similar to a Chapter 7 discharge.

### **What type of debts are not dischargeable in Chapter 13 cases?**

A full Chapter 13 discharge granted upon the completion of all payments required in the Plan discharges a Debtor from all debts except:

- (1) Debts that were paid outside of the Plan and not covered in the Plan,
- (2) Debts for domestic support obligations, which includes debts for child support and alimony,
- (3) Debts for death or personal injury caused by the Debtor's operation of a motor vehicle, vessel or aircraft while intoxicated,
- (4) Most tax debts,
- (5) Debts for restitution or criminal fines included in a sentence imposed on the Debtor for conviction a crime,

- (6) Debts for fraud, embezzlement larceny,
- (7) Debts for student loans or educational obligations unless a court rules that not discharging the debt would impose an undue hardship on the debtor and his or her dependents,
- (8) Debts for damages caused by willful or malicious conduct by the debtor,
- (9) Installment debts whose last payment is due after the completion of the Plan,
- (10) Debts incurred while the Plan was in effect that were not paid under the Plan
- (11) Debts owed to creditors who did not receive notice of the Chapter 13 case, and
- (12) Long-term debts upon which payments were made under the Plan.

A partial Chapter 13 discharge, which is granted when a Debtor is unable to complete the payments under a Plan due to circumstances for which he or she should not be held accountable, discharges the Debtor from all debts except:

- (1) Secured debts (i.e., debts secured by mortgages or liens),
- (2) Debts that were paid outside of the Plan and not covered in the Plan,
- (3) Installment debts whose last payment is due after the completion of the Plan,
- (4) Debts incurred while the Plan was in effect that were not paid under the Plan,
- (5) Debts owed to creditors who did not receive notice of the Chapter 13 case,
- (6) Debts that are not dischargeable in a Chapter 7 case, and
- (7) Long-term debts upon which payments were made under the Plan.

#### **What debts may be paid under a Chapter 13 Plan?**

Any debts whatsoever, whether they are secured or unsecured. Even debts that are non-dischargeable, such as debts for student loans or child support, may be paid under a Chapter 13 Plan.

#### **Must all debts be paid in full under a Chapter 13 Plan?**

No. While priority debts, such as debts for domestic support obligations and taxes, and fully secured debts must be paid in full under a Chapter 13 Plan, only an amount that the Debtor can reasonably

afford must be paid on most debts. The unpaid balances of most debts that are not paid in full under a Chapter 13 Plan are discharged upon the completion or termination of the Plan.

**How much of the Debtor's income must be paid to the Chapter 13 Trustee under a Chapter 13 Plan?**

Usually all of the disposable income of the Debtor and the Debtor's spouse for a 3 or 5 year period must be paid to the Chapter 13 Trustee. Disposable income is income received by the Debtor and his or her spouse that is not deemed to be necessary for the support of the Debtor and his or her dependents.

**When must the Debtor begin making payments to the Chapter 13 Trustee and how are the payments made?**

The Debtor must begin making payments to the Chapter 13 Trustee within 30 days after the Chapter 13 case is filed with the Court. The payments must be made regularly, usually on a weekly, bi-weekly, or monthly basis. If the Debtor is employed, some Courts require that the payments to be made directly to the Chapter 13 Trustee by the Debtor's employer.

**How long does a Chapter 13 Plan last?**

The required length of a Chapter 13 Plan depends on the Debtor's income. If the Debtor's annual income is less than the median family income for the Debtor's state and family size, the length of the Plan must be 3 years, unless the Debtor can justify a longer period, which may not exceed 5 years. If the Debtor's annual income exceeds the median family income, the length of the Plan must be 5 years unless all secured claims can be paid off in a shorter period. The Debtor's annual income is his or her current monthly income multiplied by 12.

**Is it necessary for all creditors to approve a Chapter 13 Plan?**

No. To become effective, a Chapter 13 Plan must be approved by the Court, not by the creditors. The Court, however, cannot approve a Plan unless each secured creditor is dealt with in the manner as described below. Also, unsecured creditors are permitted to file objections to the Debtor's Plan, and these objections must be ruled on by the Court before it can approve the Debtor's Chapter 13 Plan.

**Who is eligible to file a Chapter 13 case?**

Any individual (i.e., natural person) is eligible to file a Chapter 13 case if he or she – (1) resides in, does business in, or owns property in the United States, (2) has regular income, (3) has unsecured debts of less than \$307,675, (4) has secured debts of less than \$922,975, (5) is not a stockbroker or commodity broker, (6) has not intentionally dismissed another bankruptcy case within the last 180 days, and (7) has received a briefing from an approved credit counseling agency within the last 180 days (unless this requirement is not in effect in the local bankruptcy court). Corporations, partnerships, limited liability companies, and other business entities are not eligible to file a Chapter 13 case.

**May a husband and wife file a joint Chapter 13 case?**

A husband and wife may file a joint Chapter 13 case if each of them meets the requirements, except that only one of them need have regular income and their combined debts must meet the debt limitations.

**When should a husband and wife file a joint Chapter 13 case?**

If both spouses are liable for any significant debts, they should file a joint Chapter 13 case, even if only one of them has income. Also, if both of them have regular income, they should file a joint case.

**May a self-employed person file a Chapter 13 case?**

Yes. A self-employed person meeting the eligibility requirements may file a Chapter 13 case. A Debtor engaged in business may continue to operate the business during his or her Chapter 13 case.

**Will a person lost any property if he or she files a Chapter 13 case?**

Usually not. In a Chapter 13 case, creditors are usually paid out of the Debtor's income and not from the Debtor's property. However, if a Debtor has valuable non-exempt property and has insufficient income to pay enough to creditors to satisfy the Court, some of the Debtor's property may have to be used to pay creditors.

**How does the filing of a Chapter 13 case affect collection proceedings and foreclosures that are filed against the Debtor?**

The filing of a Chapter 13 automatically stay (stops) all lawsuits, attachments, garnishments, foreclosures, and other actions by creditors against the Debtor or the Debtor's property. This stay is called the automatic stay. A few days after the case is filed, the Court will mail a notice to all creditors

advising them of the automatic stay. Certain creditors may be notified sooner, if necessary. Most creditors are prohibited from proceeding against the Debtor during the entire course of the Chapter 13 case. If the Debtor is later granted a Chapter 13 discharge, the creditors will then be prohibited from collecting the discharged debts from the Debtor after the case is closed. If the Debtor has had a prior bankruptcy case dismissed within the past year, he or she may be denied the protection of the automatic stay.

**Is a person's employer notified when he or she files a Chapter 13 case?**

In most cases, yes. Many courts require a Debtor's employer to make payments to the Chapter 13 Trustee on the Debtor's behalf. Also, the Chapter 13 Trustee may contact an employer to verify the Debtor's income. However, if there are compelling reasons for not informing an employer in a particular case, it may be possible to make other arrangements for the required information and payments.

**When does the Debtor have to appear in Court in a Chapter 13 case?**

Most Debtors have to appear in Court at least twice: once for a hearing called the meeting of creditors, and once for a hearing on the confirmation of the Debtor's Chapter 13 Plan. The meeting of creditors is usually held about a month after the case is filed. The confirmation hearing may be held on the same day as the meeting of creditors or at a later date, depending on the scheduling practices in the local court. If difficulties or unusual circumstances arise during the course of a case, additional court appearances may be necessary.

**What is the Debtor temporarily unable to make the Chapter 13 payments?**

If the debtor is temporarily out of work, injured, or otherwise unable to make the payments required under a Chapter 13 Plan, the Plan can usually be modified so as to enable the Debtor to resume the payments when he or she is able to do so. If it appears that the Debtor's inability to make the required payments will continue indefinitely or for an extended period, the case may be dismissed or converted to a Chapter 7 case.

**What if the debtor incurs new debts or needs credit during a Chapter 13 case?**

Only two types of credit obligations or debts incurred after the filing of the case may be included in a Chapter 13 Plan. These are: (1) debts for taxes that become payable while the case is pending, and (2) consumer debts arising after the filing of the case that are for property or services necessary for the Debtor's performance under the Plan and that are approved in advance by the Chapter 13 Trustee. All

other debts or credit obligations incurred after the case is filed must be paid by the Debtor outside the Plan. Some Courts issue an order prohibiting the Debtor from incurring new debts during the case unless they are approved in advance by the Chapter 13 Trustee. Therefore, the approval of the Chapter 13 Trustee should be obtained before incurring credit or new debts after the case has been filed. The incurrence of regular debts, such as debts for telephone service or utilities, do not require the Trustee's approval.

**What should the Debtor do if he or she moves while the case is pending?**

The Debtor should immediately notify the Bankruptcy Court and the Chapter 13 Trustee in writing of the new address. Most communications in a Chapter 13 case are by mail, and if the Debtor fails to receive an order of the Court or a notice from the Chapter 13 Trustee because of an incorrect address, the case may be dismissed. Many courts have change-of-address forms that may be used if the Debtor moves.

**What happens if a Debtor is unable to complete the Chapter 13 payments?**

A Debtor who is unable to complete the Chapter 13 payments has three options: (1) dismiss the Chapter 13 case, (2) convert the Chapter 13 case to a Chapter 7 case, or (3) if the Debtor is unable to complete the payments due to circumstances for which he or she should not be held accountable, close the case and obtain a partial Chapter 13 discharge.