



Bankruptcy – Q&A*

What does filing for bankruptcy mean?

For individuals, the bankruptcy process gives debtors relief from certain debts and can provide the debtor with a fresh start financially. For businesses, the bankruptcy process allows a breathing spell from demands so that the business can reorganize and stay in business or can be dissolved to start a new venture.

What are the different types of bankruptcy proceedings?

There are three general types of bankruptcy proceedings, which are generally referred to by the relevant chapter of the applicable U.S. Bankruptcy Code:

- 1) Chapter 7 is used for liquidations. The trustee collects the debtor's nonexempt assets, converts them to cash and distributes the proceeds to the debtor's creditors. This is used for both individuals and businesses and is most of the time the preferred option for debtors.
- 2) Chapter 11 is used for reorganizations. This proceeding is typically used by a business that wants to continue operating as a business and needs to repay creditors through a plan that is authorized by the bankruptcy court. Chapter 11 has been successfully used by large companies such as Enron and various airlines as well as by closely-held businesses. The main objective of a reorganization is to develop and implement a fair and feasible plan to repay creditors and allow the company to continue operating. It is often used to give the businesses some leverage to renegotiate debts which they cannot pay.
- 3) Chapter 13 provides a method where an individual can repay their debt pursuant to a plan authorized by the court over a period of three to five years. Chapter 13 usually allows a debtor to modify his or her car loan or to "cure" a mortgage default.

What are exempt assets?

The Bankruptcy Code exempts specified property of an individual debtor from bankruptcy proceedings: The Federal exemption allows up to \$18,450 in real or personal property that is used as a residence. A motor vehicle is exempted up to \$2,950. You are allowed \$9,850 in household furnishings, goods, books and animals. In addition, unmaturred life insurance, IRAs, 401(k), company pension plans, social security, veterans and disability benefits are exempted as well.



What does the discharge of debts mean?

In a liquidation after the assets have been converted to cash the creditors will be paid in an order specified by the Bankruptcy Code. The claims that are then remaining are discharged meaning that the debtor is relieved of personal liability for the debt. This means that any judgment obtained at any time with respect to that debt is void and works an injunction against commencing or continuing any action to recover that debt. However, certain debts are not dischargeable and the debtor will remain personally liable.

Are there any debts that cannot be discharged?

Yes, taxes for which a return has not been filed or the return was filed late cannot be discharged. Debts that are not listed or scheduled properly in the filing may not be discharged. Domestic support obligations, debts for willful and malicious injury, fines and penalties, student loans and drunken driving debts are not dischargeable as well.

Am I going to lose my home during bankruptcy?

It depends on a variety of factors such as the state where you live, whether it is your primary residence or vacation home and the time you have owned the house. Certain states allow you to keep your home or have limits on the amount of equity you have in your home. This is called “homestead exemption”. In Virginia, you are exempt up to \$5,000 and \$500 per dependent. Maryland and the District of Columbia don’t have any homestead exemptions. Florida and Texas had, until very recently, an unlimited homestead exemption but Congress passed a cap of \$125,000 if the property was acquired within the previous 1215 days. However, there are higher limits for properties jointly owned by bankruptcy debtors. Special rules apply for states where homes can be owned as a tenancy by the entirety such Virginia, Maryland and the District of Colombia.

What effect did the new bankruptcy law have on individuals filing bankruptcy?

The new bankruptcy law instituted a “means test” for individuals with primarily consumer debt whose combined family income is larger than the state median. This means that individuals with higher income may have to restructure their debt instead of having it discharged.

Who can file for bankruptcy?

An individual or business cannot file bankruptcy unless they are connected with the United States. For individuals this is based on residency and domicile. For businesses, this is based on the place of business and the location of assets.



What do I have to do to initiate bankruptcy proceedings?

Most of the time, you will file your bankruptcy petition through your lawyer with the competent bankruptcy court. Interestingly, you do not need to be insolvent to do so. The petition will include a list of all creditors, a list of all property the debtor owns and a list of exempt property.

Can a third party initiate bankruptcy proceedings against me?

Yes, this is called an involuntary bankruptcy petition. Certain creditors can file such a petition under Chapter 7 and Chapter 11 bankruptcy proceedings.

I am a creditor, how much would I recover in bankruptcy proceedings?

It depends whether you have a secured or unsecured claim. There is a priority of claims in bankruptcy law and secured creditors are first in line followed by creditors allowed, unsecured claims.

When do I have a secured claim?

You have a secured claim if you have a lien on the property of the debtor. However, your claim is only secured insofar as your claim and the value of the secured asset are the same. This means that if you have a claim that is worth \$100,000 and the secured interest in the property is valued at \$50,000, you only have a secured claim in the amount of \$50,000.

How long does the bankruptcy proceeding take?

The time from filing to discharge in a Chapter 7 filing is a couple months. A Chapter 13 filing typically takes about 36-60 months to complete. A Chapter 11 filing is more fact specific and may take up to a few years to complete.

How will filing for bankruptcy affect my ability to obtain loans later on?

There will be a negative effect on your credit score but the effect will not be permanent. Nothing affects a debtors credit score more than defaulting on outstanding payments. Chapter 7 and 11 bankruptcy filings remain on your credit report for 10 years. Chapter 13 bankruptcy filings remain on your credit card report for 7 years. There are various ways to rebuild your credit during that time to ease the effect of the bankruptcy on your ability to obtain credit. Individual debtors are usually able to rebuild their credit score within two years.

What are the costs of filing a bankruptcy petition?

The bankruptcy filing fees are \$299 for Chapter 7, \$1,039 for Chapter 11 and \$274 for Chapter 13. Lawyers will often charge a flat fee for their services.



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