

***SOME INFORMATION ABOUT  
BANKRUPTCIES FOR INDIVIDUALS***



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## BANKRUPTCIES FOR INDIVIDUALS

The following information is meant to be a general discussion of consumer bankruptcy law in the two most common bankruptcy chapters filed, Chapter 7 and Chapter 13. Your particular fact situation may require the careful analysis of a bankruptcy attorney because, for every rule of law, there is always an exception. If you feel that you may have a financial situation that requires review by a bankruptcy professional please be aware that most bankruptcy attorneys, including my office, provide a free initial consultation. At the end of the consultation the attorney can recommend a course of action which may or may not include filing a bankruptcy case. Please do not hesitate to consult with a professional before you act. It costs nothing to be fully informed.

### MYTH

The biggest myth regarding bankruptcy is that financially irresponsible people are the majority of people who file bankruptcy. Nothing could be further from the truth. Most professionals who work with the bankruptcy courts will tell you that financially irresponsible people only represent a small fraction of people who file bankruptcy.

The overwhelming numbers of people file because of a catastrophic economic disruption in their lives that is completely and totally beyond their control. Among the causes are the collapse of a business, the loss of a job, illness, divorce and disability. The current economic crisis has put a number of people under financial stress who would have never dreamed of having money problems just three years ago. Bankruptcy attorneys hear people telling them day after day, "I never thought I would be sitting here."

Your financial situation must be dealt with objectively. It is a money problem. Do not let it be a health problem. Bankruptcy law was specifically set out as a power reserved for Congress in the United States Constitution. It is designed to give financially distressed people a "fresh start" by eliminating debt that would have prevented them from being productive in the future.

### COMMON BANKRUPTCY EVENTS

With the filing of a bankruptcy there are several things that happen in every case:

1. **The Automatic Stay:** There is an injunction put into place by the bankruptcy court that keeps creditors from contacting or otherwise attempting to collect debts. It is called the automatic stay. A creditor is prohibited from contacting you unless the creditor gets permission from the court. It protects you from harassment while going through the bankruptcy process.

2. **The Bankruptcy Discharge:** Most debts are forgiven by operation of law at the end of the case. That is called the bankruptcy "discharge." It is also referred to under the Code as a "fresh start." There are a wide variety of debts forgiven such as credit card debts, final judgments, medical bills, personal guarantees on business debts, and in some circumstances even income taxes. However, there are certain debts that may not be discharged or forgiven, such as child support, student loans, fraud, criminal fines, and income taxes less than three years old (some income taxes are dischargeable).

3. **The Bankruptcy Trustee:** A bankruptcy Trustee is appointed to oversee the case in all Chapter 7 and Chapter 13 cases. A bankruptcy Trustee is not a Judge and is usually an accountant or lawyer appointed by the Department of Justice to oversee the bankruptcy process and to perform a designated job depending upon the chapter filed. A meeting with the Trustee (often called a 341 meeting or meeting of creditors) occurs within twenty to forty days after the case is filed. It is an informal hearing

conducted under oath which is held in a conference room, not a courtroom. You appear with your legal representative to answer a brief set of questions about debts and assets. In well over ninety percent of cases you never see the inside of a courtroom.

4. **Bankruptcy Credit Counseling:** Among the amendments to the Bankruptcy Code passed by Congress in 2005 is a requirement for individuals to take two credit counseling courses to complete the bankruptcy process. One course is taken before you file the case and the other one after the case is filed. These courses are usually taken over the internet, but may be taken over the telephone or in person. You are provided a certificate at the completion of each course. The certificates must be filed with the court in order for you to receive a bankruptcy discharge.

## **CHAPTER 7 BANKRUPTCIES**

The most common case filed, by far, is Chapter 7. The theory behind Chapter 7 is that you are allowed to keep certain assets (called “exempt property”). The balance of your assets is surrendered to a Chapter 7 Trustee who sells and liquidates them for the benefit of creditors. In exchange, you receive a discharge of your debts. The reality is that most people, who file Chapter 7, because of the way the laws are written, keep most, if not all, of their assets.

The amount and kind of assets you are allowed to keep depends upon the jurisdiction in which you are filing and the length of time you have lived in that jurisdiction. While bankruptcy law is federal and you file bankruptcy cases in federal court, when Congress passed the Bankruptcy Code, it allowed each state to decide whether to use the federal enumerated statutes for exempt property (assets) or to use its own state law. Florida uses its state law. However, when Congress amended the Code in 2005, it imposed additional time restrictions on residency to determine which state’s exemptions you must use or if the Federal exemptions will apply. Your individual fact situation must be reviewed by a bankruptcy professional to determine what restrictions may apply to your case.

Not everyone can file Chapter 7. There are limitations. When Congress amended the Code in 2005, the new law imposed a “means test” or income test to restrict certain individuals from filing Chapter 7. If your gross income is greater than the median income in the state of Florida for your family size, the means test must be calculated to see if any excess income exists after federally prescribed deductions are subtracted. If you fail the means test you are not allowed to file a Chapter 7. There is one exception to the means test where your non-consumer debts (usually business debts or taxes) are greater than your consumer debts. Only under that limited circumstance will the amount of your income not prohibit a Chapter 7 case from being filed.

The advantage of Chapter 7 is that it is over and finished within a short period of time. After a discharge is issued you begin a new financial life free of most debts. A bankruptcy does not generally ruin your credit history. Usually a person has a tarnished history before filing and the bankruptcy discharge actually helps you rebuild your credit.

## **CHAPTER 13 BANKRUPTCIES**

Chapter 13 is available for people who either cannot file Chapter 7 or have special circumstances where Chapter 13 can be used to their great advantage. Chapter 13 is a financial reorganization for people with regular income. A monthly payment is made to a Chapter 13 Trustee who then disburses the funds to creditors in accordance with a Plan of Reorganization filed and approved by the court. The Plan can run from thirty-six to sixty months. One of the misconceptions of Chapter 13 is the belief that you must pay one hundred percent of all debts owed. In most Chapter 13 cases only a fraction of unsecured debts (creditors without liens such as credit cards) are paid over the life of the Plan.

There are three common Chapter 13 fact circumstances. These are set out below.

### *Mortgages*

Chapter 13 has traditionally been used to stop foreclosures and reinstate mortgages by allowing you to catch up missed payments over time. Today it is used in several ways to save family homes. While Congress eliminated the ability of bankruptcy courts to modify mortgages by court order, the bankruptcy court in Orlando has instituted a mediation program used in coordination with HAMP (Home Affordable Modification Program) to great success. A very high percentage of mediations result in successful mortgage modifications in Chapter 13 as contrasted with the otherwise low percentage of success outside of Chapter 13. Results are varied, but have included mortgage principal reductions, lowered and fixed payments, lowered interest rates and a shortening of the overall length of the mortgage loan period. The success rate has been substantially higher than in regular state foreclosure cases.

In addition, second mortgage liens may be stripped off homes under certain circumstances. Where the house is worth less than what is owed on the first mortgage, the second mortgage can be removed completely. Example: The home has been appraised at \$100,000. The first mortgage has a balance of \$110,000. The second mortgage has a balance owed of \$50,000. The second mortgage of \$50,000 can be stripped off. The removal of the second mortgage and the monthly payment associated with it could result in making the home more affordable and therefore allowing you to keep your home.

### *Taxes*

Income taxes are discharged or eliminated in bankruptcy if: 1) they are due and owing more than three years prior to filing the bankruptcy; 2) the tax return is filed by the taxpayer more than two years prior to the bankruptcy being filed; 3) the taxes have been assessed by the IRS more than 240 days prior to the bankruptcy being filed; and 4) the taxpayer has not been engaged in defrauding the IRS. There are other factors that can also prevent the income taxes from being discharged so you are advised to consult with a tax professional prior to filing. However, those taxes that are less than three years old or otherwise not dischargeable, may be paid without further accumulation of interest and penalties over the life of a Chapter 13 Plan. The protection of the automatic stay coupled with the freezing of the penalties and interest gives you an easy payment plan without the possibility of levy or seizure.

### *Benefits of Chapter 13 for Excess and Unprotected Assets*

The Bankruptcy Code and state law allows you to keep a certain amount of “exempt property.” But, what if you have property that is not protected and you do not have the ability to pay the Chapter 7 Trustee the sum necessary to keep the property within the time period demanded by the Trustee? You can file a Chapter 13 and pay the value of that non-exempt property to unsecured creditors over the life of the Plan. Example: After using all statutes and federal laws, you still have assets valued at \$10,000 which are not considered “exempt property.” Under a Chapter 13 Plan you are allowed to pay the unsecured creditors \$10,000 stretched over time (36 to 60 months) rather than having to pay that same amount to a Chapter 7 Trustee within a short period of filing a Chapter 7 case.

Not everyone can file a Chapter 13 case. As with Chapter 7 certain restrictions apply. Who is eligible to file a Chapter 13 is restricted by the amount of debt you owe for secured and unsecured debts.

## **MORE INFORMATION REGARDING BANKRUPTCY**

More information about the various Bankruptcy Chapters can be found at our website at: [www.jamesmonroepa.com](http://www.jamesmonroepa.com).

James H. Monroe, P.A. has also published bankruptcy articles which are posted at our bankruptcy blog site at [www.bankruptcylawyersfl.com](http://www.bankruptcylawyersfl.com).

The United States Bankruptcy Court, Middle District of Florida has also made available general information and some bankruptcy basics at its website: <http://www.flmb.uscourts.gov>.

At that website the Court has posted videos that give general information about the bankruptcy process. The Bankruptcy Court has also posted an overall general guide to bankruptcy law which can be downloaded at this website at:

<http://www.flmb.uscourts.gov/consumerdebtor/documents/bankruptcybasics.pdf>.

This seventy-eight page guide is an excellent overview of consumer bankruptcy law which will answer a number of questions not covered by this material.

## **ABOUT THE ATTORNEYS WHO WORK AT JAMES H. MONROE, P.A.**

**James H. Monroe** has practiced bankruptcy law for over thirty years. He graduated from Cumberland School of Law of Samford University in 1980. He has twice served as chairman of the Orange County Bar Bankruptcy Law Committee. The Orange County Bar Association awarded him Outstanding Committee Chair 1993 - 1994. He has also served nine years on the Board of Directors of the Central Florida Bankruptcy Law Association. He has been a frequent speaker on bankruptcy law at national, regional, and local seminars. He has a dual certification in Consumer and Business Bankruptcy Law with the American Board of Certification.

**Cynthia E. Lewis** practices bankruptcy law representing Debtors, Creditors and Trustees. This diversification of practice provides for a unique perspective in representation. She graduated from Florida A&M University, College of Law in Orlando in 2007 and is a member of the Florida Bar, Orange County Bar, American Bar Association and American Bankruptcy Institute. She is also Certified Public Accountant.

## **HOW TO CONTACT US**

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