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The New Bankruptcy Law: Changes to Chapter 7 and 13

Chapter 7 bankruptcy may be harder to file under the new law.

The latest changes to bankruptcy law may be making it harder for some people to file bankruptcy. And a few filers with higher incomes are no longer allowed to use Chapter 7 bankruptcy, but will instead have to repay at least some of their debt under Chapter 13. All debtors now have to get credit counseling before they can file a bankruptcy case -- and additional counseling on budgeting and debt management before their debts can be wiped out. And, because the law imposes new requirements on lawyers, it is sometimes tougher to find an attorney to represent you in a bankruptcy case.

Here are some of the most important changes.

Restricted Eligibility for Chapter 7 Bankruptcy

Under the old rules, most filers could choose the type of bankruptcy that seemed best for them -- and most chose Chapter 7 bankruptcy (liquidation) over Chapter 13 bankruptcy (repayment). The new law prohibits some filers with higher incomes from using Chapter 7 bankruptcy.

How High is Your Income?

Under the new rules, the first step in figuring out whether you can file for Chapter 7 bankruptcy is to measure your "current monthly income" against the median income for a household of your size in your state. If your income is less than or equal to the median, you can file for Chapter 7 bankruptcy. If it is more than the median, however, you must pass "the means test" -- another requirement of the new law -- in order to file for Chapter 7.

The Means Test

The purpose of the means test is to figure out whether you have enough disposable income, after subtracting certain allowed expenses and required debt payments, to make payments on a Chapter 13 plan. To find out whether you pass the means test, you subtract certain allowed expenses and debt payments from your current monthly income. If the income that's left over after these calculations is below a certain amount, you can file for Chapter 7.

If you're looking for an easy way to determine your eligibility under the means test, there is a means test calculator at <http://www.legalconsumer.com/bankruptcy/nolo>. Once



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you enter your zip code, the calculator uses the applicable income and expense standards for your state, county, and region to determine your eligibility.

Counseling Requirements

Before you can file for bankruptcy under either Chapter 7 or Chapter 13, you must complete credit counseling with an agency approved by the United States Trustee's office. (To find an approved agency in your area, go to the Trustee's website, www.usdoj.gov/ust, and click "Credit Counseling and Debtor Education".) The purpose of this counseling is to give you an idea of whether you really need to file for bankruptcy or whether an informal repayment plan would get you back on your economic feet.

Counseling is required even if it's obvious that a repayment plan isn't feasible or you are facing debts that you find unfair and don't want to pay. You are required only to participate, not to go along with any repayment plan the agency proposes. However, if the agency does come up with a repayment plan, you will have to submit it to the court, along with a certificate showing that you completed the counseling, before you can file for bankruptcy.

Toward the end of your bankruptcy case, you'll have to attend another counseling session, this time to learn personal financial management. Only after you submit proof to the court that you fulfilled this requirement can you get a bankruptcy discharge wiping out your debts. (The website above also lists approved debt counselors.)

Lawyers May Be Harder to Find -- and More Expensive

As you can see, the new law adds some complicated requirements to the field of bankruptcy. This makes it more expensive -- and time-consuming -- for lawyers to represent clients in bankruptcy cases, which means attorney fees have gone up.

The new law also imposes some additional requirements on lawyers, chief among them that the lawyer must personally vouch for the accuracy of all of the information their clients provide them. This means attorneys have to spend more time on bankruptcy cases, and charge their clients accordingly. This combination of new requirements have driven some bankruptcy lawyers out of the field altogether.

Some Chapter 13 Filers Will Have to Live on Less

Under the old rules, people who filed under Chapter 13 had to devote all of their disposable income -- what they had left after paying their actual living expenses -- to their repayment plan. The new law added a wrinkle to this equation: Although Chapter 13 filers still have to hand over all of their disposable income, they have to calculate their disposable income using *allowed* expense amounts dictated by the IRS -- not their



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actual expenses -- if their income is higher than the median in their state. And these allowed expense amounts must be subtracted not from the filer's actual earnings each month, but from the filer's average income during the six months before filing.

Other Changes

There are other changes that can affect bankruptcy filers negatively, including how property is valued (at replacement cost instead of auction value) -- this means more debtors are at risk of having their property taken and sold by the trustee -- and how long a filer must live in a state to use that state's exemption laws (this can make a big difference in the amount of property a bankruptcy filer gets to keep).

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