

The Truth About Bankruptcy

This is the “end of the line” for the debtor who is drowning in debts. Bankruptcy is the ultimate trump card. A declaration of bankruptcy forces all commercial creditors to cease and desist from attempting to collect the debts owed them; it stops wage garnishment, reverses judgments, and generally wipes out the debts, depending on which form of bankruptcy is declared.

Frankly, for some people, bankruptcy is the only realistic option. If you owe \$50,000 in debts, and you’ll never earn more than \$1,000 per month, then you’re broke! The sooner you face the music and wipe out the debts, the sooner you’ll have a fresh start. Judging by the record number of bankruptcy filings during the past few years, this is a very popular option among consumers. In fact, so many people have filed personal bankruptcy lately—nearly 1.5 million in 2001 alone—that in 2003 Congress passed legislation that will make it tougher to take this option.

There are two forms of personal bankruptcy: Chapter 7, usually called “straight bankruptcy,” and Chapter 13, usually called “consolidation bankruptcy” or “the wage-earner’s plan.” The Chapter 13 approach is typically a very bad deal, because you end up paying back most of the debts over a three to five year period anyway, plus you have the bankruptcy on your credit history for ten years. There are certain unique financial circumstances that might point a person toward a Chapter 13 type of bankruptcy, but the majority of people file the Chapter 7 bankruptcy.

Basically, the way it works is that certain personal property is treated as “exempt,” meaning your creditors cannot touch that property in attempting to recover the money you owe them. An automobile, a certain amount of home equity, personal effects like clothing, and some other assets, are usually considered exempt, although the exact details vary from state to state. Any property that is not exempt is liquidated and distributed to the creditors under the supervision of the court. Since most people entering bankruptcy have only exempt property anyway, there’s usually nothing left to distribute, so the creditors typically get nothing.

Unfortunately, it’s too easy to file bankruptcy in this country. Many people mistakenly view it as a free lunch. There are HIDDEN COSTS associated with bankruptcy that make it a very bad solution for most people. (The cost of filing bankruptcy itself is minimal. Depending on what state you live in, and depending on how much your attorney charges to perform the service, you can expect to pay anywhere from \$300 on up to \$2,500 for the whole process.)