

New bankruptcy law makes Chapter 13 tougher for many people

If you're thinking of filing for bankruptcy protection (or are worrying that some people or businesses who owe you money are), the rules have just changed and the changes are huge. Congress passed a comprehensive bankruptcy reform law in April after years of partisan wrangling. The new law is a complete overhaul of the personal bankruptcy rules. More people will be repaying creditors instead of erasing their debts. The last chance to qualify under the old law ends on October 17, 2005.

Concerns about abuse

The new law is the *Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*. Its long name indicates what Congress set out to do. A majority in Congress was convinced, rightly or wrongly, that Americans were abusing the bankruptcy rules and the new law aims to prevent abuse.

According to supporters, the old rules were too loose. Bankruptcy is intended to give people a "fresh start." Instead of using bankruptcy protection to get one "fresh start," people were filing multiple bankruptcies.

For many years, banks and credit card companies lobbied hard to tighten the rules, especially under Chapter 7, which allows people to liquidate their debts. They wanted, and they got, a "means test" to limit Chapter 7 bankruptcy and move more people into Chapter 13. Debtors in Chapter 13 are required to repay their creditors.

Opponents claim that the new means test is too rigid and is contrary to the "fresh start" of bankruptcy. Regardless of the philosophical differences, the means test is now law and just about everyone, with some exceptions, will have to face it.

Means test

The means test is complex. The needs-based test requires an individual's assets and income to be considered when deciding if the person is abusing the system by seeking Chapter 7 liquidation, instead of repaying debts under a Chapter 13 repayment plan. Bankruptcy judges currently make that decision at their discretion, and debtors are not required to prove insolvency to wipe out most debts.

Personal debts and taxes

More debts are not dischargeable under the new law. This means you remain liable for them just as if you had never filed for bankruptcy. Luxury items and cash advances just before filing are two types of debts that are not dischargeable.

The IRS will almost always get what it is owed. Most unpaid taxes take priority over other types of debts and the new law strengthens these priority rules. The new law also treats taxes consistently under Chapter 7 and Chapter 13.

More requirements

The new law also requires bankrupt individuals to seek credit counseling. Within 180 days of filing, debtors will have to show that they received credit counseling and set up a repayment plan.

Debtors also will have to give a copy of their federal tax return to any creditor that asks and make sure they file returns with the IRS. If returns aren't filed, the bankruptcy case could be dismissed.

Consumer protections

Some important savings accounts are protected from creditors under the new law. Creditors cannot reach your IRA up to \$1 million. Educational IRAs and 529 plans have limited protection.

Oversight

The new law also imposes some tough requirements on attorneys, accountants and others who advise people about bankruptcy. They have to inform clients about alternatives to bankruptcy and adhere to many new regulations.

Rush to file

Many experts are predicting a flood of bankruptcy filings in the coming months. The new bankruptcy law, although signed into law on April 20, doesn't take effect until October 17, 2005. Until then, the old law, without the means test, applies.

If you're thinking about bankruptcy, or are concerned about giving credit to someone or some business that might declare bankruptcy, give our office a call. Bankruptcy has many ramifications. On the one hand, it gives many people a chance to start over but, on the other hand, there is a price. The ability of the bankrupt to get credit or buy a home may be impaired. The new law adds another layer of complexity to an already complicated process. Our office can help you get a handle on how the new rules affect you or your business and explore alternatives.