



Region Legal Service Office Hawaii
Legal Assistance Department
850 Willamette Street
Pearl Harbor, HI 96860

Preventative Law Series

Bankruptcy

Bankruptcy allows a debtor who is unable or unwilling to pay his or her creditors to resolve debts through the liquidation and division of assets among creditors, or in some cases through the repayment of the debt at a reduced rate over a specified period of time.

The purpose of bankruptcy is to relieve the debtor of the burden of his or her financial obligations while treating the creditors with some measure of equality. Federal bankruptcy law emphasizes the equal treatment of those within a each class of creditors.

Bankruptcy law is contained in Title 11 of the United States Code (Bankruptcy Code). States may not regulate bankruptcy, though they may pass laws that govern other aspects of the debtor-creditor relationship, such as what property is *exempt* from bankruptcy actions. There is a two-year residency requirement in advance of the filing, or reversion to a prior state of residency, to determine which state exemptions may apply.

Bankruptcy proceedings are supervised by and litigated in the United States Bankruptcy Courts. These courts are a part of the District Courts of The United States. There are two basic types of Bankruptcy proceedings. A filing under **Chapter 7** is called liquidation. It is the most common type of bankruptcy proceeding. Liquidation involves the appointment of a trustee who collects the non-exempt property of the debtor, sells it and distributes the proceeds to the creditors. Bankruptcy proceedings under **Chapter 11** involves the rehabilitation of the debtor to allow him or her to use future earnings to pay off creditors.

A bankruptcy proceeding may be entered into either voluntarily by a debtor or initiated by creditors. After a bankruptcy proceeding is filed, creditors, for the most part, may not seek to collect their debts outside of the proceeding. Usually after the filing for bankruptcy protection, collection actions are stayed and such stays are often automatic. The debtor is not allowed to transfer property that has been declared part of the estate subject to proceedings. A trustee is appointed to supervise the assets of the debtor. Furthermore, certain pre-proceeding transfers of property, secured interests, and liens may be delayed or invalidated.

As of October 17, 2005, credit counseling from a government approved organization within six months before the filing for bankruptcy is required. The U.S. Trustee Program keeps the list of government-approved credit counseling organizations at www.usdoj.gov/ust .

The Federal Trade also has information on credit counseling requirements and how to choose a credit counselor. See <http://www.ftc.gov/bcp/menus/consumer/credit/debt.shtm> or visit your local Naval Legal Service Office for more information.