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Chapter 13 Bankruptcy and What it Means

Many home owners these days face the possibility of foreclosure due to the sluggish economy. What’s worse is that their mortgages may be underwater i.e. the value of the mortgage exceeds the market selling price of the home. When this happens, selling your home does not absolve you from all your debts to the bank. What can you do to avoid foreclosure?

You can file for bankruptcy. Although there is no guarantee that a bankruptcy filing will save your home from foreclosure, but it remains a viable option.

Most people will file for a Chapter 13 bankruptcy, named such after the section of the bankruptcy code it is derived from. Chapter 13 bankruptcy is a scheduled payment plan ordered by the bankruptcy court for you to clear off your debts over a period of up to 5 years. For it to work, you must have a regular source of income.

One good thing about filing for Chapter 13 bankruptcy is that once it is affected, the court grants you an automatic stay on all collection efforts on you. This stops the phone calls, collection letters and foreclosures, giving you time to craft out your proposed Chapter 13 repayment plan with your bankruptcy attorney.

Besides your mortgage, you would probably have other unsecured debts also, such as credit card debts, medical bills etc. Under a Chapter 13 bankruptcy, you will also pay some portion of these unsecured debts as a Chapter 13 filing permits you to discharge some of that unsecured debt.

How much your unsecured debts can be discharged depends on a few factors like how much you presently earn, the size of your mortgage and your mortgage arrears. Ask you bankruptcy attorney to help you calculate your amount of discharge. The amount discharged will release some money to help you in making your mortgage payments under Chapter 13.

Here's another welcomed advantage of a Chapter 13 bankruptcy – you tend to be deemed more credit-worthy after filing it. The reason is that credit companies will be more willing to grant you credit after you have freed up some of your funds than when you were laden with debts. Some debtors are pleasantly surprised to find credit card offers given to them even before they exit Chapter 13.

Obviously, filing Chapter 13 bankruptcy will affect your credit score, but if you do it right, the impact may not be as devastating as you expect. You should start with a reasonable amount, carefully limit your debt and slowly rebuild your credit. By the time you complete your Chapter 13 repayments, your credit score might be better than when you entered Chapter 13.