

Bankruptcy Basics

Lesson Author

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Standards and Benchmarks (see page 29)

Lesson Description

Students learn that bankruptcy is a federal court proceeding designed to help individuals address debt problems and to provide fair treatment to creditors. They learn the six different types of bankruptcy; however, the lesson focuses on the two types of bankruptcies used mostly by consumers: Chapter 7 and Chapter 13. They analyze bankruptcy terms and learn the similarities and differences between Chapter 7 and Chapter 13 procedures. They also participate in an activity that requires them to work collaboratively to match a bankruptcy step with its correct description. As an assessment, they review scenarios and suggest the best bankruptcy option.

This lesson assumes that students are familiar with credit, uses of credit, types of credit, and basic credit terminology.

Grade Level

9-12

Concepts

Asset	Creditor	Exempt property	Repossession
Automatic stay	Debtor	Foreclosure	Secured debt
Bankruptcy	Debtor attorney	Liquidation	Unsecured debt
Bankruptcy trustee	Debts (liabilities)	Means test	Wage garnishment
Budget	Discharge	Nondischargeable debt	
Chapter 7	Dischargeable debt	Nonexempt property	
Chapter 13	Equity	Petition	

Compelling Question

How are individuals and businesses affected by bankruptcy?

Objectives

Students will

- describe the two main types of bankruptcy most commonly used by consumers: Chapter 7 and Chapter 13;
 - define the dual purpose of bankruptcy;
 - describe and distinguish the differences between dischargeable and nondischargeable debt;
 - describe and distinguish the differences between Chapter 7 and Chapter 13;
 - state and describe the common causes of bankruptcy;
 - describe consequences of bankruptcy; and
 - analyze scenarios to determine which type of bankruptcy is appropriate.
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Materials

- “Bankruptcy Basics” PowerPoint slides; https://www.stlouisfed.org/~media/Education/Lessons/powerpoint/bankruptcy_basics.pptx
 - Handout 1, one copy for each student and one copy for the teacher to use as a visual
 - Handouts 2 and 3, one copy of each for each student
 - Handouts 2 and 3 Answer Keys for the teacher
 - Handouts 4 and 5, one copy of each cut into cards
 - Handouts 4 and 5 Answer Keys for the teacher
 - Handout 6, one copy for each student
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Time Required

90-120 minutes

Procedure

1. Display Slide 1. Begin the lesson by discussing the following:
 - What is **bankruptcy**? (*Answers will vary, but common responses may include not having money to pay your bills, losing your home or other possessions, or being financially unstable.*)
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2. Display Slide 2. Explain that bankruptcy is a legal process declaring that a person or business is unable to pay **debts**. There are federal laws and court proceedings designed to provide individuals or businesses with a way to address debt problems. Debt is money owed in exchange for loans or for goods or services purchased with credit. Discuss the following:
 - What are some examples of debts? (*Answers will vary, but common responses may include credit card bills, auto loans, cell phone bills, medical bills, student loans, or bank overdraft charges.*)
 - How can individuals or businesses address their debt problems? (*Answers will vary, but most students will probably suggest not paying their debts or working out a plan.*)

3. Display Slide 3. Explain and discuss the following:
 - Bankruptcy serves a dual-purpose: (i) It provides a fresh-start for a **debtor**, and (ii) it allows for the fair treatment of **creditors**.
 - A debtor is a person or business that owes money in exchange for loans or for goods or services purchased with credit.
 - A creditor is a person, financial institution, or other business that lends money.
 - There are six main types of bankruptcy.
 - Which of the six types of bankruptcy do you know about? (*Answers will vary; however, if students know any of the types they will probably be Chapter 7, Chapter 11, or Chapter 13.*)

4. Display Slide 4. Explain and discuss the following:
 - **Chapter 7** is often called “straight” or “**liquidation**” bankruptcy. It is available to individuals and businesses with insufficient income to pay their debts.
 - Chapter 9 is reorganization bankruptcy available to municipalities.
 - What is a “municipality”? (*Answers will vary but may include a city or town. Municipalities include cities, towns, villages, and counties.*)
 - Chapter 11 is also reorganization bankruptcy, but it is available to businesses. The debtor (business) proposes a plan to stay in business and pay creditors over time. Chapter 11 is most often associated with corporations but can be used by partnerships or small businesses.
 - Chapter 12 provides financial relief for a family farmer or family fisherman.
 - **Chapter 13** is designed for individuals with regular income who are temporarily unable to pay their debts but have sufficient income to make payments to their creditors. It is often called a “pay back” or “wage earner” plan.
 - Chapter 15 allows representatives of a foreign company involved in foreign bankruptcy to access U.S. courts.

5. Display a copy of *Handout 1: Key Bankruptcy Terms* as a visual. Distribute a copy of Handout 1 to each student. Explain that from this point the lesson will focus on the two main types of bankruptcy used by individual consumers: Chapter 7 and Chapter 13. The handout provides key bankruptcy terms. Review the terms and instruct students to highlight the following terms already mentioned in the lesson: bankruptcy, Chapter 7, Chapter 13, creditor, debtor, debts, and liquidation. Instruct the students to continue to highlight terms as they are mentioned in the lesson.
6. Display Slide 5. Explain to students that the slide contains a list of various types of debts. Tell them they will work in small groups to discuss two categories of debt: **dischargeable debt** and **nondischargeable debt**. Organize students into groups of 2 to 4 and distribute chart paper to each group. Instruct the groups to (i) draw a horizontal line halfway down the chart and (ii) on the top half draw a T-chart with “Dischargeable” and “Nondischargeable” as the headings. (They will use the bottom half later.) Each group is to determine which debts on Slide 5 are dischargeable and which are nondischargeable and why and to then list each debt under the appropriate heading. When they have completed the task, the groups’ lists will be compared.
7. Allow time for students to work, and then have a spokesperson from each group explain and defend why the group categorized the debts the way it did.
8. Explain to students that determining which debts are dischargeable and nondischargeable is a complex and legal task. For example, certain debts can be **discharged** in Chapter 13 but not in Chapter 7.
9. Display Slide 6. Review the correct answers and have students write a corrected list on the bottom half of their charts. Explain and discuss the following:
 - Student loans are almost never dischargeable in bankruptcy. The only way to discharge a student loan is by demonstrating extreme hardship, which is tremendously difficult to do.
 - In many cases, nondischargeable debts are not erased, because of public policy reasons, and the U.S. Congress has made this determination.
 - What do the nondischargeable debts have in common? (As students identify the different categories of debt, such as owed to the government or in support of others, instruct them to identify and note the category by each type of debt in the bottom section of the charts.) *(i) Some are debts owed to the government—court fines, student loans, and taxes. (ii) Some are debts used to support other individuals—alimony, child support, and personal injury payments. (iii) Some are debts related to crime—criminal debt and fraudulent debt. (iv) There are also debts incurred outside the bankruptcy timeframe—bankruptcy doesn’t absolve you of your debts forever.)*

10. Ask students to return to their seats. Display Slide 7. Tell students they will now compare and contrast the differences between Chapter 7 and Chapter 13. Discuss the following:
 - What similarities do you recognize between Chapter 7 and Chapter 13? (*Both have an **automatic stay**—a court order that stops creditors from collecting or attempting to collect debts from a debtor who has filed for bankruptcy.*)
 - What differences do you recognize between Chapter 7 and Chapter 13? (*In Chapter 7, the debtor does not have sufficient income to pay debts, while in Chapter 13, the debtor does have sufficient income to pay debts. A main reason to file Chapter 7 is to have your debts discharged, while a main reason to file Chapter 13 is to keep your possessions.*)
11. Explain that in order to file Chapter 7 or Chapter 13 bankruptcy, certain procedures must be followed and differ for each bankruptcy type. Distribute a copy of *Handout 2: Basic Procedures for Chapter 7 Bankruptcy* to each student. Tell the students that they will first review Chapter 7 procedures. As each step is displayed on a slide, they are to fill in the information next to each bullet on the handout.
12. Display Slide 8. Explain to students that credit counseling is mandatory by law. The debtor must use an approved provider, and the case will be dismissed if credit counseling is not completed. Discuss the following:
 - Why do you think it is mandatory for a debtor to complete credit counseling before filing Chapter 7 bankruptcy? (*Answers will vary. The purpose of credit counseling is to determine if bankruptcy is the right option for the debtor before the debtor begins the legal procedure.*)
13. Display Slide 9. Explain to students that the next step is to file a bankruptcy **petition**, which involves filing multiple forms and paying a filing fee at bankruptcy court. The fee is set by law and is the same for everyone (\$335 in 2019; for the current fee, see <https://www.moeb.us-courts.gov/filing-fees>). The forms contain information that helps the court complete a **means test**. A means test determines the level of a person's current income or **assets**—to see if the debtor has sufficient income or assets to pay his or her debts. Discuss the following:
 - If a debtor has sufficient income to repay creditors, will the debtor pass the means test or fail the means test? (*Pass*)
 - If the debtor has sufficient income to repay creditors, will the debtor qualify for Chapter 7 or Chapter 13? (*Chapter 13*)
14. Display Slide 10. Discuss and explain the following:
 - What is an automatic stay? (*An automatic stay is a court order that stops creditors from collecting or attempting to collect debts from a debtor who has filed for bankruptcy.*)

- Remind students that once the filing fee has been paid and the forms have been submitted, the automatic stay takes effect that very minute and creditors are notified. Some types of collections halted by the automatic stay include the following:
 - Letters and phone calls from people or agencies seeking to collect a past-due debt on behalf of a creditor
 - **Wage garnishment**—A court order imposed on an employer to withhold a portion of an employee’s wages to be sent to a person or business to whom the employee owes money
 - **Foreclosure**—The legal process by which a property that is mortgaged as security for a loan may be sold and the proceeds of the sale applied to the mortgage debt
 - **Repossession**—To retake possession of something when the buyer fails to make payments
 - The automatic stay is one of the main reasons debtors file.
15. Display Slide 11. Explain to students that the next step in the Chapter 7 bankruptcy process is for the court to assign an independent person, known as the **bankruptcy trustee**, to represent the unsecured creditors, review the case, and begin collecting the debtor’s **nonexempt property** to pay creditors, including cash, investments, and/or valuable items. An unsecured creditor is one who has provided an unsecured loan. An unsecured loan is a loan not backed with collateral. Some examples include credit card and student loan debt. A secured loan is a loan backed by collateral. Some examples are auto loans and mortgage loans.
16. Display Slide 12. Explain and discuss the following:
- A meeting—called a 341 meeting—is held for creditors to obtain information about the debtor’s financial condition.
 - The debtor is required to answer questions under oath regarding his or her finances.
 - This meeting determines if the debtor qualifies for Chapter 7 bankruptcy.
 - Participants in attendance at this meeting include the debtor, **debtor attorney**, bankruptcy trustee, and creditors.
 - The main reason for this meeting is to make sure the debtor is not “hiding” any assets.
 - What is an **asset**? (*A resource with economic value that an individual, corporation, or country owns with the expectation that it will provide future benefits; property owned by a debtor and that has value.*)
 - Lying under oath is a very serious crime and can have many consequences, including the dismissal of the bankruptcy proceeding.
17. Display Slide 13. Explain to students that if the Chapter 7 process continues, the bankruptcy trustee will begin collecting the collateral the debtor used to secure debts and give that collat-

eral to the appropriate creditor. Although the debtor can keep **exempt property**, the bankruptcy trustee can also take property that is nonexempt and sell it to pay creditors. The creditors receive any **equity** in the property seized. Discuss the following:

- What types of property are considered exempt from collection? (*Necessary clothing and household goods and furnishings, tools for a trade or profession, and pensions and public benefits*)
- What is equity? (*The difference between the market value of an asset and what is owed on the asset*)

18. Display Slide 14. Explain to students that by law, it is mandatory for the debtor to take a personal finance education course. The debtor is also required to use an approved provider and file a certificate of completion. If a certificate is not filed, the bankruptcy case will be dismissed without discharge. Discuss the following:

- Why do you think debtors have to complete a personal finance education course before discharge? (*Answers will vary. The purpose of the course is to teach debtors how to manage money and use credit wisely after bankruptcy.*)

19. Display Slide 15. Explain to students that once a discharge is granted, the debtor's obligation to pay dischargeable debt is eliminated (wiped out). At this point, the automatic stay is lifted (removed), which means that creditors can begin collection proceedings on any debt that was not discharged. Any new debt taken on would have to be paid. Discharge is the main reasons debtors file. (NOTE: If needed, review Slide 6 again—dischargeable and nondischargeable debt.)

20. Display Slide 16. Explain the following:

- The final step in Chapter 7 proceedings is to close the case.
- It is important to understand that Chapter 7 bankruptcy remains on the debtor's credit report for 10 years.
- Although the debtor can file for bankruptcy again at any time, the discharging of debts will not be allowed again for 8 years.
- Just like any other important paperwork, all bankruptcy documents should be kept for future reference.
- Chapter 7 bankruptcy is designed to provide a fresh start for individuals whose income is insufficient to pay their debts.
- Chapter 7 bankruptcy is commonly referred to as "straight bankruptcy" or "liquidation."

21. Distribute a copy of *Handout 3: Basic Procedures for Chapter 13 Bankruptcy* to each student. Tell students that they will now review Chapter 13 procedures. Again, as each step is displayed, they are to fill in the information next to each bullet. Because Chapter 7 and Chapter 13 have different objectives, it is necessary to review both sets of procedures.

22. Display Slide 17. Explain to students that the first step in a Chapter 13 bankruptcy proceeding is exactly the same as the first step in a Chapter 7 bankruptcy. Mandatory by law, the debtor must complete credit counseling from an approved provider or the case will be dismissed.
23. Display Slide 18. Explain the following:
- As with Chapter 7, the next step is to file a bankruptcy petition. In this case, it consists of filing multiple forms, paying the filing fee, and submitting a Chapter 13 bankruptcy plan.
 - Forms vary by federal district, but the filing fee is the same for everyone (\$310 in 2019; for the latest fee, see <https://www.moeb.uscourts.gov/filing-fees>).
 - Drafting a Chapter 13 plan requires extensive knowledge and understanding of many rules, regulations, and procedures. Although individuals can file a plan without an attorney, debtors are encouraged to seek legal assistance.
 - The Chapter 13 plan is extremely important because it outlines how the debtor is going to pay back his or her debts. The plan can be revised if necessary.
24. Display Slide 19. Explain to students that, as before, the next step is to have a bankruptcy trustee assigned. In this case, that person is called a Chapter 13 standing bankruptcy trustee. The trustee reviews the plan and all submitted paperwork and then either approves or rejects the plan. If the plan is rejected, the case can be dismissed or the debtor may be allowed to make revisions and resubmit a new plan.
25. Display Slide 20. Explain to students that in most instances, once the Chapter 13 petition is filed, the automatic stay takes effect that very minute. When the automatic stay begins, creditors are notified. The automatic stay stops collections just as it does for Chapter 7. Emphasize again to students that an automatic stay is one of the main reasons debtors file for bankruptcy.
26. Display Slide 21. Explain to students that the bankruptcy trustee will hold a 341 meeting with creditors, just like for Chapter 7. Participants include the debtor, debtor attorney, bankruptcy trustee, and creditors. The debtor must attend and answer questions from the trustee and creditors regarding his or her financial affairs and repayment proposed by the Chapter 13 plan. Creditors can object to the plan. If the debtor does not attend, the case can be dismissed.
27. Display Slide 22. Explain to students that the confirmation hearing is held so that the bankruptcy judge can hear the case and provide the bankruptcy trustee or creditors the opportunity to object to the plan. Ultimately, the judge will approve or reject the plan. If the bankruptcy judge rejects the plan, the debtor will be given the opportunity to revise and resubmit it and another hearing will be held. The goal of the hearing is for the bankruptcy judge to confirm the plan.
28. Display Slide 23. Explain to students that once the bankruptcy judge confirms the plan, the debtor will begin making single monthly payments to the bankruptcy trustee. The bankruptcy

trustee is responsible for disbursing money to the creditors—if the creditors filed a proof of claim. Typically, a Chapter 13 bankruptcy plan remains in effect for 3 to 5 years. Discuss the following:

- What do you think happens if the debtor neglects to make payments to the bankruptcy trustee? (*Answers will vary. The case can be dismissed and the automatic stay removed.*)
29. Display Slide 24. Explain to students that just like for Chapter 7, Chapter 13 also requires the debtor to take a personal finance education course. The debtor must use an approved provider and file a certificate of completion. If the certificate is not filed, the case will be dismissed—without discharge. Discuss the following:
- Why do you think the debtor would be obligated to take a personal finance course? (*Answers will vary. The purpose of the course is to teach the individual how to manage money and use credit wisely after bankruptcy.*)
30. Display Slide 25. Explain to students that the percentage of unsecured debt not paid during the plan is eliminated (wiped out). However, only dischargeable debt is eliminated. Also at this point, the automatic stay is lifted. Discuss the following:
- What are examples of dischargeable debt? (*Medical bills, credit card debt, unsecured debt, personal loans, payday loans, and utility bills*)
 - What are examples of nondischargeable debt? (*Alimony, child support, court fines, criminal/personal injury debt, debt incurred after bankruptcy is filed, fraudulent debt, most taxes, and most student loans*)
31. Display Slide 26. Explain the following:
- The final step in Chapter 13 proceedings is to close the case.
 - It is important to understand that Chapter 13 bankruptcy can remain on a credit report for up to 7 years. After that time, a debtor may file again, however rules and time frames do apply.
 - Just like any other important paperwork, all bankruptcy documents should be kept for future reference.
 - Chapter 13 bankruptcy is designed to provide a fresh start for individuals who have steady and sufficient income to pay their debts.
 - Chapter 13 is commonly referred to as a pay-back or wage-earner plan.
32. Tell students that they are going to use their new knowledge on bankruptcy to complete an activity. (NOTE: The activity is designed to demonstrate Chapter 7 and Chapter 13 basic procedures. Chapter 7 should be completed first, then Chapter 13. The Chapter 7 activity will require 18 students, and the Chapter 13 activity will require 20 students. Depending on class size, students may end up participating in both demonstrations.) Proceed as follow:

- Arrange 18 students into 2 groups of 9 students.
 - Give each student in the first group a “step” card (the step is noted on the bottom right of the card) from *Handout 4: Chapter 7 Step Cards*.
 - Give each student in the second group a “description” card from Handout 4.
 - Instruct the students to find the step card that matches their description card (and vice versa). There is only one correct match per card. Allow time for students to find a match.
 - Once the students believe they have found the correct match, instruct them to line up in numeric order, by step, from left to right.
 - Ask each set of students to read off their step and description cards. Poll the rest of the class for agreement or changes.
33. Display *Handout 4: Chapter 7 Step Cards—Answer Key* to confirm answers. Reiterate to students that Chapter 7 bankruptcy is a complicated, legal process.
34. Repeat the activity described in Step 32, but this time with 20 students and using *Handout 5: Chapter 13 Step Cards*. Allow time for students to find a match. When finished, have the class assess whether or not they agree with the order in which the students have placed the cards. When completed, ask students to return to their seats.
35. Display *Handout 5: Chapter 13 Step Cards—Answer Key* to confirm answers. Reiterate that Chapter 13 bankruptcy is a complicated legal process. Bankruptcy can happen to anyone, for many reasons, and each story is unique and different.
36. Ask students what they think are common causes of bankruptcy. Display Slide 27. Give students an opportunity to review the slide. Instruct the students to turn to a neighbor and discuss anything that surprises them about the common causes of bankruptcy. After a few minutes, give them the opportunity to share with the rest of the class. Complete the discussion by summarizing the causes of bankruptcy as follows:
- Although many times unavoidable, medical debt can cause severe financial hardship for individuals with or without health insurance. Illness, disability, and even death can create unforeseen expenses.
 - Extended unemployment can place a heavy burden on individuals and families, and while you cannot always control losing your job, you can plan and save while working.
 - Divorce and separation can create an enormous burden on both spouses; paying child support, alimony, and legal fees can add a significant financial burden to a single-parent household’s **budget**.
 - Natural disasters and accidents can be very costly. It is very important to make sure you protect yourself and your family with proper insurance—auto, life, health, disability, and

homeowners or renters. However, depending on the seriousness of the disaster or accident, even those with insurance coverage can find the financial burden unbearable.

- It is very important to take your personal finances seriously. Developing a financial plan should begin at an early age—your age. A financial plan begins with a budget.

37. Discuss the following:

- What is a budget? (*Answers will vary. A budget is an itemized summary of probable income and expenses for a given period. It is a plan for managing income, spending, and saving for a given period.*)

38. Explain the following:

- A budget is the most basic and most important financial tool individuals can use.
- It helps ensure individuals that they will have enough money for the things they want.
- Following a budget can help keep individuals out of debt or help them work their way out of debt.
- A budget is a powerful tool that can help individuals become financially successful and avoid bankruptcy.

39. Explain to students that sometimes they cannot control life events and bankruptcy may be the only option. Whatever the reason for filing bankruptcy, it is necessary to understand the consequences and negative effects. Discuss the following:

- What are consequences of bankruptcy? (*Answers will vary, but responses may include that bankruptcy stays on your credit report for a long time or makes it harder to get a loan.*)

40. Display Slide 28. Explain to students that there are numerous consequences and negative effects of bankruptcy. Bankruptcy can stay on a credit report for up to 10 years and any discharged debts will also be listed on the credit report. Any type of negative information appearing on a credit report will significantly lower a credit score. Having bankruptcy information on a credit report may make it very difficult to obtain future credit, increase the interest rates for borrowing, and/or make the terms of borrowing very unfavorable. Discuss the following:

- Why might bankruptcy make it more difficult to rent an apartment? (*Bankruptcy lowers a person's credit score. Potential landlords may be wary of people who have had a bankruptcy, fearing they may not pay their rent or may be irresponsible with the property.*)
- Why might bankruptcy make it more difficult or expensive to obtain a loan? (*Answers will vary. Creditors may be concerned that if all or part of past loans were not paid, future debts might not be paid. Creditors may still issue the loan, but at a higher interest rate to compensate for the additional risk they're taking.*)

- Why might bankruptcy negatively affect relationships? *(Answers will vary. Individuals who take their financial situations seriously may be wary of getting involved with individuals who have declared bankruptcy. Bankruptcy may cause stress on a current relationship, and couples who share joint finances may find that one person's poor money management negatively affects them both.)*
 - Why might bankruptcy make it more difficult to get a job? *(Individuals may find it very difficult to obtain a position that involves passing a security clearance, such as some jobs with banks or the federal government. Prospective employers may worry about the organizational skills of someone who has claimed bankruptcy. Prospective employers may simply view the applicant as risky and choose someone else.)*
41. Explain to students that young people can help prevent financial pitfalls by being educated consumers who pay their bills in full and on time, developing good saving habits, and having the necessary financial literacy skills to help them make wise economic decisions. Remind students that there is a relationship between educational attainment and income-earning potential. Individuals with more education are likely to earn higher incomes.
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Closure

42. As review, discuss the following:
- What are the two types of bankruptcy most commonly used by consumers? *(Chapter 7 and Chapter 13)*
 - What is the dual purpose of bankruptcy? *(To provide a fresh start for debtors and fair treatment to creditors)*
 - What are three examples of a dischargeable debt? *(Answers will vary but may include credit card debt, payday loans, personal loans, medical bills, unsecured debt, or utility bills.)*
 - What are three examples of a nondischargeable debt? *(Answers will vary but may include alimony, child support, court fines, criminal/personal injury debt, debt incurred after bankruptcy is filed, fraudulent debt, most taxes, and most student loans.)*
 - Name three characteristics of Chapter 7 bankruptcy. *(Answers will vary but may include the following: It is often referred to as liquidation or straight bankruptcy. The debtor has no steady or sufficient income to pay his or her debts. The main reasons to file include being granted an automatic stay and debt being discharged.)*
 - Name three characteristics of Chapter 13 bankruptcy. *(Answers will vary but may include the following: It is often referred to as a pay-back or wage-earner plan. The debtor has steady and sufficient income to pay debts. The main reasons to file include being granted an automatic stay and being able to keep possessions.)*
 - What are common causes of bankruptcy? *(Answers will vary but may include accidents, business failure, disasters, credit debt, divorce, lack of financial planning, medical bills, unemployment, or reduced income.)*
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- What are consequences and negative effects of bankruptcy? (*Answers will vary but may include that it will lower your credit score and can stay on your credit report for up to 10 years, make it more difficult to rent an apartment or obtain a loan, harm personal/business relationships, lead to higher interest rates when borrowing, or hinder future employment opportunities.*)
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Assessment

43. Distribute a copy of *Handout 6: Assessment—You Be the Judge!* Review the directions and allow students time to complete it either individually or in groups (or assign as homework). See the Handout 6—Answer Key below to check answers.

Handout 6 Assessment—You Be the Judge!—Answer Key

1. *Nicole should file for Chapter 13 bankruptcy—the pay-back or wage-earner plan. Nicole has steady and sufficient income to pay nondischargeable debts.*
2. *Brett should file for Chapter 7 bankruptcy—liquidation or straight bankruptcy. Brett does not have sufficient income to pay his secured debts. His sports car and condo will have to be sold to pay creditors. If after the sale of the sports car and condo there is still unpaid debt (including credit card [unsecured] debt), that debt may be discharged.*

Handout 1: Key Bankruptcy Terms

Asset	A resource with economic value that an individual, corporation, or country owns with the expectation that it will provide future benefits.
Automatic stay	A court order that stops creditors from collecting or attempting to collect debts from a debtor who has filed for bankruptcy.
Bankruptcy	A legal process for declaring that a person is unable to pay his or her debts. The process may involve a court-supervised process of selling the bankrupt person's belongings to pay part of the debts owed to creditors.
Bankruptcy trustee	An independent person appointed to administer a bankruptcy case, collect assets, and pay creditors.
Budget	An itemized summary of probable income and expenses for a given period. It is a plan for managing income, spending, and saving for a given period.
Chapter 7	A type of bankruptcy that requires individuals unable to pay their debts to sell his or her assets to pay creditors. Also known as "liquidation" or "straight" bankruptcy.
Chapter 13	A type of bankruptcy for a person temporarily unable to pay his or her debts but with sufficient income to make payments to his or her creditors. Also known as the "pay back" or "wage earner" plan.
Creditor	A person, financial institution, or other business that lends money.
Debtor	A person or business that owes money in exchange for loans or for goods or services purchased with credit.
Debtor attorney	A person who provides legal representation of a debtor.
Debts (liabilities)	Money owed in exchange for loans or for goods or services purchased with credit.
Discharge	The goal of bankruptcy—a court order that releases the debtor from paying debts (liabilities) owed.
Dischargeable debt	Debts (liabilities) that can be eliminated (wiped out) through a bankruptcy proceeding.
Equity	The difference between the value of an asset and what is owed on the asset.
Exempt property	Property a debtor is allowed to keep when filing for bankruptcy.
Foreclosure	The legal process by which a property that is mortgaged as security for a loan may be sold and the proceeds of the sale applied to the mortgage debt.
Liquidation	The sale of a debtor's nonexempt property and the distribution of the proceeds to creditors.
Means test	A test to determine the level of a person's current income or assets.
Nondischargeable debt	A type of debt that cannot be eliminated (wiped out) through a bankruptcy proceeding.
Nonexempt property	Property a debtor filing for bankruptcy must forfeit (give up) to pay creditors.
Petition	All required documentation that will begin a bankruptcy proceeding (e.g., bankruptcy forms, schedules, statements, plan) plus payment of the court filing fee.
Repossession	To retake possession of something when the buyer fails to make payments.
Secured debt	A loan that is backed with collateral; a loan for which the lender requires and the borrower offers property as a guarantee of repayment.
Unsecured debt	A loan not backed with collateral.
Wage garnishment	A court order imposed on an employer to withhold a portion of an employee's wages to be sent to a person or business to whom the employee owes money.

Handout 2: Basic Procedures for Chapter 7 Bankruptcy

1. Debtor Takes Credit Counseling
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2. Bankruptcy Petition Filed
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3. Automatic Stay Takes Effect
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4. Bankruptcy Trustee Assigned to Case
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5. 341 Meeting with Creditors
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6. Bankruptcy Trustee Begins Liquidation Process
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7. Debtor Takes Personal Finance Education Course
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8. Discharge Granted
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9. Case Closed
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Handout 2: Basic Procedures for Chapter 7 Bankruptcy—Answer Key**1. Debtor Takes Credit Counseling**

- Mandatory by law
- Debtor must use approved provider
- Case dismissed if counseling not completed

2. Bankruptcy Petition Filed

- Involves multiple forms and paying a filing fee (fee same for all)
- Provides information for a means test, which determines if the debtor has sufficient income or assets to pay debts

3. Automatic Stay Takes Effect

- Begins the minute petition is filed
- Creditors notified
- Stops collections: e.g., letters/calls, wage garnishments, foreclosures, and repossessions
- One of the main reasons debtors file

4. Bankruptcy Trustee Assigned to Case

- Independent person appointed to represent the unsecured creditors
- Reviews case
- Begins collecting debtor's nonexempt property (e.g., cash, investments, and/or valuable items) to pay creditors

5. 341 Meeting with Creditors

- Debtor required to answer questions under oath regarding finances
- Determines if debtor qualifies for Chapter 7
- Includes the debtor, debtor attorney, bankruptcy trustee, and creditors
- Makes sure debtor isn't "hiding" assets

6. Bankruptcy Trustee Begins Liquidation Process

- Collects collateral and gives to creditors
- Debtor can keep exempt property (necessary clothing and household goods and furnishings, tools for a trade or profession, and pensions and public benefits)
- Nonexempt property may be sold to pay creditors

7. Debtor Takes Personal Finance Education Course

- Mandatory by law
- Debtor must use approved provider
- Debtor must file certificate of completion or case will be dismissed without discharge

8. Discharge Granted

- Debtor's obligation to pay dischargeable debt eliminated (wiped out)
- Automatic stay lifted (removed)
- Main reason debtors file

9. Case Closed

- Bankruptcy remains on debtor's credit report for 10 years
- Debtor can file for bankruptcy again at any time, but cannot discharge debts again for 8 years
- Debtor should keep documents for future reference

Handout 3: Basic Procedures for Chapter 13 Bankruptcy

1. Debtor Takes Credit Counseling
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2. Bankruptcy Petition Filed
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3. Chapter 13 Standing Bankruptcy Trustee Assigned
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4. Automatic Stay
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5. 341 Meeting with Creditors
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6. Confirmation Hearing
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7. Bankruptcy Plan Begins
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8. Debtor Takes Personal Finance Education Course
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9. Discharge Granted at End of Plan
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10. Case Closed
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Handout 3: Basic Procedures for Chapter 13 Bankruptcy—Answer Key

- 1. Debtor Takes Credit Counseling**
 - Mandatory by law
 - Debtor must use approved provider
 - Case dismissed if not completed
- 2. Bankruptcy Petition Filed**
 - Includes multiple forms and paying a filing fee (fee same for all)
 - Bankruptcy plan must be submitted
 - Plan can be revised if necessary
- 3. Chapter 13 Standing Bankruptcy Trustee Assigned**
 - Reviews Chapter 13 bankruptcy plan and paperwork
 - Approves or rejects plan
 - If rejected, case dismissed or plan revised/resubmitted
- 4. Automatic Stay**
 - Begins the minute petition is filed
 - Creditors notified
 - Stops collections: e.g., letters/calls, wage garnishments, foreclosures, and repossessions
 - One of the main reasons debtors file
- 5. 341 Meeting with Creditors**
 - Debtor required to answer questions under oath regarding finances and bankruptcy plan
 - Includes the debtor, debtor attorney, bankruptcy trustee, and creditors
 - Creditors can object to bankruptcy plan
 - If debtor doesn't attend, case can be dismissed
- 6. Confirmation Hearing**
 - Bankruptcy judge hears the case
 - Trustee or creditors can object to plan
 - Judge approves or rejects plan
 - If rejected, debtor revises/resubmits plan and another hearing held
- 7. Bankruptcy Plan Begins**
 - Debtor pays single monthly payments to bankruptcy trustee
 - Bankruptcy trustee disburses money to creditors who filed proof of claim
 - Typically, plan remains in effect 3-5 years
- 8. Debtor Takes Personal Finance Education Course**
 - Mandatory by law
 - Debtor must use approved provider
 - Debtor must file certificate of completion or case will be dismissed without discharge
- 9. Discharge Granted at End of Plan**
 - Debt eliminated—specifically, the percentage of unsecured debt not paid during the plan
 - Only dischargeable—not nondischargeable—debt eliminated
 - Automatic stay lifted
- 10. Case Closed**
 - Bankruptcy can remain on debtor's credit report for up to 7 years
 - Debtor may file again, if necessary—rules and time frames apply
 - Debtor should keep documents for future reference

Handout 4: Chapter 7 Step Cards (page 1 of 3)

<p>econlowdown® click, teach, engage.</p> <h2>Debtor Takes Credit Counseling</h2> <p>Chapter 7</p>	<p>econlowdown® click, teach, engage.</p> <ul style="list-style-type: none">• Mandatory by law• Debtor must use approved provider• Case dismissed if counseling not completed <p>Chapter 7: Step 1</p>
<p>econlowdown® click, teach, engage.</p> <h2>Bankruptcy Petition Filed</h2> <p>Chapter 7</p>	<p>econlowdown® click, teach, engage.</p> <ul style="list-style-type: none">• Involves multiple forms and paying a filing fee (fee same for all)• Provides information for a means test, which determines if the debtor has sufficient income or assets to pay debts <p>Chapter 7: Step 2</p>
<p>econlowdown® click, teach, engage.</p> <h2>Automatic Stay Takes Effect</h2> <p>Chapter 7</p>	<p>econlowdown® click, teach, engage.</p> <ul style="list-style-type: none">• Begins the minute petition is filed• Creditors notified• Stops collections: e.g., letters/calls, wage garnishments, foreclosures, and repossessions• One of the main reasons debtors file <p>Chapter 7: Step 3</p>

Handout 4: Chapter 7 Step Cards (page 2 of 3)

<p>econlowdown® click.teach.engage.</p> <h2>Bankruptcy Trustee Assigned to Case</h2> <p>Chapter 7</p>	<p>econlowdown® click.teach.engage.</p> <ul style="list-style-type: none">• Independent person appointed to represent the unsecured creditors• Reviews case• Begins collecting debtor’s nonexempt property (e.g., cash, investments, and/or valuable items) to pay creditors <p>Chapter 7: Step 4</p>
<p>econlowdown® click.teach.engage.</p> <h2>341 Meeting with Creditors</h2> <p>Chapter 7</p>	<p>econlowdown® click.teach.engage.</p> <ul style="list-style-type: none">• Debtor required to answer questions under oath regarding finances• Determines if debtor qualifies for Chapter 7• Includes the debtor, debtor attorney, bankruptcy trustee, and creditors• Makes sure debtor isn’t “hiding” assets <p>Chapter 7: Step 5</p>
<p>econlowdown® click.teach.engage.</p> <h2>Bankruptcy Trustee Begins Liquidation Process</h2> <p>Chapter 7</p>	<p>econlowdown® click.teach.engage.</p> <ul style="list-style-type: none">• Collects collateral and gives to creditors• Debtor can keep exempt property (necessary clothing and household goods and furnishings, tools for a trade or profession, and pensions and public benefits)• Nonexempt property may be sold to pay creditors <p>Chapter 7: Step 6</p>

Handout 4: Chapter 7 Step Cards (page 3 of 3)

<p>econlowdown® click, teach, engage.</p> <h2 style="text-align: center;">Debtor Takes Personal Finance Education Course</h2> <p style="text-align: right;">Chapter 7</p>	<p>econlowdown® click, teach, engage.</p> <ul style="list-style-type: none"> • Mandatory by law • Debtor must use approved provider • Debtor must file certificate of completion or case will be dismissed without discharge <p style="text-align: right;">Chapter 7: Step 7</p>
<p>econlowdown® click, teach, engage.</p> <h2 style="text-align: center;">Discharge Granted</h2> <p style="text-align: right;">Chapter 7</p>	<p>econlowdown® click, teach, engage.</p> <ul style="list-style-type: none"> • Debtor's obligation to pay dischargeable debt eliminated (wiped out) • Automatic stay lifted (removed) • Main reason debtors file <p style="text-align: right;">Chapter 7: Step 8</p>
<p>econlowdown® click, teach, engage.</p> <h2 style="text-align: center;">Case Closed</h2> <p style="text-align: right;">Chapter 7</p>	<p>econlowdown® click, teach, engage.</p> <ul style="list-style-type: none"> • Bankruptcy remains on debtor's credit report for 10 years • Debtor can file for bankruptcy again at any time, but cannot discharge debts again for 8 years • Debtor should keep documents for future reference <p style="text-align: right;">Chapter 7: Step 9</p>

Handout 4: Chapter 7 Step Cards—Answer Key

Step	Procedures
Debtor Takes Credit Counseling Chapter 7	<ul style="list-style-type: none"> • Mandatory by law • Debtor must use approved provider • Case dismissed if counseling not completed <p style="text-align: right;">Chapter 7: Step 1</p>
Bankruptcy Petition Filed Chapter 7	<ul style="list-style-type: none"> • Involves multiple forms and paying a filing fee (fee same for all) • Provides information for a means test, which determines if the debtor has sufficient income or assets to pay debts <p style="text-align: right;">Chapter 7: Step 2</p>
Automatic Stay Takes Effect Chapter 7	<ul style="list-style-type: none"> • Begins the minute petition is filed • Creditors notified • Stops collections: e.g., letters/calls, wage garnishments, foreclosures, and repossessions • One of the main reasons debtors file <p style="text-align: right;">Chapter 7: Step 3</p>
Bankruptcy Trustee Assigned to Case Chapter 7	<ul style="list-style-type: none"> • Independent person appointed to represent the unsecured creditors • Reviews case • Begins collecting debtor’s nonexempt property (e.g., cash, investments, and/or valuable items) to pay creditors <p style="text-align: right;">Chapter 7: Step 4</p>
341 Meeting with Creditors Chapter 7	<ul style="list-style-type: none"> • Debtor required to answer questions under oath regarding finances • Determines if debtor qualifies for Chapter 7 • Includes the debtor, debtor attorney, bankruptcy trustee, and creditors • Makes sure debtor isn’t “hiding” assets <p style="text-align: right;">Chapter 7: Step 5</p>
Bankruptcy Trustee Begins Liquidation Process Chapter 7	<ul style="list-style-type: none"> • Collects collateral and gives to creditors • Debtor can keep exempt property (necessary clothing and household goods and furnishings, tools for a trade or profession, and pensions and public benefits) • Nonexempt property may be sold to pay creditors <p style="text-align: right;">Chapter 7: Step 6</p>
Debtor Takes Personal Finance Education Course Chapter 7	<ul style="list-style-type: none"> • Mandatory by law • Debtor must use approved provider • Debtor must file certificate of completion or case will be dismissed without discharge <p style="text-align: right;">Chapter 7: Step 7</p>
Discharge Granted Chapter 7	<ul style="list-style-type: none"> • Debtor’s obligation to pay dischargeable debt eliminated (wiped out) • Automatic stay lifted (removed) • Main reason debtors file <p style="text-align: right;">Chapter 7: Step 8</p>
Case Closed Chapter 7	<ul style="list-style-type: none"> • Bankruptcy remains on debtor’s credit report for 10 years • Debtor can file for bankruptcy again at any time, but cannot discharge debts again for 8 years • Debtor should keep documents for future reference <p style="text-align: right;">Chapter 7 Step 9</p>

Handout 5: Chapter 13 Step Cards (page 1 of 4)

<p>econlowdown[®] click, teach, engage.</p> <h2>Debtor Takes Credit Counseling</h2> <p>Chapter 13</p>	<p>econlowdown[®] click, teach, engage.</p> <ul style="list-style-type: none">• Mandatory by law• Debtor must use approved provider• Case dismissed if counseling not completed <p>Chapter 13: Step 1</p>
<p>econlowdown[®] click, teach, engage.</p> <h2>Bankruptcy Petition Filed</h2> <p>Chapter 13</p>	<p>econlowdown[®] click, teach, engage.</p> <ul style="list-style-type: none">• Involves multiple forms and paying a filing fee (fee same for all)• Bankruptcy plan must be submitted• Plan can be revised if necessary <p>Chapter 13: Step 2</p>
<p>econlowdown[®] click, teach, engage.</p> <h2>Chapter 13 Standing Bankruptcy Trustee Assigned</h2> <p>Chapter 13</p>	<p>econlowdown[®] click, teach, engage.</p> <ul style="list-style-type: none">• Reviews Chapter 13 bankruptcy plan and paperwork• Approves or rejects plan• If rejected, case dismissed or plan revised/resubmitted <p>Chapter 13: Step 3</p>

Handout 5: Chapter 13 Step Cards (page 2 of 4)

<p>econlowdown[®] click, teach, engage.</p> <h2>Automatic Stay</h2> <p>Chapter 13</p>	<p>econlowdown[®] click, teach, engage.</p> <ul style="list-style-type: none">• Begins the minute petition is filed• Creditors notified• Stops collections: e.g., letters/calls, wage garnishments, foreclosures, and repossessions• One of the main reasons debtors file <p>Chapter 13: Step 4</p>
<p>econlowdown[®] click, teach, engage.</p> <h2>341 Meeting with Creditors</h2> <p>Chapter 13</p>	<p>econlowdown[®] click, teach, engage.</p> <ul style="list-style-type: none">• Debtor required to answer questions under oath regarding finances and bankruptcy plan• Includes the debtor, debtor attorney, bankruptcy trustee, and creditors• Creditors can object to bankruptcy plan• If debtor doesn't attend, case can be dismissed <p>Chapter 13: Step 5</p>
<p>econlowdown[®] click, teach, engage.</p> <h2>Confirmation Hearing</h2> <p>Chapter 13</p>	<p>econlowdown[®] click, teach, engage.</p> <ul style="list-style-type: none">• Bankruptcy judge hears the case• Trustee or creditors can object to plan• Judge approves or rejects plan• If rejected, debtor revises/resubmits plan and another hearing held <p>Chapter 13: Step 6</p>

Handout 5: Chapter 13 Step Cards (page 3 of 4)

<p>econlowdown® click.teach.engage.</p> <h2>Bankruptcy Plan Begins</h2> <p>Chapter 13</p>	<p>econlowdown® click.teach.engage.</p> <ul style="list-style-type: none">• Debtor pays single monthly payments to bankruptcy trustee• Bankruptcy trustee disburses money to creditors who filed proof of claim• Typically, plan remains in effect 3-5 years <p>Chapter 13: Step 7</p>
<p>econlowdown® click.teach.engage.</p> <h2>Debtor Takes Personal Finance Education Course</h2> <p>Chapter 13</p>	<p>econlowdown® click.teach.engage.</p> <ul style="list-style-type: none">• Mandatory by law• Debtor must use approved provider• Debtor must file certificate of completion or case will be dismissed without discharge <p>Chapter 13: Step 8</p>
<p>econlowdown® click.teach.engage.</p> <h2>Discharge Granted at End of Plan</h2> <p>Chapter 13</p>	<p>econlowdown® click.teach.engage.</p> <ul style="list-style-type: none">• Debt eliminated—specifically, the percentage of unsecured debt not paid during the plan• Only dischargeable—not nondischargeable—debt eliminated• Automatic stay lifted <p>Chapter 13: Step 9</p>

Handout 5: Chapter 13 Step Cards (page 4 of 4)

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Case Closed

Chapter 13

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- Bankruptcy can remain on debtor's credit report for up to 7 years
- Debtor may file again, if necessary—rules and time frames apply
- Debtor should keep documents for future reference

Chapter 13: Step 10

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Handout 5: Chapter 13 Step Cards—Answer Key

Step	Procedures
Debtor Takes Credit Counseling Chapter 13	<ul style="list-style-type: none"> • Mandatory by law • Debtor must use approved provider • Case dismissed if counseling not completed Chapter 13: Step 1
Bankruptcy Petition Filed Chapter 13	<ul style="list-style-type: none"> • Involves multiple forms and paying a filing fee (fee same for all) • Bankruptcy plan must be submitted • Plan can be revised if necessary Chapter 13: Step 2
Chapter 13 Standing Bankruptcy Trustee Assigned Chapter 13	<ul style="list-style-type: none"> • Reviews Chapter 13 bankruptcy plan and paperwork • Approves or rejects plan • If rejected, case dismissed or plan revised/resubmitted Chapter 13: Step 3
Automatic Stay Chapter 13	<ul style="list-style-type: none"> • Begins the minute petition is filed • Creditors notified • Stops collections: e.g., letters/calls, wage garnishments, foreclosures, and repossessions • One of the main reasons debtors file Chapter 13: Step 4
341 Meeting with Creditors Chapter 13	<ul style="list-style-type: none"> • Debtor required to answer questions under oath regarding finances and bankruptcy plan • Includes the debtor, debtor attorney, bankruptcy trustee, and creditors • Creditors can object to bankruptcy plan • If debtor doesn't attend, case can be dismissed Chapter 13: Step 5
Confirmation Hearing Chapter 13	<ul style="list-style-type: none"> • Bankruptcy judge hears the case • Trustee or creditors can object to plan • Judge approves or rejects plan • If rejected, debtor revises/resubmits plan and another hearing held Chapter 13: Step 6
Bankruptcy Plan Begins Chapter 13	<ul style="list-style-type: none"> • Debtor pays single monthly payments to bankruptcy trustee • Bankruptcy trustee disburses money to creditors who filed proof of claim • Typically, plan remains in effect 3-5 years Chapter 13: Step 7
Debtor Takes Personal Finance Education Course Chapter 13	<ul style="list-style-type: none"> • Mandatory by law • Debtor must use approved provider • Debtor must file certificate of completion or case will be dismissed without discharge Chapter 13: Step 8
Discharge Granted at End of Plan Chapter 13	<ul style="list-style-type: none"> • Debt eliminated—specifically, the percentage of unsecured debt not paid during the plan • Only dischargeable—not nondischargeable—debt eliminated • Automatic stay lifted Chapter 13 Step 9
Case Closed Chapter 13	<ul style="list-style-type: none"> • Bankruptcy can remain on debtor's credit report for up to 7 years • Debtor may file again, if necessary—rules and time frames apply • Debtor should keep documents for future reference Chapter 13 Step 10

Handout 6: Assessment—You Be the Judge!

Directions: Review the following scenarios. For each, determine what type of bankruptcy you would recommend and why.

1. Nicole is a recent college graduate with \$85,000 in student loans. With hard work and perseverance, she was able to secure a full-time job a few weeks after graduation, with a starting salary of \$62,000 plus health insurance. Unfortunately, after celebrating her new job, she was involved in a car accident deemed her fault—for driving while intoxicated. She is now being sued by the injured parties in the other vehicle. Nicole always thought she was well protected by purchasing her state’s mandatory vehicle liability insurance. However, the cost of the damages and injuries sustained by both Nicole and the other injured parties greatly exceeded her insurance coverages. Nicole’s injuries were minor, and she was able to start her new job. Nonetheless, she is faced with the following debts in addition to her monthly living expenses:
 - Attorney’s fee: \$10,000 (because injured parties sued her)
 - Medical bills of injured parties: \$132,000
 - Damage to the other vehicle: \$40,000
 - Student loan debt: \$85,000 (monthly payments of \$350 to begin in five months)

What type of bankruptcy would you recommend and why?

2. Brett was a high school All-American in baseball. He received a full scholarship to a major university to play at the Division I level. He declined the scholarship and instead hired an agent and declared he was eligible for the Major League Baseball draft. He was drafted in the second round and received a signing bonus of \$800,000. Brett was living his childhood dream of becoming a Major League Baseball player. Unfortunately, he never made it to the big leagues. Instead of saving and investing his signing bonus, he spent it on expensive luxury items (cars, travel, clothes, a condo, etc.). Three years after signing his contract, he was released. Compounded with his current reduction in income, lack of education, and luxury lifestyle, he is faced with massive debt. Brett is currently employed at a local sporting goods store making \$22,000 annually. Over the past three years, he has accumulated the following debts that he still owes:
 - Sports car: \$75,000 (\$1,750 monthly payment)
 - Condo: \$500,000 (\$3,500 monthly payment plus utilities)
 - Credit cards: \$25,000 (\$1,000 minimum total monthly payments at a 18.9 percent interest rate)

Brett has debt collectors knocking at his door to repossess the sports car and foreclose on the condo. The credit card companies are assessing him with late fees because he cannot make his payments on time. He is trying to sell the condo; however, the housing market where he purchased it has not been seeing many sales lately.

What type of bankruptcy would you recommend and why?

National Standards for Financial Literacy

Standard 4: Using Credit. Credit allows people to purchase goods and services that they can use today and pay for those goods and services in the future with interest. People choose among different credit options that have different costs. Lenders approve or deny applications for loans based on an evaluation of the borrower’s past credit history and expected ability to pay in the future. Higher-risk borrowers are charged higher interest rates; lower-risk borrowers are charged lower interest rates.

- **Benchmark: Grade 12**

8. Failure to repay a loan has significant consequences for borrowers such as negative entries on their credit report, repossession of property (collateral), garnishment of wages, and the inability to obtain loans in the future.
9. Consumers who have difficulty repaying debt can seek assistance through credit counseling services and by negotiating directly with creditors.
10. In extreme cases, bankruptcy may be an option for consumers who are unable to repay debt. Although bankruptcy provides some benefits, filing for bankruptcy also entails considerable costs, including having notice of the bankruptcy appear on a consumer’s credit report for up to 10 years.
11. People often apply for a mortgage to purchase a home. A mortgage is a type of loan that is secured by real estate property as collateral.