Maryland Bankruptcy Legal Library

A comprehensive guide to Chapter 7 and Chapter 13

Alan J. Belsky, Esq.
The Belsky Law Firm
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66 complete articles on eligibility, property protection, debts, bankruptcy procedure, repayment plans, and related planning decisions.

About this book

This book brings together the complete Maryland bankruptcy article collection by Alan J. Belsky. It is intended to help readers understand the questions raised by Chapter 7, Chapter 13, and bankruptcy planning before discussing individual circumstances with counsel.

The legal discussion reflects the approved article text as compiled on October 25, 2026. Statutes, exemption amounts, court rules, agency standards, and case law can change. This book provides general information and does not establish an attorney-client relationship or replace advice about a particular matter.

The Belsky Law Firm is a debt relief agency. We help people file for bankruptcy relief under the Bankruptcy Code.

Online articles and current contact information are available at belskybankruptcy.com.

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Chapter 7 Bankruptcy in Maryland: What It Does, What It Does Not Do, and What You Should Know Before Filing

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By Alan J. Belsky, Attorney at Law

Understanding Chapter 7 Bankruptcy

Chapter 7 bankruptcy is a federal legal proceeding designed to provide qualifying individuals with relief from debts they cannot reasonably repay. Often called a “straight bankruptcy” or “liquidation bankruptcy,” Chapter 7 permits debtors to eliminate many financial obligations while retaining property protected by applicable exemption laws.

The word *liquidation* can be misleading. Although a Chapter 7 trustee has authority to sell certain nonexempt property, many consumer bankruptcy cases are concluded without the sale of any property whatsoever. These are commonly called *no-asset cases*.

For Maryland residents, the availability of Chapter 7 relief depends upon the interaction of federal bankruptcy law, Maryland exemption statutes, the debtor's financial circumstances, and the nature of the debts involved.

A properly planned Chapter 7 case can provide substantial relief. An inadequately evaluated filing, however, can expose property to liquidation, jeopardize otherwise available protections, or leave the debtor responsible for obligations the debtor expected to eliminate.

1. What Chapter 7 Bankruptcy Accomplishes

The principal benefit of Chapter 7 is the discharge of qualifying debts.

A bankruptcy discharge is a federal court order that generally eliminates the debtor's personal legal obligation to pay debts covered by the discharge. It also prohibits creditors from attempting to collect those discharged debts as personal liabilities.

Common examples include ordinary credit card balances, medical bills, unsecured personal loans, certain deficiency balances following repossession, and many civil judgments.

The discharge does not necessarily eliminate every debt, invalidate every lien, or resolve every dispute concerning ownership of property.

Chapter 7 ordinarily offers relief through two distinct mechanisms: the automatic stay, which generally protects the debtor during the bankruptcy proceeding, and the discharge injunction, which protects the debtor against collection of discharged debts afterward.

2. The Automatic Stay: Immediate Protection From Collection

Under 11 U.S.C. § 362, filing a bankruptcy petition generally creates an automatic stay without the necessity of obtaining a separate court order.

The stay ordinarily prohibits creditors from beginning or continuing collection lawsuits, enforcing judgments, garnishing wages, pursuing most collection calls, and taking many other actions to collect prepetition debts.

The automatic stay can also temporarily stop foreclosure proceedings, repossessions, and certain other actions involving the debtor's property.

But the protection is not absolute.

Certain criminal proceedings, domestic support matters, governmental regulatory actions, and other specifically identified activities may continue. The stay may also be limited when a debtor has had bankruptcy cases dismissed within the preceding year.

A creditor may request relief from the stay, particularly when its collateral is not adequately protected or other statutory grounds exist.

Why timing matters

Consider an employee whose wages are being garnished to satisfy a credit card judgment. Filing a Chapter 7 petition will ordinarily stop further garnishment of postpetition wages for that prepetition debt.

Whether money previously withheld can be recovered is a separate question involving the timing of the garnishment, ownership of the funds, exemption rights, and potentially the bankruptcy trustee's avoidance powers.

The filing date can therefore make a significant difference.

3. Who Qualifies for Chapter 7 Bankruptcy?

Chapter 7 is available to qualifying individuals, including those who are employed, unemployed, retired, or receiving disability benefits.

There is no general requirement that a debtor be unemployed or have no income.

Eligibility involves several considerations, including the debtor's income, household circumstances, allowable expenses, prior bankruptcy filings, and the statutory restrictions applicable to certain debtors.

The means test

The Chapter 7 means test, principally governed by 11 U.S.C. § 707(b), is designed to identify certain consumer cases in which granting Chapter 7 relief may constitute an abuse of the bankruptcy system.

The analysis generally begins by calculating current monthly income, a term with a technical meaning under the Bankruptcy Code.

For most debtors, current monthly income is based on qualifying income received during the six complete calendar months preceding the month of filing, subject to statutory inclusions and exclusions.

This is not necessarily the debtor's current paycheck multiplied by twelve.

If the debtor's annualized current monthly income does not exceed the applicable Maryland median income for the relevant household size, the statutory presumption of abuse under the means test generally does not arise.

If income exceeds that threshold, the debtor may still qualify after applying the statutory expense deductions and other calculations.

The applicable median-income figures and permitted expense standards change periodically. They must be determined using the figures applicable on the anticipated filing date.

Household size is not always obvious

A debtor living with adult children, an elderly parent, or other relatives may face questions concerning household size.

Residence under the same roof does not automatically resolve the issue. Courts have considered different approaches to household composition, economic interdependence, and financial support.

The correct analysis depends upon the governing law, the particular facts, and the purpose for which household size is being determined.

This subject deserves its own article because household size can materially affect both means-test eligibility and the assessment of reasonable household expenses.

4. What Happens to Your Property in Chapter 7?

When a bankruptcy petition is filed, most of the debtor's legal and equitable interests in property become part of the bankruptcy estate under 11 U.S.C. § 541.

That does not mean the trustee automatically takes possession of everything the debtor owns.

The Bankruptcy Code permits debtors to exempt qualifying property from administration, subject to applicable federal and state law.

Property that is properly exempted is generally protected from liquidation for the benefit of ordinary bankruptcy creditors.

Nonexempt property, however, may be sold by the Chapter 7 trustee if doing so will produce a meaningful benefit to the estate after accounting for secured claims, exemptions, costs of sale, and administrative expenses.

The no-asset Chapter 7 case

Many individual Chapter 7 cases are administered as no-asset cases because the debtor's property is exempt, has insufficient realizable equity, or otherwise offers no meaningful distribution to unsecured creditors.

A no-asset case does not mean that the debtor owns nothing.

It means that the trustee has not identified property available for distribution after considering the relevant legal and economic factors.

Debtors should not assume that their cases will be no-asset cases without a careful examination of their property and exemption rights.

5. Maryland Bankruptcy Exemptions

Maryland has opted out of the federal bankruptcy exemption scheme contained in 11 U.S.C. § 522(d). Consequently, debtors subject to Maryland exemption law generally rely upon Maryland exemptions and other applicable federal nonbankruptcy protections.

Maryland Courts and Judicial Proceedings Article § 11-504 provides important protections for qualifying personal property, residential property, retirement assets, and certain other interests. Its provisions have been amended, making reliance on older exemption charts potentially hazardous.

Exemption planning requires more than comparing the value of an asset with a statutory dollar amount. The nature of the debtor's ownership interest, outstanding liens, valuation, applicable statutory restrictions, and sometimes the debtor's domicile history can be decisive.

Homes and real estate

A debtor who owns a home is not automatically disqualified from Chapter 7.

The relevant questions include its fair market value, mortgage balances, ownership structure, available exemptions, and whether a trustee could realize a meaningful amount for creditors.

Special considerations arise when a married couple owns real estate as tenants by the entirety. Maryland law may protect entirety property against claims of creditors of only one spouse, but joint obligations can substantially change the analysis.

Divorce, separation, jointly owned property, and prior transfers require particular attention.

Retirement accounts

Many qualified retirement accounts receive substantial protection under Maryland and federal law. However, not every account labeled a retirement account necessarily qualifies for identical treatment.

Inherited accounts, excessive contributions, and other unusual arrangements may require additional analysis.

6. Which Debts Can Be Discharged?

Most ordinary unsecured consumer debts are potentially dischargeable in Chapter 7.

Other obligations may survive bankruptcy because Congress has determined that they should not be eliminated automatically, or because a creditor establishes a statutory exception.

Examples include certain domestic support obligations, some taxes, debts arising from particular forms of fraud, and certain obligations involving willful and malicious injury.

Student loans are generally subject to special discharge rules under 11 U.S.C. § 523(a)(8). They are not categorically impossible to discharge, but relief ordinarily requires establishing undue hardship in an appropriate proceeding.

A debtor should also understand that discharge of personal liability ordinarily does not eliminate a valid mortgage or other lien securing a debt.

7. What Happens to Your Car and Mortgage?

A common misconception is that bankruptcy necessarily results in the loss of a financed automobile or home.

Chapter 7 can eliminate personal liability for a dischargeable debt without automatically eliminating the creditor's lien against the collateral.

A debtor who wishes to retain collateral generally must address the secured creditor's rights and the continuing payment obligations.

Depending on the type of collateral, the agreement, and applicable law, the options may involve maintaining payments, reaffirmation, redemption, surrender, or other arrangements.

Reaffirmation deserves particular caution. A valid reaffirmation agreement can preserve personal liability for a debt that otherwise would have been discharged.

8. The Chapter 7 Trustee and Meeting of Creditors

After filing, a Chapter 7 trustee is appointed to examine the debtor's financial affairs and administer any property available for creditors.

The debtor must ordinarily attend a meeting under 11 U.S.C. § 341, commonly called the *meeting of creditors*.

The meeting is not a trial. A bankruptcy judge does not preside. The trustee questions the debtor under oath about the petition, schedules, property, debts, income, and other relevant matters. Creditors may attend and ask appropriate questions, although their attendance is not required.

Most routine meetings are relatively brief, but the trustee may request additional documents or continue the examination.

Accuracy in the bankruptcy schedules and full cooperation with the trustee are essential.

9. Transfers and Payments Made Before Bankruptcy

One of the most important parts of bankruptcy planning concerns transactions occurring before the petition is filed.

Debtors sometimes attempt to protect assets by transferring property to relatives, repaying family members, changing account ownership, or disposing of valuable possessions.

Such transactions can create serious complications.

Under 11 U.S.C. §§ 547 and 548, trustees possess powers to avoid certain preferential payments and fraudulent transfers, subject to statutory requirements and defenses.

A transfer made without fraudulent intent may still create problems.

For example, repayment of a substantial loan to a family member shortly before bankruptcy may expose that family member to a preference action.

The appropriate response is not to conceal the transaction. It is to disclose it and evaluate the consequences before filing.

10. The Importance of Complete Disclosure

Bankruptcy requires comprehensive disclosure of assets, debts, income, expenses, financial transactions, and other information requested in the official forms.

Assets include more than bank accounts and tangible property.

Potential claims arising from automobile accidents, medical malpractice, employment disputes, contract breaches, and other legal wrongs may constitute property of the bankruptcy estate, even when no lawsuit has yet been filed.

Failure to disclose a claim can produce consequences extending beyond bankruptcy, including disputes over who controls the claim and whether the debtor may pursue it afterward.

Intentional concealment, false oaths, or other serious misconduct can result in denial or revocation of discharge, and potentially criminal consequences.

11. How Long Does Chapter 7 Take?

A relatively straightforward Chapter 7 case commonly results in discharge approximately three to four months after filing, although the actual timetable varies.

Before filing, most individual debtors must complete approved credit counseling. After filing, an additional financial management course is generally required before discharge.

The meeting of creditors ordinarily occurs early in the case. Deadlines for objections and other proceedings follow.

A discharge does not necessarily mean the case has closed. When assets must be administered, the trustee's work may continue well beyond the discharge date.

12. What Chapter 7 Does Not Accomplish

Chapter 7 does not guarantee that every debt will disappear, that every asset will be protected, or that every creditor will be prevented from exercising legitimate secured rights.

It does not ordinarily discharge a nonfiling cosigner's independent liability. Nor does it resolve every tax obligation, support obligation, or debt involving alleged misconduct.

Bankruptcy also does not repair the underlying circumstances that created financial difficulties. A debtor whose ongoing expenses exceed income may need additional financial adjustments even after obtaining a discharge.

For some individuals, Chapter 13 may provide a better solution, particularly when they need to cure mortgage arrears, protect nonexempt property, or address debts that cannot effectively be managed through Chapter 7.

13. Why Bankruptcy Planning Matters

The decision to file Chapter 7 should follow a careful review of the debtor's financial condition.

The analysis should include the value and ownership of assets, available exemptions, secured and unsecured debts, income history, household expenses, prior transfers, pending lawsuits, potential inheritances, and the consequences of filing at a particular time.

A debtor with substantial credit card debt and fully exempt assets may be an excellent Chapter 7 candidate.

Another debtor with similar debt, but significant nonexempt home equity or a pending personal injury recovery, may face substantial risks.

The difference is not necessarily the amount owed. It is the legal and financial structure of the debtor's affairs.

The Bottom Line

Chapter 7 bankruptcy can provide a meaningful fresh start by eliminating qualifying debts and protecting assets within the limits established by law.

Its benefits, however, depend upon accurate financial disclosure, careful exemption analysis, appropriate timing, and a realistic understanding of what bankruptcy can and cannot accomplish.

For Maryland residents, those considerations should be evaluated before the petition is filed—not after the trustee discovers a problem.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 362 — Automatic stay.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 522 — Exemptions.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 524 — Effect of discharge and reaffirmation agreements.
- 11 U.S.C. § 547 — Preferential transfers.
- 11 U.S.C. § 548 — Fraudulent transfers.
- 11 U.S.C. § 707 — Dismissal and abuse of Chapter 7.
- 11 U.S.C. § 727 — Chapter 7 discharge and grounds for denial.

Maryland law

- Maryland Code, Courts and Judicial Proceedings § 11-504 — Maryland exemptions.

Selected decisions

- *Schwab v. Reilly*, 560 U.S. 770 (2010) — Explains the importance of how exemptions are claimed and valued.
- *Law v. Siegel*, 571 U.S. 415 (2014) — Limits bankruptcy courts' authority to override statutory exemption protections through equitable powers.
- *Harris v. Viegelahn*, 575 U.S. 510 (2015) — Addresses undistributed postpetition wages following conversion from Chapter 13 to Chapter 7.
- *Taggart v. Lorenzen*, 587 U.S. 554 (2019) — Establishes the standard for civil contempt sanctions for violation of a discharge injunction.

Administrative reference

- United States Trustee Program — Means Testing — Official median-income figures and allowable expense standards, updated periodically.

Maryland's New Homestead Exemption: Why Chapter 7 Bankruptcy Is Now an Option for Many More Homeowners

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By Alan J. Belsky, Attorney at Law

A Major Change in Maryland Bankruptcy Law

For many years, Maryland homeowners considering Chapter 7 bankruptcy faced a difficult choice. They might have qualified financially for a discharge of their debts but possessed too much equity in their homes to file Chapter 7 without risking the sale of their property by a bankruptcy trustee.

That calculation changed dramatically on June 1, 2026.

Under legislation enacted as Senate Bill 939, Chapter 400 of the Laws of Maryland 2026, the Maryland General Assembly increased the bankruptcy exemption for qualifying owner-occupied residential property from $31,575 to $125,000.

The increase represents nearly a fourfold expansion in the amount of home equity ordinarily protected under this particular exemption.

The practical significance is substantial. Many homeowners who previously had to consider Chapter 13 bankruptcy to protect their residences may now be eligible to obtain relief under Chapter 7 without exposing their homes to liquidation.

This change does not guarantee that every homeowner can safely file Chapter 7. It does, however, warrant a fresh examination of cases in which home equity previously presented the principal obstacle.

1. Why the Former Exemption Was a Problem

Chapter 7 bankruptcy is sometimes described as a liquidation proceeding. Although most consumer cases do not involve the sale of assets, a Chapter 7 trustee has authority to liquidate nonexempt property for the benefit of creditors.

Before June 1, 2026, Maryland's bankruptcy residential-property exemption was tied to the federal homestead exemption amount, which had increased to $31,575 effective April 1, 2025.

For homeowners whose equity substantially exceeded that amount, Chapter 7 could be risky.

Consider a homeowner with a residence worth $425,000 and an outstanding mortgage balance of $325,000.

The homeowner has approximately $100,000 in equity. Under the former exemption, approximately $68,425 of that equity exceeded the residential exemption, before considering other potentially applicable exemptions, liens, and sale expenses.

That amount could provide a financial incentive for a Chapter 7 trustee to sell the residence.

The homeowner might therefore have been advised to consider Chapter 13, even if the debtor otherwise qualified for Chapter 7 and had no need for a repayment plan.

Under the new law, the same homeowner's $100,000 equity interest may fall entirely within the $125,000 residential exemption.

The result can be a fundamentally different bankruptcy analysis.

2. What the New Maryland Law Provides

Maryland Courts and Judicial Proceedings Article § 11-504(f), as amended by Chapter 400, provides an exemption of up to $125,000 for an individual's qualifying interest in owner-occupied residential property in bankruptcy.

The protection extends to qualifying residences, including conventional houses, condominium units, specified manufactured homes, cooperative housing interests, and certain residential property held in revocable trusts.

The statute also provides that when multiple individuals in the same bankruptcy proceeding claim the exemption for the same property, the combined exemption cannot exceed $125,000.

The law eliminates certain former restrictions concerning previous claims of the residential exemption and provides for inflation adjustments beginning in fiscal year 2028.

The $125,000 figure is therefore not necessarily doubled merely because two spouses file bankruptcy together.

The exemption protects equity, not the entire home's value

A homeowner need not own an inexpensive home to benefit.

The critical distinction is between the market value of the residence and the value of the debtor's ownership interest after accounting for enforceable liens and other relevant interests.

A house worth $600,000 with $500,000 in qualifying mortgage debt may present substantially less liquidation risk than a mortgage-free house worth $200,000.

The amount of equity, rather than the property's gross value alone, is central to the analysis.

3. How Much Difference Does the Increase Make?

The following examples assume one qualifying homeowner, a valid mortgage, and no additional liens or unusual exemption issues.

Illustrative comparison for a homeowner with $100,000 in equity: the former $31,575 residential exemption left $68,425 above that exemption; the $125,000 exemption leaves no equity above that exemption. These figures assume one qualifying homeowner and disregard other liens, exemptions, and sale expenses, as stated above.

The new exemption can change the outcome for homeowners with moderate equity. It is particularly important for individuals who have accumulated equity through years of mortgage payments or rising real estate values but lack sufficient disposable income to pay their unsecured debts.

4. Does the New Exemption Mean the Trustee Cannot Sell the House?

Not necessarily.

A Chapter 7 trustee evaluates the debtor's interest in the property, its market value, enforceable liens, applicable exemptions, estimated costs of sale, and the amount potentially available for creditors.

When the debtor's entire equity interest is properly exempt, there ordinarily is no economic benefit to the estate from selling the property solely to reach that equity.

If equity exceeds the available exemption, however, the trustee may consider liquidation.

A sale is not automatic merely because a small amount of equity is nonexempt. Trustees must consider whether the proceeds remaining after relevant expenses would justify administering the property.

Conversely, a debtor should not assume that modest nonexempt equity is harmless.

The proper inquiry is whether the trustee could generate a meaningful distribution for the estate.

5. Home Valuation Can Determine the Outcome

The increased exemption makes accurate property valuation especially important.

A homeowner may believe the property is worth $475,000 while a trustee believes it could sell for $525,000. That $50,000 difference may determine whether the property is protected or presents a liquidation opportunity.

Online valuation estimates, tax assessments, real estate market analyses, and formal appraisals may produce different figures.

The Bankruptcy Code generally measures the value of the debtor's property interest as of the petition date.

In borderline cases, obtaining a credible appraisal before filing may be worthwhile.

Mortgage payoff figures, home-equity lines of credit, judgment liens, and other encumbrances must also be examined. Not every recorded claim necessarily has the same priority or legal effect.

6. Married Homeowners and Tenancy by the Entirety

Maryland recognizes tenancy by the entirety, a form of ownership available to married couples that can provide substantial protection against creditors holding claims against only one spouse.

This protection is distinct from the statutory residential exemption.

A married homeowner may have protection arising from the ownership structure itself, even when the property's equity exceeds the statutory exemption.

However, the existence of joint debts can materially change the result.

A creditor holding an enforceable claim against both spouses may occupy a different position from a creditor holding a claim against only one.

The analysis becomes more complicated when only one spouse files bankruptcy, when both spouses file, or when the spouses are separated or divorced.

A divorce can terminate tenancy-by-the-entirety ownership, changing the nature of the former spouses' property interests even when the deed has not been changed.

Accordingly, marital status, the source of the debts, the deed, and the history of property ownership should all be examined before filing.

The increased residential exemption provides another important protection, but it does not eliminate the need to analyze tenancy by the entirety.

7. What About Homes Held in Revocable Trusts?

The 2026 legislation expressly extends the residential exemption to qualifying property held in a revocable trust.

This addresses an important concern for homeowners who have transferred title to a revocable living trust as part of their estate planning.

A revocable trust generally permits the settlor to retain significant control over the trust property, including the ability to revoke or modify the arrangement.

The bankruptcy consequences depend upon the trust's terms, the debtor's legal and equitable interests, and applicable law.

The new statutory language makes clear that qualifying residential property of a settlor held in a revocable trust is included within the residential exemption.

That does not mean every trust arrangement qualifies. Irrevocable trusts, interests held for others, and arrangements involving multiple beneficiaries require separate examination.

8. Does the Exemption Stop Foreclosure?

No. This distinction is critical.

The homestead exemption generally protects the debtor's equity against administration for unsecured creditors through the bankruptcy estate. It does not eliminate a valid mortgage lien or relieve the homeowner of the need to address mortgage payments.

A homeowner who is substantially behind on mortgage payments may still face foreclosure after the automatic stay ends or the lender obtains relief from the stay.

Chapter 7 does not ordinarily provide a mechanism to cure mortgage arrears through a multiyear repayment plan.

Chapter 13 may therefore remain the better choice for a homeowner who has significant arrears but sufficient income to resume regular payments and cure the default.

The increased homestead exemption primarily changes the analysis for homeowners who can maintain their mortgages but have unsecured debts they cannot reasonably repay.

9. Why Chapter 7 May Now Be Preferable to Chapter 13

Chapter 13 remains an important option for homeowners who need to cure mortgage arrears, address certain nondischargeable obligations, or protect assets that cannot be exempted.

But Chapter 13 generally requires a repayment plan lasting three to five years. The debtor must make required plan payments, comply with ongoing obligations, and obtain court approval of the plan.

For a homeowner whose mortgage is current, whose equity is now protected, and whose other financial circumstances permit Chapter 7, a Chapter 13 repayment plan may no longer be necessary.

Chapter 7 ordinarily offers a faster discharge, fewer continuing obligations, and no multiyear repayment plan.

That distinction is particularly important for older homeowners, retirees, and individuals whose income is sufficient to maintain housing expenses but insufficient to service substantial unsecured debt.

The means test and other Chapter 7 eligibility requirements still apply.

10. What If the Home Has More Than $125,000 in Equity?

Exceeding the exemption does not automatically disqualify a homeowner from Chapter 7.

The trustee must consider whether liquidation would provide a meaningful financial benefit to the estate.

For example, a homeowner with $135,000 in equity may have only $10,000 exceeding the exemption before considering the costs of selling the property and administering the estate.

Those expenses may make a sale economically unattractive.

But this is not a safe assumption in every case. Property valuation, sale expenses, lien priority, trustee compensation, and other factors can change the result.

A debtor should not file Chapter 7 merely because the excess equity appears small.

11. The Importance of Filing Dates and Residency

The new Maryland exemption took effect June 1, 2026.

A debtor who filed before that date should not assume the increased exemption automatically applies retroactively.

Exemption rights ordinarily are determined under the law applicable to the bankruptcy filing, subject to governing statutory provisions.

Federal law also imposes domicile requirements that can affect which state's exemption laws a debtor may use.

Under 11 U.S.C. § 522(b)(3)(A), the relevant analysis generally examines the debtor's domicile during the 730 days preceding filing, with additional rules when the debtor has not been domiciled in one state throughout that period.

Consequently, someone who recently moved to Maryland may not automatically qualify to use Maryland's new exemption.

12. Why Homeowners Should Reconsider Earlier Bankruptcy Advice

A homeowner who consulted a bankruptcy attorney in 2024 or 2025 may have been advised that Chapter 7 was too risky because of home equity.

That advice may have been entirely appropriate when given.

But the legal landscape has changed.

A homeowner who previously could not safely pursue Chapter 7 may now have sufficient exemption protection to do so.

This does not mean the earlier advice was incorrect. It means that the legal assumptions underlying the recommendation may no longer apply.

For homeowners burdened by credit card debt, medical bills, personal loans, or judgments, the increased exemption may open a path to debt relief that was previously unavailable.

The prudent course is to obtain a new analysis using the current exemption statute, current property value, outstanding mortgage balances, and the debtor's complete financial circumstances.

Conclusion

Maryland's 2026 increase in its bankruptcy residential-property exemption is one of the most consequential changes in recent years for homeowners considering Chapter 7 relief.

By increasing the protected equity amount to $125,000, the General Assembly significantly reduced the risk of liquidation for many homeowners.

The change does not eliminate every bankruptcy risk. Mortgages remain enforceable, nonexempt equity may still be administered, and Chapter 7 eligibility requirements remain in effect.

Nevertheless, homeowners who previously ruled out Chapter 7 because of home equity should reconsider their options under the new law.

For many Maryland families, the increased exemption may make the difference between years of repayment obligations and a relatively prompt Chapter 7 discharge.

Related Bankruptcy Cases and Authorities

Maryland statutes and legislation

- Maryland Code, Courts and Judicial Proceedings § 11-504 — Governs Maryland exemptions, including the bankruptcy residential-property exemption under subsection (f).
- 2026 Maryland Senate Bill 939, Chapter 400 — Increased the residential exemption to $125,000, expanded qualifying property to include certain revocable trusts, and established inflation adjustments.
- Maryland Department of Legislative Services, Fiscal and Policy Note, SB 939 — Explains the legislative changes and prior law.

Federal statutes

- 11 U.S.C. § 522 — Exemptions and applicable domicile requirements.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 363 — Sale and administration of estate property.
- 11 U.S.C. § 704 — Duties of the Chapter 7 trustee.
- 11 U.S.C. § 1325 — Chapter 13 plan confirmation, including the liquidation-value requirement.

Selected decisions

- *Schwab v. Reilly*, 560 U.S. 770 (2010) — Addresses the distinction between exempting a specified value in property and claiming the property itself as exempt.
- *Law v. Siegel*, 571 U.S. 415 (2014) — Holds that bankruptcy courts cannot use general equitable powers to contravene express statutory exemption protections.
- *Owen v. Owen*, 500 U.S. 305 (1991) — Addresses lien avoidance and the interaction between state exemption law and federal bankruptcy protections.
- *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992) — Explains the significance of timely objections to claimed exemptions.
- *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985) — Addresses the administration of tenancy-by-the-entirety property in bankruptcy when joint creditors exist.

Legal review draft | October 24, 2026. The $125,000 amount has been checked against the enacted Maryland statute. Final publication should include a citation and technical accuracy review.

Tenancy by the Entirety in Maryland Bankruptcy: How Joint Debts, Divorce, and Property Ownership Affect Protection of the Family Home

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By Alan J. Belsky, Attorney at Law

A Form of Ownership That Can Protect More Than the Homestead Exemption

Maryland law recognizes a form of property ownership between married persons known as *tenancy by the entirety*. It provides protections against creditors that can be considerably more valuable than an ordinary dollar-limited bankruptcy exemption.

In some circumstances, a married debtor may file Chapter 7 bankruptcy and protect an interest in a residence containing hundreds of thousands of dollars in equity, even though the equity exceeds Maryland's statutory homestead exemption.

The protection does not arise simply because the debtor is married or because both spouses live in the house. It depends upon how the property is owned, whether the marriage remains legally intact, and, critically, whether creditors hold claims against one spouse or both.

A single joint debt can materially change the analysis.

For Maryland homeowners considering bankruptcy, the distinction between individual and joint obligations can be as important as the amount of equity in the residence.

1. What Is Tenancy by the Entirety?

Tenancy by the entirety is a form of concurrent ownership available to married spouses.

Under Maryland law, property held by the entirety is owned by the marital unit rather than by each spouse as the holder of an independently transferable fractional share.

Neither spouse acting alone can ordinarily convey or encumber the property so as to defeat the other's interest. Each spouse also possesses a right of survivorship: upon the death of one spouse, the surviving spouse continues to own the property.

Maryland courts have long recognized that entireties property generally cannot be reached by a creditor holding a claim against only one spouse.

In *Bruce v. Dyer*, 309 Md. 421, 524 A.2d 777 (1987), the Supreme Court of Maryland, then known as the Court of Appeals, discussed the distinctive characteristics of entireties ownership, including the limitations on unilateral severance.

The protection is not an unlimited exemption from every creditor. A creditor with an enforceable obligation against both spouses stands in a materially different position.

2. How Tenancy by the Entirety Differs From Other Forms of Joint Ownership

Married couples sometimes assume that any jointly owned property receives the same protection. It does not.

Form of ownership	Principal characteristics
Tenancy by the entirety	Ownership by married spouses as a marital unit, with survivorship and special protection against individual creditors
Joint tenancy	Co-owners hold interests with survivorship rights, generally subject to severance
Tenancy in common	Each owner possesses a separate undivided interest, generally transferable and inheritable
Sole ownership	One individual owns the property, subject to any applicable marital rights and liens

The wording of the deed, the marital status of the owners when title was acquired, and subsequent events must be examined.

A deed conveying Maryland real estate to two married persons generally creates a tenancy by the entirety unless the instrument indicates a contrary intention. Nevertheless, the actual deed should always be reviewed.

The names appearing on a mortgage statement or property tax bill do not conclusively establish the form of ownership.

3. Why Individual Creditors Generally Cannot Reach Entireties Property

Suppose a married couple owns a home as tenants by the entirety.

The husband incurs $90,000 in credit card debt solely in his name. His wife neither signs the credit agreements nor otherwise becomes legally responsible for those obligations.

The credit card creditors may obtain judgments against the husband personally. Ordinarily, however, they cannot execute against the couple's entireties residence to satisfy his individual debts.

The same principle generally applies when the wife alone incurs an unsecured obligation.

Federal tax liens require separate analysis. State protection of entireties property against an individual spouse's ordinary creditors does not by itself prevent a federal tax lien from attaching to that spouse's property rights. United States v. Craft, 535 U.S. 274 (2002), rejects reliance on state entireties immunity alone to defeat the federal tax lien.

The protection follows from Maryland property law, not from the amount of the bankruptcy homestead exemption.

This distinction can have enormous practical consequences.

A debtor may have a substantial ownership interest in a valuable residence while possessing relatively little nonexempt property available to satisfy individual unsecured creditors.

But the analysis changes when the spouses are jointly liable.

4. Joint Debts: The Critical Exception

A creditor holding an enforceable claim against both spouses may reach property held by the entirety.

Joint liability can arise in several ways, including a loan agreement signed by both spouses, a joint credit account, a jointly incurred contractual obligation, or a judgment establishing liability against both.

It is important to distinguish a genuine joint credit account from an account on which one spouse is merely an authorized user.

Marriage alone does not ordinarily make one spouse liable for every debt incurred by the other.

Example: One joint credit card changes the picture

Assume a husband files Chapter 7 individually.

He and his wife own a home with $250,000 in equity as tenants by the entirety.

The husband has $120,000 in individual unsecured debts. His wife has no responsibility for those obligations.

If there are no joint unsecured creditors and no other complicating circumstances, the entireties exemption may protect the residence notwithstanding the substantial equity.

Now assume the spouses also owe $15,000 on a genuinely joint credit card.

That obligation changes the legal analysis because a creditor of both spouses may reach entireties property.

The Chapter 7 trustee may have authority to administer the property for the benefit of joint creditors, subject to the Bankruptcy Code's requirements.

It would be incorrect to conclude that the house is necessarily safe simply because the joint debt is small compared with the home's value.

Whether administration is economically justified is a separate question.

5. The Fourth Circuit's Decision in *Sumy v. Schlossberg*

The controlling Fourth Circuit decision is *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985).

The debtor filed Chapter 7 individually and sought to exempt his interest in Maryland entireties property. His scheduled debts included obligations owed jointly with his nonfiling spouse.

The court held that the entireties exemption does not protect the property to the extent of joint claims.

Importantly, the court recognized that a Chapter 7 trustee may administer entireties property for the benefit of joint creditors under the applicable provisions of 11 U.S.C. § 363.

The decision rejected the proposition that the presence of a nonfiling spouse automatically prevents administration of entireties property.

At the same time, *Sumy* recognized the continuing protection afforded against creditors holding only individual claims.

The practical lesson from *Sumy*

The relevant inquiry is not simply whether the debtor owns the home with a spouse.

It is whether the creditors whose claims are relevant to the bankruptcy administration could reach the property under Maryland nonbankruptcy law.

The amount and character of joint indebtedness therefore require careful examination before filing.

6. Can a Trustee Sell the House When Only One Spouse Files?

Potentially, yes.

Under 11 U.S.C. § 363(h), a trustee may, in specified circumstances, sell both the bankruptcy estate's interest and a nondebtor co-owner's interest in property held as tenants by the entirety, joint tenants, or tenants in common.

The statute imposes conditions, including requirements concerning the impracticability of partition, the benefit to the estate, the detriment to co-owners, and certain limitations involving energy-related property.

The nonfiling spouse's interest cannot simply be disregarded.

Section 363(i) provides qualifying co-owners with a right to purchase the property at the price at which the proposed sale would otherwise be consummated.

Section 363(j) governs distribution of sale proceeds according to the respective interests of the estate and co-owners after appropriate costs and expenses.

Thus, a trustee's authority to administer entireties property does not mean that the trustee automatically receives all proceeds free of the nonfiling spouse's rights.

Nevertheless, a forced sale can create substantial financial and personal disruption even where the nonfiling spouse is entitled to protections under the statute.

7. Does a Small Joint Debt Put the Entire Home at Risk?

The presence of even a relatively small joint claim can defeat the argument that entireties property is completely immune from administration.

But that does not necessarily mean a trustee will sell the residence.

A trustee must consider the value available to satisfy allowable claims, the expenses of administration, the rights of the nonfiling spouse, and the practical consequences of a proposed sale.

In some cases, administration may be economically unattractive.

In others, the trustee may seek a negotiated resolution rather than a sale.

A debtor should not rely on the assumption that a trustee will ignore a small joint debt.

The question is sufficiently consequential that the complete list of joint obligations should be examined before a Chapter 7 petition is filed.

8. What Happens When Both Spouses File Bankruptcy?

A joint bankruptcy filing introduces additional considerations.

When both spouses become debtors, the entireties interests and the claims against each spouse must be analyzed in the context of the joint proceeding.

The presence of joint creditors may permit administration of property that would otherwise be protected against creditors of either spouse individually.

The filing of a joint petition does not automatically consolidate the spouses' bankruptcy estates for every purpose. Substantive consolidation is a separate matter, and 11 U.S.C. § 302(b) authorizes the court to determine the extent to which the estates should be consolidated.

Accordingly, the decision whether one spouse or both should file is not merely a question of convenience or filing expense.

It can materially affect the treatment of property and creditors.

A married couple should not assume that filing together always provides greater protection than filing individually.

9. What Happens to Tenancy by the Entirety After Divorce?

Divorce is one of the most consequential events affecting entireties ownership.

Under Maryland law, an absolute divorce terminates the marital relationship upon which tenancy by the entirety depends.

Unless the property has been otherwise validly disposed of, the former spouses ordinarily become tenants in common.

That change can occur even though the original deed remains recorded in both spouses' names and no new deed has been executed.

The distinction is critical in bankruptcy.

Example: A divorce without a new deed

A husband and wife purchase their home while married, taking title as tenants by the entirety.

They later divorce. Their divorce judgment or marital settlement agreement leaves both parties with ownership interests, and neither executes a deed transferring the property to the other.

The former spouses may continue living in the same residence and paying the mortgage.

Nevertheless, the property is no longer held by the entirety merely because the original deed remains unchanged.

Their respective interests generally become those of tenants in common, subject to the actual terms of any applicable judgment, agreement, or other legally effective disposition.

If one former spouse subsequently files Chapter 7, that debtor's undivided ownership interest may be administered by the trustee, subject to applicable exemptions and other protections.

The former entireties exemption cannot be assumed to survive the divorce.

10. Separation Is Not the Same as Divorce

Physical separation ordinarily does not, by itself, terminate tenancy by the entirety.

Spouses may live in separate residences, maintain separate finances, and intend never to reconcile while remaining legally married.

If they still own qualifying property by the entirety, the form of ownership ordinarily continues unless lawfully terminated.

However, a property transfer, divorce judgment, or other legally effective event may alter the ownership interests.

A bankruptcy attorney should review the actual status of the marriage and any relevant court orders rather than relying solely on whether the spouses live together.

11. Can a Marital Settlement Agreement Change the Analysis?

Yes, but the language and legal effect of the agreement are important.

A settlement agreement may establish contractual rights between spouses without itself accomplishing every change in legal title that the parties contemplate.

A divorce judgment may also affect ownership independently of whether a subsequent deed is recorded.

Questions can arise when an original settlement agreement is amended, when a deed has not been delivered or recorded, or when the parties' conduct differs from their written obligations.

A bankruptcy trustee may examine not only the recorded deed but also the divorce decree, settlement agreements, amendments, and other documents affecting the debtor's property interests.

A debtor should therefore disclose the complete history of the ownership arrangement.

12. The New Maryland Homestead Exemption Provides Another Layer of Protection

Maryland's 2026 expansion of its bankruptcy residential-property exemption makes the entireties analysis even more important.

The statutory residential exemption and the entireties exemption are separate protections arising from different sources of law.

The residential exemption protects qualifying equity up to the applicable statutory amount.

The entireties exemption, recognized through 11 U.S.C. § 522(b)(3)(B) and Maryland property law, protects qualifying entireties interests to the extent they are immune from creditor process under state law.

The protections are not interchangeable, and they should not be assumed to combine automatically.

Where entireties protection is unavailable or limited because of joint debts, the statutory residential exemption may still be relevant to the debtor's equity.

Conversely, entireties protection may be especially valuable where the residence contains equity exceeding the statutory exemption.

The proper application depends on the ownership interests, claims, applicable exemptions, and the circumstances of the bankruptcy filing.

13. Why Paying Off Joint Debts Before Filing Requires Caution

A debtor who learns that joint indebtedness threatens entireties protection may be tempted to pay those obligations before filing.

That decision should not be made without evaluating the bankruptcy consequences.

Under 11 U.S.C. § 547, certain payments made before bankruptcy may constitute avoidable preferences.

Payments to insiders, including family members, can raise additional concerns. Transfers intended to hinder, delay, or defraud creditors may implicate fraudulent-transfer law.

Paying a legitimate joint creditor before filing is not automatically improper. But the source of the funds, timing, amount, identity of the creditor, and resulting financial circumstances matter.

The debtor should also avoid assuming that removing a spouse's name from an account necessarily eliminates an existing joint obligation.

Any proposed prebankruptcy debt restructuring should be evaluated before the transaction occurs.

14. Other Assets May Be Held by the Entirety

Although the family home is the most common example, tenancy by the entirety is not necessarily limited to real estate.

Maryland law recognizes entireties interests in certain personal property, including qualifying financial accounts and other assets, depending upon the form of ownership and applicable legal requirements.

The mere presence of both spouses' names on an account does not conclusively establish entireties ownership.

Account documentation, the parties' intentions, applicable presumptions, and the source and treatment of funds may matter.

Business interests and other forms of property require particularly careful analysis.

15. The Importance of Reviewing Every Debt and Every Ownership Document

A meaningful entireties analysis requires more than a copy of the deed.

The attorney should examine the nature of each significant obligation, including whether it is owed by one spouse or both, and whether an apparent joint obligation is legally enforceable against both.

Credit reports are useful but are not necessarily conclusive.

The examination should also address guarantees, tax obligations, judgments, prior property transfers, divorce proceedings, and other circumstances that may affect ownership or creditor rights.

A homeowner with substantial equity and exclusively individual unsecured debts may be an excellent candidate for Chapter 7.

Another homeowner with the same equity and the same total debt may face materially different risks because some obligations are jointly owed.

Conclusion

Tenancy by the entirety is among the most important protections available to married Maryland homeowners considering bankruptcy.

Its value lies in the distinction between debts owed by one spouse and debts owed by both.

The protection can preserve substantial home equity, but it can also be lost or limited through joint indebtedness, divorce, changes in title, or other legally significant events.

The central question is not simply how much the home is worth. It is who owns it, in what form, and which creditors have legally enforceable claims against that ownership interest.

Those questions should be answered before filing bankruptcy.

16. Can a Judgment Against One Spouse Affect Entireties Property?

A judgment against one spouse generally cannot be enforced against Maryland property held as tenants by the entirety.

However, the creditor may still pursue property owned individually by the judgment debtor. The creditor's rights may also change if the tenancy by the entirety terminates.

For example, divorce may convert the spouses' ownership into a tenancy in common, potentially exposing the debtor's resulting individual interest to collection.

A judgment creditor's rights following divorce require examination of the judgment, the timing of the divorce, the property's ownership history, and applicable lien law.

17. What If One Spouse Dies?

Tenancy by the entirety includes a right of survivorship.

When one spouse dies, the surviving spouse ordinarily becomes the sole owner of the property by operation of law.

This feature has significant bankruptcy implications.

Under 11 U.S.C. § 541(a)(5), certain property interests acquired or becoming available to a debtor within 180 days after filing, including certain interests arising through inheritance or property settlements, may enter the bankruptcy estate.

However, survivorship interests in entireties property require separate analysis. The debtor already possessed an interest in the property before the spouse's death.

The consequences of a spouse's death during bankruptcy depend on the nature of the ownership interest, the timing, the claims involved, and applicable law.

The death of a spouse should be reported promptly to bankruptcy counsel.

18. Practical Bankruptcy Planning for Married Homeowners

Before filing, counsel should determine how the residence is titled, whether the marriage remains legally intact, whether one or both spouses are liable for particular debts, and whether any judgments or liens affect the property.

The review should include the original deed, mortgage documents, credit agreements, judgments, divorce documents if applicable, and the debtor's complete creditor list.

Particular attention should be paid to obligations that may appear individual but are actually joint.

A small jointly incurred loan or credit account can create a complication that would not exist if all unsecured obligations belonged exclusively to the filing spouse.

The purpose of this investigation is not to conceal or rearrange assets improperly. It is to determine the legal consequences of existing ownership and obligations before filing.

Conclusion

Tenancy by the entirety can provide exceptionally valuable protection for Maryland homeowners considering bankruptcy.

Unlike a conventional exemption limited to a specified dollar amount, entireties protection may shield substantial home equity from creditors holding claims against only one spouse.

But the protection depends upon the continuing existence of the tenancy and the character of the debts.

Joint obligations, divorce, ownership changes, and the filing of a bankruptcy petition by one or both spouses can materially affect the result.

Maryland's expanded homestead exemption provides an additional reason to revisit the available options, but it does not eliminate the need for a careful entireties analysis.

For married homeowners, determining precisely who owns the property and who owes the debts should precede any decision to file Chapter 7.

Related Bankruptcy Cases and Authorities

Federal bankruptcy statutes

- 11 U.S.C. § 522(b)(3)(B) — Exemption of qualifying entireties and joint-tenancy interests to the extent protected under applicable nonbankruptcy law.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 363(h)–(j) — Sales of co-owned property, purchase rights, and distribution of proceeds.
- 11 U.S.C. § 302 — Joint bankruptcy cases involving spouses.
- 11 U.S.C. § 547 — Avoidable preferential transfers.

Maryland statutes

- Maryland Code, Courts and Judicial Proceedings § 11-504 — Maryland statutory exemptions.
- Maryland Code, Real Property § 2-117 — Requires express language to create a joint tenancy; it is not itself the source of the marital tenancy by the entirety presumption, which arises under Maryland common law.

Selected decisions

- Sumy v. Schlossberg, 777 F.2d 921 (4th Cir. 1985) — Holds that Maryland entireties property may be administered in an individual bankruptcy to the extent of joint claims against both spouses.
- Schlossberg v. Barney, 380 F.3d 174 (4th Cir. 2004) — Discusses Maryland entireties protection and limitations on a trustee's ability to reach exempt entireties property.
- *Williams v. Peyton (In re Williams)*, 104 F.3d 688 (4th Cir. 1997) — Addresses the administration of entireties property in connection with joint creditor claims.
- *Bruce v. Dyer*, 309 Md. 421, 524 A.2d 777 (1987) — Explains the nature and incidents of tenancy-by-the-entirety ownership under Maryland law.
- *State v. Friedman*, 283 Md. 701, 393 A.2d 1356 (1978) — Recognizes the distinction between creditors of one spouse and creditors holding claims against both spouses.
- *Cordova v. Mayer (In re Cordova)*, 73 F.3d 38 (4th Cir. 1996) — Addresses the effect of divorce upon entireties ownership in bankruptcy.

Federal statutes

Maryland law

- Maryland common law governing tenancy by the entirety and the effect of absolute divorce on ownership.
- *Greenblatt v. Ford*, 638 F.2d 14 (4th Cir. 1981) — Addresses Maryland tenancy-by-the-entirety property and its protection from individual creditors.
- *Beall v. Beall*, 291 Md. 224, 434 A.2d 1015 (1981) — Examines the nature of tenancy-by-the-entirety ownership under Maryland law.
- *In re Ford*, 3 B.R. 559 (Bankr. D. Md. 1980), aff'd, 638 F.2d 14 (4th Cir. 1981) — Addresses the treatment of Maryland entireties property in bankruptcy.

The Automatic Stay in Bankruptcy: What Creditors Must Stop, What They Can Continue, and What Happens When They Violate It

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By Alan J. Belsky, Attorney at Law

Bankruptcy Protection Begins Before the Discharge

One of the most immediate and valuable protections available to a person filing bankruptcy is the *automatic stay*. Under 11 U.S.C. § 362, the filing of a bankruptcy petition ordinarily imposes an immediate legal prohibition against most efforts to collect debts, enforce judgments, or obtain possession of property belonging to the debtor or bankruptcy estate.

The protection generally arises automatically, without a hearing, a separate motion, or an order specifically directing creditors to stop collection activity.

It is not necessary to wait until the bankruptcy court grants a discharge.

The automatic stay and the bankruptcy discharge serve different purposes. The stay generally protects the debtor and estate during the bankruptcy proceeding. The discharge ordinarily eliminates personal liability for qualifying debts and replaces the stay with a continuing discharge injunction against collection of those debts.

The distinction matters because the stay is temporary, contains important exceptions, and may be modified or terminated before the bankruptcy case concludes.

1. What Collection Activities Does the Automatic Stay Prohibit?

Section 362(a) broadly prohibits numerous actions against the debtor, the debtor's property, and property of the bankruptcy estate.

Among the activities ordinarily prohibited are:

- Commencing or continuing lawsuits to recover prepetition debts.
- Enforcing prepetition judgments.
- Garnishing wages to collect prepetition obligations.
- Continuing bank account attachments or levies.
- Repossessing vehicles or other collateral.
- Conducting foreclosure sales.
- Creating, perfecting, or enforcing certain liens.
- Demanding payment of prepetition debts through prohibited collection activity.
- Exercising control over estate property in circumstances prohibited by the statute.

The stay generally applies to creditors whether or not they agree with the bankruptcy filing.

However, the particular statutory subsection matters. Some conduct may be prohibited by one provision but not another, and certain exceptions permit actions that might otherwise appear to be stayed.

2. Does the Creditor Have to Receive Notice Before the Stay Takes Effect?

Ordinarily, no.

The automatic stay arises by operation of law when the petition is filed, subject to statutory exceptions and limitations.

A creditor's lack of notice does not necessarily mean its postpetition action was legally permissible. But knowledge of the bankruptcy is particularly important when determining whether a violation was willful and whether damages are available.

For that reason, prompt and accurate notice to creditors is essential.

The bankruptcy petition and schedules should identify creditors using sufficient information to permit effective notice. Where a garnishment, foreclosure, repossession, or other collection proceeding is pending, counsel may also need to notify the creditor's attorney, the sheriff, the employer, or another participant directly.

A debtor should not assume that every collection participant will immediately learn of the bankruptcy through ordinary court notices.

3. Wage Garnishments: What Happens After Filing?

Wage garnishment is one of the most common reasons individuals seek bankruptcy protection.

In Maryland, an unsecured judgment creditor may obtain a wage garnishment under Maryland Rule 2-646, subject to applicable statutory protections.

When the employee files bankruptcy, the automatic stay ordinarily prohibits further collection of the prepetition judgment through garnishment.

The employer's role

Once the employer receives adequate notice of the bankruptcy, continued withholding for a stayed prepetition judgment can create serious problems.

But the employer may be acting under an existing court order, and prompt communication with the creditor and garnishment court may be necessary to terminate or suspend the process properly.

The debtor's attorney should identify the garnishment proceeding, provide notice, and determine whether additional action is required.

What about wages already garnished?

Money withheld before filing presents a different question.

The debtor may have rights to recover some funds, depending on when the garnishment occurred, when the creditor acquired an interest in the funds, whether the money was transferred, and whether exemptions or avoidance provisions apply.

A transfer made before bankruptcy may be recoverable as a preference under 11 U.S.C. § 547 if the statutory requirements are satisfied.

Section 522(h) may permit a debtor to avoid certain transfers that the trustee does not pursue, subject to specific conditions.

Consequently, it is important to determine exactly when wages were earned, withheld, transferred, and received.

4. Bank Account Garnishments and Frozen Accounts

Bank account attachments can be particularly disruptive because they may deprive the debtor of funds needed for housing, food, transportation, and other necessities.

Filing bankruptcy ordinarily stays further efforts to enforce a prepetition judgment against the debtor's bank account.

But filing does not invariably produce an immediate release of every restraint or an automatic return of all funds.

The legal consequences depend on whether the funds remain property of the debtor or bankruptcy estate, whether the creditor acquired a valid lien, whether the funds are exempt, and whether turnover or avoidance relief is appropriate.

A bank may also assert setoff rights or maintain restrictions while determining its obligations under bankruptcy law.

The Supreme Court's decision in *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16 (1995), illustrates that a temporary administrative hold associated with a claimed setoff is not necessarily equivalent to an impermissible setoff.

A debtor whose account remains frozen after filing may require prompt legal intervention.

5. Foreclosure: What the Automatic Stay Can and Cannot Do

The automatic stay generally stops a foreclosure sale scheduled to occur after a bankruptcy petition is filed, assuming the stay applies and has not been terminated.

This can provide immediate protection to a homeowner facing the loss of a residence.

But the stay does not eliminate the mortgage, cure arrears, or permanently prevent foreclosure.

A mortgage lender may seek relief from the stay under § 362(d), particularly when payments are not being made or the creditor's interest lacks adequate protection.

Chapter 7 versus Chapter 13

Chapter 7 ordinarily provides temporary protection from foreclosure but does not furnish a long-term repayment mechanism for curing mortgage arrears.

Chapter 13 may allow an eligible debtor to cure qualifying arrears through a repayment plan while maintaining ongoing mortgage payments.

The distinction can determine which chapter is appropriate.

A homeowner whose mortgage is current but who has substantial unsecured debt may benefit greatly from Chapter 7, particularly under Maryland's expanded residential exemption.

A homeowner who is seriously delinquent may need Chapter 13 or another arrangement to preserve the property.

Foreclosure proceedings already completed

Timing is critical.

If a foreclosure sale has already occurred, filing bankruptcy afterward may not restore ownership or undo rights that became fixed under applicable state law.

Maryland foreclosure procedures contain several legally significant stages, and the effect of filing must be evaluated in relation to those stages.

A debtor facing an imminent sale should seek advice before the sale occurs, rather than assuming bankruptcy can reverse it afterward.

6. Vehicle Repossessions

The automatic stay generally prevents a secured creditor from repossessing a vehicle after the bankruptcy filing when the stay applies.

However, the filing does not extinguish the lender's lien or necessarily permit the debtor to retain the vehicle without addressing the secured debt.

A creditor may request relief from the stay to repossess collateral.

What if the car was repossessed before bankruptcy?

The debtor's rights depend on state law, the repossession agreement, the timing, and the status of the vehicle.

The Supreme Court's decision in *City of Chicago v. Fulton*, 592 U.S. 154 (2021), held that merely retaining possession of property seized before bankruptcy does not, by itself, violate § 362(a)(3).

The decision does not eliminate other possible obligations or remedies, including turnover proceedings where applicable.

A debtor should therefore not assume that filing bankruptcy automatically compels a lender to return a previously repossessed vehicle.

The right to recover the vehicle and the procedure for obtaining its return require separate analysis.

7. Collection Lawsuits and Judgments

The automatic stay generally suspends pending lawsuits against the debtor seeking recovery of prepetition debts.

This includes ordinary collection actions involving credit cards, personal loans, medical bills, and similar obligations.

The stay ordinarily prevents further proceedings to obtain or enforce a money judgment against the debtor.

However, bankruptcy does not automatically erase a judgment lien that attached to property before filing. Depending on the circumstances, lien avoidance under 11 U.S.C. § 522(f) may be available.

A creditor's claim may also survive bankruptcy if the debt falls within an exception to discharge.

What about lawsuits brought by the debtor?

The automatic stay generally does not prevent a debtor from pursuing a lawsuit the debtor initiated.

However, the lawsuit may become property of the bankruptcy estate, and the trustee may acquire authority over its prosecution or settlement.

Counterclaims against the debtor can raise separate stay issues.

This is particularly important when a debtor has a pending personal injury claim, employment claim, or other potentially valuable cause of action.

8. What Collection Activities Can Continue Despite Bankruptcy?

The automatic stay contains numerous statutory exceptions under § 362(b).

Important examples include certain criminal proceedings, specified family-law matters, governmental regulatory actions, and tax-related activities.

Criminal proceedings

The commencement or continuation of a criminal proceeding against the debtor is generally excepted from the automatic stay.

Bankruptcy is not a means of preventing criminal prosecution merely because the alleged conduct also involves a financial obligation.

Domestic relations matters

Certain proceedings concerning paternity, divorce, child custody, domestic support, and domestic violence may continue.

Collection of domestic support obligations from property that is not property of the bankruptcy estate is also subject to specific statutory exceptions.

Section 362(b)(2)(C) separately permits qualifying withholding of income for domestic support under an order or statute, even when that income is property of the estate. The exception for a divorce proceeding does not authorize division of estate property without addressing the stay. Support enforcement and property division must therefore be analyzed separately.

The treatment of support obligations differs from ordinary unsecured debts, and those obligations generally are not discharged.

Governmental regulatory actions

Government agencies may continue certain proceedings to enforce police or regulatory powers.

For example, bankruptcy generally does not prevent a governmental agency from pursuing legitimate regulatory enforcement merely because the proceeding may ultimately involve financial consequences.

However, the exception for regulatory proceedings does not provide unlimited authority to enforce money judgments.

Tax matters

Certain tax audits, assessments, notices of deficiency, and demands for tax returns may continue notwithstanding bankruptcy.

Actual collection and enforcement actions require separate analysis.

A debtor should not assume that all IRS activity must cease immediately upon filing.

9. Repeat Bankruptcy Filings: When the Stay Is Limited or Never Takes Effect

Special rules apply when a debtor has had bankruptcy cases dismissed within the preceding year.

Under § 362(c)(3), if one qualifying case was pending and dismissed during the preceding year, the automatic stay generally terminates with respect to the debtor on the thirtieth day after the new filing unless the court extends it.

An extension requires a timely motion, notice, and a hearing completed before expiration of the thirty-day period. The statute imposes good-faith requirements.

Courts have disagreed about the extent to which this termination affects property of the bankruptcy estate, making the governing circuit and bankruptcy decisions important.

Under § 362(c)(4), when two or more qualifying cases were pending and dismissed during the preceding year, the automatic stay generally does not take effect upon filing the new petition.

A party in interest may seek an order imposing the stay, but the request must be made within thirty days and must satisfy the applicable statutory requirements.

These deadlines are particularly important for debtors facing imminent foreclosure or repossession.

Simply filing another bankruptcy petition may provide little or no protection.

10. Relief From the Automatic Stay

A creditor may request permission from the bankruptcy court to proceed with an action otherwise prohibited by the stay.

This is called a motion for relief from stay.

Under § 362(d), relief may be granted for cause, including lack of adequate protection, or under other specified circumstances involving collateral and the debtor's equity.

A mortgage lender may seek relief when payments are not being made. A vehicle lender may seek relief when collateral is uninsured, depreciating, or otherwise inadequately protected.

A creditor involved in a pending personal injury lawsuit may also request relief to permit litigation to continue, sometimes solely to establish liability and recover available insurance proceeds.

Relief limited to insurance proceeds

Where the debtor has applicable liability insurance, a court may permit an underlying lawsuit to proceed while restricting recovery to available insurance.

Such relief can allow an injured claimant to pursue compensation without exposing the debtor's personal assets to collection.

The terms of the order matter. Permission to establish liability is not necessarily permission to execute against the debtor personally.

This subject warrants a separate article addressing motions for relief from stay for insurance purposes.

11. What Constitutes a Willful Violation of the Automatic Stay?

Under § 362(k)(1), an individual injured by a willful violation of the automatic stay is entitled to recover actual damages, including costs and attorney's fees, and may recover punitive damages in appropriate circumstances.

A creditor need not necessarily intend to violate bankruptcy law.

Generally, knowledge of the bankruptcy and intentional commission of an act that violates the stay can support a finding of willfulness, even if the creditor mistakenly believes its conduct is permissible.

The precise standard and available remedies depend on governing precedent.

Examples of potentially actionable conduct include knowingly continuing prohibited wage garnishment, attempting to collect a stayed debt through repeated demands, or proceeding with enforcement after receiving notice of the bankruptcy.

An inadvertent act committed before the creditor learns of the filing raises different issues from continued collection after actual notice.

12. Damages for Violating the Stay

A debtor injured by a willful stay violation may seek compensation for provable losses.

Depending on the circumstances, recoverable damages may include improperly collected funds, lost wages, bank charges, transportation expenses, other financial losses, and reasonable attorney's fees.

Emotional distress damages may also be available when supported by sufficient evidence under applicable law.

Punitive damages require additional justification and are not automatic.

The debtor should preserve collection letters, account statements, call records, voicemail messages, employer communications, and other evidence establishing the violation and resulting harm.

A creditor's prompt corrective action may affect the practical resolution and the damages analysis, although it does not necessarily erase an earlier violation.

13. How Long Does the Automatic Stay Last?

The duration depends on the nature of the property or conduct involved.

Under § 362(c)(1), the stay protecting property of the estate generally continues until the property is no longer estate property.

Under § 362(c)(2), the stay against other covered acts ordinarily continues until the case is closed, dismissed, or the debtor receives or is denied a discharge, whichever occurs first.

The stay can terminate earlier under other statutory provisions or through court-ordered relief.

When a discharge is granted, § 524(a) ordinarily prohibits attempts to collect discharged debts as personal liabilities.

The discharge injunction is separate from the automatic stay and has its own enforcement standards.

In *Taggart v. Lorenzen*, 587 U.S. 554 (2019), the Supreme Court addressed the standard for civil contempt for violating a discharge order.

14. Is an Action Taken in Violation of the Stay Automatically Invalid?

Courts have used different terminology and approaches when describing actions taken in violation of the automatic stay, including whether such acts are void or voidable.

The distinction can be important when a creditor conducts a foreclosure sale, obtains a judgment, or takes other action without first obtaining relief.

Section 362(d) expressly permits a bankruptcy court to annul the stay in appropriate circumstances. Annulment can operate retroactively.

Consequently, an action taken during the stay should not be assumed either permanently effective or incapable of being validated.

Prompt judicial relief may be necessary to establish the parties' rights.

15. Why Emergency Bankruptcy Filings Require Careful Planning

An impending foreclosure, garnishment, or repossession may create pressure to file immediately.

But a hurried petition can create serious problems if the debtor has undisclosed assets, prior dismissed cases, substantial nonexempt equity, or other circumstances that have not been evaluated.

A bankruptcy petition may stop one collection problem while exposing the debtor to another.

For example, a homeowner facing wage garnishment might file Chapter 7 to obtain immediate protection, only to discover that the trustee can administer valuable nonexempt property.

The automatic stay is powerful, but it is not a substitute for evaluating the entire bankruptcy case.

Conclusion

The automatic stay is one of the Bankruptcy Code's most important protections.

It can stop wage garnishments, interrupt collection lawsuits, prevent many repossessions, and temporarily halt foreclosure proceedings.

But it is not absolute. Some proceedings are excepted, creditors may obtain relief, repeat filings may receive limited protection, and the stay does not eliminate secured liens or guarantee a discharge.

The consequences of violating the stay can be substantial, including liability for damages and attorney's fees.

For debtors and creditors alike, understanding precisely when the stay begins, what it prohibits, and when it terminates is essential.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 362 — Automatic stay, exceptions, duration, relief, and damages.
- 11 U.S.C. § 524 — Effect of discharge and discharge injunction.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 542 — Turnover of estate property.
- 11 U.S.C. § 547 — Preferential transfers.
- 11 U.S.C. § 522(f) — Avoidance of certain liens impairing exemptions.

Maryland procedure

- Maryland Rule 2-646 — Wage garnishment proceedings.

Selected decisions

- *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16 (1995) — Addresses temporary administrative holds and setoff rights in bankruptcy.
- *City of Chicago v. Fulton*, 592 U.S. 154 (2021) — Holds that mere retention of property seized before bankruptcy does not itself violate § 362(a)(3).
- *United States v. Whiting Pools, Inc.*, 462 U.S. 198 (1983) — Addresses estate property and turnover of property seized before bankruptcy.
- *Taggart v. Lorenzen*, 587 U.S. 554 (2019) — Establishes the civil contempt standard for violation of a discharge injunction.
- *In re Kestell*, 99 F.3d 146 (4th Cir. 1996) — Addresses abuse of the bankruptcy process in the context of domestic relations obligations.

The Chapter 7 Means Test in Maryland: How Income, Household Size, and Allowable Expenses Determine Eligibility

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By Alan J. Belsky, Attorney at Law

Earning Too Much to File Chapter 7? Not Necessarily.

One of the most common misconceptions about Chapter 7 bankruptcy is that a person must have little or no income to qualify. In fact, many employed individuals, including some with relatively substantial earnings, may qualify for Chapter 7 relief.

The Bankruptcy Code does not establish a single maximum salary above which Chapter 7 is prohibited. Instead, it employs a means-testing system intended to identify certain consumer bankruptcy filings that may constitute an abuse of Chapter 7.

The analysis considers income received during a defined period, household size, allowable expenses, certain debt obligations, and other statutory factors.

A debtor whose income exceeds Maryland's median income may nevertheless qualify for Chapter 7. Conversely, passing the means test does not guarantee that a case is immune from dismissal for abuse.

Understanding the distinction can prevent individuals from unnecessarily ruling out bankruptcy relief.

1. What Is the Chapter 7 Means Test?

The means test was introduced through the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.

Its principal statutory authority is 11 U.S.C. § 707(b), which governs dismissal or conversion of certain Chapter 7 cases involving primarily consumer debts.

The means test attempts to determine whether the debtor has sufficient presumed repayment capacity to make Chapter 7 relief potentially abusive.

It is not simply a comparison between gross income and monthly household bills.

The statutory calculation uses defined income measures, standardized expense allowances, actual expenses permitted by law, and deductions for certain secured and priority debts.

The calculation ordinarily appears on Official Forms 122A-1 and, when required, 122A-2.

2. The First Question: Are Your Debts Primarily Consumer Debts?

The means-test presumption under § 707(b) generally applies to individual debtors whose debts are primarily consumer debts.

The Bankruptcy Code defines consumer debt in 11 U.S.C. § 101(8) as debt incurred primarily for a personal, family, or household purpose.

Credit card purchases for ordinary household needs, personal vehicle loans, and many residential mortgages are common examples.

Business-related obligations may be nonconsumer debts.

The distinction matters because an individual whose debts are primarily nonconsumer debts generally is not subject to dismissal under § 707(b)'s means-test framework.

Business debt and personal guarantees

A debtor who operated a business may have substantial personal liability arising from business loans, commercial leases, vendor accounts, or guarantees.

Those obligations may be nonconsumer debts depending on the purpose for which they were incurred.

A personal guarantee does not automatically transform a business debt into consumer debt.

The characterization of debt requires an examination of the underlying transaction and applicable case law.

3. Current Monthly Income: The Six-Month Lookback

The means test begins with *current monthly income*, a statutory term defined principally in 11 U.S.C. § 101(10A).

Despite its name, current monthly income is ordinarily not the debtor's income during the month the petition is filed.

For most debtors, the calculation averages qualifying income received during the six complete calendar months ending on the last day of the month before filing.

Example

A debtor files Chapter 7 on October 24, 2026.

The ordinary six-month measurement period is April 1 through September 30, 2026.

Income received in October generally is not included in that historical calculation.

A debtor filing on November 1, however, would ordinarily use May 1 through October 31.

A difference of only a few days in filing date can therefore change the income calculation substantially.

The statutory calculation generally concerns income received, rather than income earned but not yet paid, subject to the applicable rules.

4. What Income Must Be Included?

Current monthly income generally includes income from all sources received by the debtor during the relevant period, subject to statutory exclusions.

Depending on the circumstances, included income may consist of wages, salary, commissions, bonuses, business income, rental income, pensions, and regular contributions toward household expenses from others.

For married debtors, the treatment of a nonfiling spouse's income requires particular care.

Income figures used for means testing may differ from taxable income, adjusted gross income, or the amount deposited into a checking account after payroll deductions.

A debtor should not assume that the number appearing on a tax return is the correct means-test figure.

5. Social Security Benefits Are Generally Excluded

The definition of current monthly income excludes benefits received under the Social Security Act.

This exclusion is particularly important for retirees and disabled individuals whose household resources include Social Security retirement or disability benefits.

For example, a debtor receiving Social Security Disability Insurance benefits may have funds available for living expenses without those benefits being included in statutory current monthly income.

However, not every payment described informally as disability income is necessarily a Social Security Act benefit.

Private disability insurance, employer disability payments, veterans' benefits, workers' compensation, and other income sources require separate statutory analysis.

The Bankruptcy Code also contains specific exclusions for certain payments connected to military service and veterans' benefits.

The classification of each income source should be verified rather than inferred from its description.

6. Maryland Median Income: The First Screening Test

After calculating current monthly income, the debtor generally annualizes the figure by multiplying it by twelve.

That amount is compared with the applicable median family income for Maryland and the relevant household size.

The median-income figures are published by the United States Trustee Program and periodically adjusted.

The figures applicable to a bankruptcy case depend on the petition date.

If the debtor's annualized current monthly income does not exceed the applicable median, the statutory presumption of abuse under the means test generally does not arise.

That does not necessarily resolve every eligibility issue.

A debtor may still face scrutiny under other provisions of § 707(b), including the totality of the circumstances or bad-faith grounds.

Why household size matters

Median-income thresholds increase with household size.

A debtor living alone may be above the applicable median while another debtor with identical income and a larger qualifying household may be below it.

Determining household size is therefore a substantive legal question, not merely an administrative detail.

7. Adult Children, Relatives, and Shared Households

The Bankruptcy Code does not provide a universally applicable, comprehensive definition of household size for every means-test circumstance.

Courts have considered different approaches, including household membership, economic interdependence, and financial dependency.

An adult child who lives in the debtor's home but pays all personal expenses may present a different case from an adult child whose housing, food, transportation, and other necessities are substantially paid by the debtor.

Likewise, an elderly parent or another relative may be financially dependent upon the debtor even though that person is not a minor child.

The number of people living under one roof does not always determine the answer.

Nor does the number of dependents claimed on a federal income tax return necessarily control the bankruptcy analysis.

The proper approach must account for governing precedent and the debtor's actual financial arrangements.

This subject merits a separate article because household composition can affect both the median-income comparison and the calculation of allowable expenses.

8. What Happens If Income Exceeds the Maryland Median?

Being above the median does not automatically disqualify a debtor from Chapter 7.

Instead, most above-median debtors subject to the means test must complete the additional calculations required by Official Form 122A-2.

The calculation begins with current monthly income and subtracts allowable expenses and other statutory deductions.

The resulting figure is used to determine whether the presumption of abuse arises under § 707(b)(2).

The deductions do not necessarily correspond to the debtor's actual monthly expenditures.

Some are based on national or local standards, while others depend on documented actual expenses or statutory conditions.

9. National and Local Expense Standards

The means test incorporates expense standards associated with the Internal Revenue Service, subject to the Bankruptcy Code's specific provisions.

National Standards address certain categories such as food, clothing, and other necessary living expenses.

Local Standards address housing, utilities, and transportation, with amounts varying according to geographic location and household circumstances.

Other expenses may be allowed based on actual costs and statutory requirements.

The allowable deduction for a particular expense may differ from the amount the debtor actually spends.

For example, a debtor's unusually high discretionary spending does not necessarily become deductible merely because the expense appears in the household budget.

Conversely, a debtor may qualify for a standardized allowance that differs from the amount actually paid, depending on the governing statutory provision and judicial interpretation.

In Lynch v. Jackson, 853 F.3d 116 (4th Cir. 2017), the Fourth Circuit held that a debtor may use the full applicable IRS National or Local Standard for a category in which the debtor incurs an expense, even if actual spending is lower. The expense category must apply; Ransom bars the vehicle ownership allowance without a qualifying loan or lease cost. Other Necessary Expenses remain governed by actual-expense requirements.

10. Secured Debt Payments

The means test permits certain deductions relating to secured debt obligations.

Mortgage and vehicle loan payments can materially affect the calculation.

The statutory secured-debt deduction generally considers amounts contractually due during the sixty months following the petition date, subject to the applicable provisions.

The treatment of payments on collateral the debtor intends to surrender can present legal questions.

Similarly, the distinction between vehicle ownership expenses and operating expenses has generated significant litigation.

In *Ransom v. FIA Card Services, N.A.*, 562 U.S. 61 (2011), the Supreme Court held that a debtor who owned a vehicle free of loan or lease payments could not claim the vehicle ownership-cost allowance merely because the debtor owned a car.

The decision illustrates why means-test deductions cannot be determined solely by reference to the debtor's actual household budget.

11. Taxes, Insurance, and Other Deductions

Above-median debtors may be entitled to deductions for qualifying taxes, mandatory payroll deductions, insurance, healthcare expenses, childcare, and other specified expenditures.

The availability and amount of each deduction depend on the statutory language and applicable rules.

Actual tax liability is not necessarily the same as payroll withholding.

A debtor who deliberately overwithholds income taxes may receive a substantial refund, but the excess withholding does not automatically qualify as a necessary tax expense.

Similarly, voluntary retirement contributions, retirement loan repayments, and other payroll deductions may receive different treatment depending on the applicable provision and chapter.

Careful review of pay statements and supporting documents is essential.

12. Priority Debts and Other Statutory Deductions

Certain priority obligations, including qualifying tax debts and domestic support obligations, may affect the means-test calculation.

The Bankruptcy Code permits specified deductions for payments on qualifying priority claims, generally calculated over a sixty-month period.

A debtor with significant priority tax obligations may therefore present a different means-test result from a debtor with identical income and ordinary unsecured credit card debt.

But the mere existence of a debt does not establish that it qualifies for a particular deduction.

Its legal classification must be determined.

13. How the Presumption of Abuse Is Calculated

After allowable deductions are applied, the means test calculates a monthly disposable-income figure and multiplies it by sixty.

Under § 707(b)(2)(A)(i), the resulting amount is compared with statutory thresholds, including a percentage of qualifying nonpriority unsecured claims.

Those thresholds are adjusted periodically under 11 U.S.C. § 104.

The calculation can result in a presumption of abuse, but it is not a final judicial determination that Chapter 7 relief must be denied.

The debtor may have grounds to rebut the presumption, and procedural requirements govern how abuse issues are raised and resolved.

The appropriate thresholds must be obtained from the official figures applicable to the filing date.

14. Special Circumstances: Rebutting the Presumption

Section 707(b)(2)(B) permits a debtor to rebut the presumption of abuse by demonstrating special circumstances that justify additional expenses or adjustments to current monthly income.

The statute identifies examples such as a serious medical condition or a call or order to active duty in the Armed Forces.

The examples are not necessarily exhaustive.

However, the debtor must satisfy demanding documentation and procedural requirements.

The debtor must itemize the additional expenses or income adjustments, provide documentation, and explain why the circumstances justify the adjustment.

The debtor must also show that no reasonable alternative exists, attest under oath to the accuracy of the supporting information, and establish that the justified adjustments reduce the statutory calculation below the applicable threshold. A special circumstance is not established merely by documenting an expense.

A general assertion that the debtor cannot afford to repay creditors is not enough.

15. What If Income Has Recently Declined?

The historical nature of current monthly income can produce misleading results when a debtor's financial circumstances have changed.

A debtor may have earned substantial income during the six-month measurement period but subsequently lost employment, experienced reduced hours, or suffered a significant decline in business income.

The means test may initially reflect income that is no longer being received.

Depending on the circumstances, the debtor may need to consider filing timing, the special-circumstances provisions, and the broader abuse analysis.

A temporary decline in income and a permanent loss of employment may warrant different treatment.

A debtor should not assume that a historical above-median calculation conclusively prevents Chapter 7 relief.

16. Married Debtors and the Nonfiling Spouse

Marriage does not require both spouses to file bankruptcy.

However, when only one spouse files, the means test may require consideration of income received by the nonfiling spouse.

The Bankruptcy Code generally includes amounts regularly paid by another person toward the household expenses of the debtor or the debtor's dependents.

Official means-test forms also address the income of a nonfiling spouse and permit a marital adjustment in appropriate circumstances.

The marital adjustment is not a blanket exclusion of the spouse's earnings.

Rather, it generally concerns amounts not regularly contributed toward qualifying household expenses.

Documentation and accurate allocation of expenditures are important.

The analysis becomes especially complicated when spouses are separated, maintain separate finances, or share a residence without functioning as a single economic household.

17. Does Passing the Means Test Guarantee Chapter 7 Relief?

No.

Section 707(b)(3) permits consideration of whether a debtor filed in bad faith or whether the totality of the debtor's financial circumstances demonstrates abuse.

A debtor may pass the mechanical means test but nevertheless face an abuse challenge.

For example, a debtor with substantial stable income, unusually low necessary expenses, and significant ability to repay creditors may warrant further analysis even if the statutory presumption does not arise.

The means test is therefore an important screening mechanism, not an absolute guarantee.

18. Timing a Bankruptcy Filing

Because current monthly income is based on a rolling six-month period, filing date can materially affect eligibility.

A debtor who recently received a large bonus, substantial overtime, severance payment, or other income may obtain a different means-test result by filing in a later month.

But delaying bankruptcy also carries risks.

Creditors may continue garnishment, foreclosure, repossession, or other lawful collection activity until bankruptcy protection begins.

The debtor's assets, exemptions, tax obligations, and recent transfers may also change during the waiting period.

Appropriate timing requires consideration of the entire financial picture, not merely the means-test result.

19. Why the Means Test Should Not Be Completed in Isolation

The means test is only one component of Chapter 7 planning.

A debtor may qualify financially but own substantial nonexempt property that could be liquidated.

Another debtor may have significant income but little nonexempt property and qualify for Chapter 7 after applying allowable deductions.

A third debtor may have debts that are primarily nonconsumer obligations and therefore fall outside the ordinary § 707(b) means-test presumption.

These distinctions explain why two individuals with identical salaries may receive very different bankruptcy recommendations.

The proper analysis includes debt classification, household composition, property ownership, exemptions, secured obligations, priority claims, and the debtor's present and anticipated financial circumstances.

Conclusion

The Chapter 7 means test is more complex than a simple income ceiling.

It uses a statutory six-month income calculation, compares annualized income with Maryland median-income figures, and, when necessary, applies detailed expense deductions and additional tests.

A debtor who earns more than the Maryland median may still qualify for Chapter 7. A debtor who passes the means test may nevertheless face other bankruptcy concerns.

The most important lesson is that Chapter 7 eligibility should not be determined by salary alone.

Before ruling out Chapter 7 because of income, the debtor's complete financial circumstances should be evaluated under the applicable bankruptcy rules.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 101(8) — Definition of consumer debt.
- 11 U.S.C. § 101(10A) — Definition of current monthly income.
- 11 U.S.C. § 104 — Periodic adjustment of statutory dollar amounts.
- 11 U.S.C. § 707(b) — Dismissal or conversion of abusive Chapter 7 consumer cases.
- 11 U.S.C. § 1325(b) — Disposable-income provisions relevant to Chapter 13.

Official forms and administrative authorities

- United States Trustee Program — Means Testing — Official median-income figures and expense standards.
- United States Courts — Bankruptcy Forms — Official Forms 122A-1 and 122A-2.

Selected decisions

- *Ransom v. FIA Card Services, N.A.*, 562 U.S. 61 (2011) — Explains the limits on claiming vehicle ownership-cost deductions.
- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Permits consideration of known or virtually certain changes in income or expenses when calculating projected disposable income in Chapter 13.
- *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365 (2007) — Addresses bad-faith conduct and limitations on conversion between bankruptcy chapters.
- *In re Kestell*, 99 F.3d 146 (4th Cir. 1996) — Discusses abuse of bankruptcy relief and the significance of the debtor's conduct.
- *In re Calhoun*, 650 F.3d 338 (4th Cir. 2011) — Addresses Chapter 7 abuse analysis and the statutory framework governing dismissal.

Household Size in Bankruptcy: Adult Children, Elderly Parents, Separated Spouses, and Shared Living Arrangements

BELSKY BANKRUPTCY LEGAL LIBRARY | CHAPTER 7 ELIGIBILITY AND MEANS TESTING

By Alan J. Belsky, Attorney at Law

Who Counts as a Member of Your Household?

Determining household size in bankruptcy can be surprisingly complicated. A married couple with two minor children ordinarily presents a straightforward case. But what about an unmarried debtor supporting an elderly parent, a divorced person living with adult children, or spouses who remain married but maintain separate households?

The answer can significantly affect Chapter 7 eligibility.

Household size determines which median-income threshold applies under the bankruptcy means test. It can also affect standardized living-expense allowances and the assessment of a debtor's actual household expenses.

The Bankruptcy Code does not establish a single comprehensive definition of household size applicable to every bankruptcy calculation. Courts have developed different approaches, sometimes reaching different conclusions on similar facts.

Consequently, the number of people residing at a particular address does not always establish the number who should be included in the bankruptcy household.

1. Why Household Size Matters

Under 11 U.S.C. § 707(b)(7), an individual debtor whose annualized current monthly income does not exceed the applicable state median income for the relevant family size generally is not subject to the presumption of abuse under § 707(b)(2).

Median-income thresholds increase with household size.

A debtor whose income exceeds the median for a household of one may fall below the median for a household of three.

For above-median debtors, household size can also affect the allowable amounts for food, clothing, housing, utilities, and other expenses.

Thus, household size may influence both the initial median-income comparison and the subsequent means-test calculation.

However, increasing household size does not necessarily increase every allowable deduction, and the appropriate household count may vary according to the particular form or legal issue involved.

2. Three Approaches Courts Have Used

Courts have generally discussed three approaches to determining household size: the heads-on-beds approach, the income-tax-dependent approach, and the economic-unit approach.

These labels describe judicial approaches rather than three alternatives freely available for debtors to choose.

The heads-on-beds approach

Under this approach, household size generally reflects the number of people who regularly reside in the home.

Its advantage is relative simplicity.

Its weakness is that it may include individuals who share an address but maintain substantially independent finances.

For example, a debtor who rents a bedroom to an unrelated tenant ordinarily should not assume that the tenant automatically qualifies as part of the debtor's bankruptcy household merely because they occupy the same residence.

The income-tax-dependent approach

This approach looks to the individuals whom the debtor may claim as dependents under applicable federal tax rules.

It provides a relatively objective measure of financial dependency.

However, bankruptcy household composition and federal income-tax dependency are not necessarily identical.

A debtor may provide meaningful support to a relative who does not qualify as a tax dependent. Conversely, a person claimed on a tax return may not reside with the debtor throughout the relevant period.

The economic-unit approach

The economic-unit approach examines the degree to which individuals function together financially.

Relevant factors may include shared housing, food, utilities, transportation, household purchases, and the extent to which one person supports another.

This approach recognizes that a household is often an economic arrangement rather than simply a collection of people living at the same address.

Its disadvantage is that it requires a fact-intensive examination.

3. The Fourth Circuit's Decision in *Johnson v. Zimmer*

For Maryland bankruptcy cases, an important decision is *Johnson v. Zimmer*, 686 F.3d 224 (4th Cir. 2012).

The Fourth Circuit addressed household size in a Chapter 13 case and approved the economic-unit approach.

The court rejected a rigid method based solely on physical residence or tax dependency.

Instead, the analysis considers whether individuals operate as a financially integrated household.

Although *Johnson* arose in Chapter 13, its reasoning is highly relevant to household-size questions arising in Chapter 7 means testing.

The decision does not establish that every person living in a debtor's home must be counted. Nor does it require that every household member be completely financially dependent on the debtor.

The inquiry focuses on the actual economic relationship among the individuals.

4. Adult Children Living With a Parent

Adult children present one of the most common household-size questions.

An adult child may live with a parent while attending college, seeking employment, recovering from financial difficulties, or saving money for independent housing.

The child's age alone does not resolve whether the child belongs in the bankruptcy household.

Example: Two adult children living at home

A divorced debtor lives with two adult children.

The debtor pays the mortgage, utilities, homeowners insurance, and most household expenses.

The children occupy bedrooms in the residence, use the kitchen and laundry facilities, and share groceries and other household necessities.

Even though the children are adults, these circumstances may support treating the household as an economic unit of three people.

The analysis becomes stronger if the debtor provides substantial financial support and the children have limited independent income.

But if both children are fully employed, pay rent, purchase their own food, and maintain substantially separate finances, the conclusion may differ.

The relevant issue is not simply whether the children reside in the home, but how the household actually functions.

5. Must Adult Children Be Financially Dependent?

Not necessarily in the same sense required under federal tax law.

The economic-unit approach does not always require complete financial dependency.

An adult child may contribute toward household expenses while remaining part of an integrated family economic unit.

For example, an employed adult child might contribute $500 monthly toward household expenses while the parent pays the mortgage, utilities, insurance, and most food costs.

That contribution does not automatically establish that the child is a separate household.

Likewise, an adult child with no income may be financially dependent upon the parent even though the child is not claimed as a tax dependent.

The amount and regularity of financial contributions should be documented.

6. Adult Children Who Pay Rent

A child who pays rent to a parent may occupy either of two different financial positions.

The arrangement may resemble an ordinary landlord-tenant relationship, with the child maintaining independent finances.

Alternatively, the payment may be an informal contribution toward a shared family household.

Relevant considerations include whether the payment reflects market rent, whether food and utilities are shared, whether the parent provides additional support, and whether the parties maintain separate financial arrangements.

The label placed on the payment is not necessarily controlling.

A payment described as rent may function economically as a household contribution.

Conversely, an adult child who pays a fixed amount for a separate living area and otherwise maintains independent finances may not function as part of the same economic unit.

7. Elderly Parents and Other Relatives

A debtor may provide housing and financial support to an elderly parent, disabled relative, sibling, grandchild, or other family member.

These arrangements can support inclusion in household size where the facts establish an integrated economic unit.

For example, a debtor who houses an elderly parent, purchases groceries, pays utilities, and provides transportation may have a larger household than the debtor's tax return suggests.

But the parent's own income and contributions may also be relevant.

A parent receiving Social Security benefits who contributes toward shared expenses may still be part of the economic unit.

The classification of Social Security benefits for current-monthly-income purposes is a separate question from whether the recipient belongs to the household.

8. Married Debtors Living Together

A married couple residing together ordinarily presents a household of at least two.

If they have children or other qualifying household members, the household may be larger.

However, whether one spouse files alone or both spouses file jointly can affect the means-test income calculation.

The income of a nonfiling spouse may need to be included, subject to the applicable rules governing marital adjustments and contributions toward household expenses.

Household size and income inclusion are related but distinct questions.

A spouse's presence in the household does not mean every dollar of that spouse's income is necessarily treated identically for every bankruptcy calculation.

9. Married but Separated Spouses

Separation creates additional complications.

Some spouses live at different addresses and maintain independent finances. Others remain under the same roof because neither can afford separate housing.

A couple may be legally separated, informally separated, or involved in divorce proceedings.

The legal status of the marriage does not by itself resolve household size.

A debtor who lives separately from a spouse may have a different household composition from a debtor who remains in a shared residence with the spouse.

The means-test forms also distinguish certain circumstances involving spouses who are legally separated or living separately.

The precise treatment of income and expenses requires review of the statutory provisions, official forms, and actual financial arrangements.

10. Divorced Spouses Who Continue Living Together

A divorce does not necessarily result in separate residences.

Former spouses may continue living in the same house because of financial necessity, unresolved property issues, or arrangements concerning children.

They may share a kitchen, laundry facilities, utilities, and mortgage payments while maintaining separate bedrooms and personal finances.

The fact that they are divorced does not automatically establish that they constitute separate economic units.

Conversely, continued residence in the same property does not necessarily establish a single bankruptcy household.

The actual financial relationship is critical.

Example: Former spouses sharing a home

A debtor and former spouse remain joint owners of their residence after divorce.

Each pays half the mortgage. They share utility costs but purchase groceries separately and maintain separate bank accounts.

They occupy different portions of the house.

Whether they form one economic unit requires examining the extent of shared expenses, financial dependency, and household integration.

The answer may differ from a case in which one former spouse pays nearly all expenses and supports the other.

11. Roommates and Unrelated Adults

Sharing a residence does not automatically make unrelated adults members of the same bankruptcy household.

Roommates may divide rent and utilities while maintaining entirely separate finances.

A debtor renting a room to an unrelated individual may have rental income or household contributions that require disclosure, but that does not necessarily establish that the tenant should be counted as a household member.

Conversely, unrelated individuals may function as an integrated economic unit when they share finances and support one another.

The inquiry should focus on economic reality rather than family relationship alone.

12. Children Who Divide Their Time Between Households

Shared custody and other arrangements involving children who reside in more than one household present difficult questions.

A child may spend weekdays with one parent and weekends with another, or divide time approximately equally.

The debtor may pay substantial expenses for the child even when the child is not present every day.

Courts applying the economic-unit approach may consider the amount of time the child resides with the debtor and the extent of financial support.

The appropriate treatment is fact-specific.

A debtor should not automatically exclude a child merely because the child also resides with another parent.

Nor should the debtor assume that every child for whom support is paid must be counted as a full household member.

Johnson approved a fact-based household calculation that accounted for children who lived with the debtor only part of the time. The decision permits attention to the actual economic unit rather than mechanically counting every child as a full-time resident; it does not authorize a debtor to choose whichever household count produces the best result.

13. Household Contributions and Current Monthly Income

The Bankruptcy Code's definition of current monthly income generally includes amounts regularly paid by another person toward the household expenses of the debtor or the debtor's dependents, subject to statutory rules.

This can create an important interaction between household size and income.

Suppose an adult child contributes $600 each month toward household expenses.

That contribution may be relevant to the debtor's current-monthly-income calculation even if the child is not counted as a household member.

Similarly, an adult child's membership in the economic unit does not automatically mean the child's entire income must be included in the debtor's means test.

The amount actually and regularly contributed toward qualifying household expenses may be the relevant measure.

A household-size analysis should therefore be accompanied by an accurate examination of financial contributions.

14. Household Size and Expense Deductions

Household size can affect standardized allowances for food, clothing, and other living expenses.

Housing and utility allowances may depend on household composition and geographic location.

However, not every expense is determined solely by the number of household members.

Some deductions depend on actual payments, statutory limitations, or other factors.

The means test should not be manipulated by including household members for the purpose of increasing allowances while disregarding relevant household contributions.

Consistency between the household description, income disclosures, and expense calculations is important.

15. How Household Size Affects Schedule J

Schedule J reports the debtor's current monthly expenses.

Its purpose differs from the means test, which employs a historical income calculation and specified standardized deductions.

Schedule J ordinarily concerns the debtor's actual and anticipated household expenses.

A debtor may have legitimate expenses supporting adult children or other relatives even when those individuals' treatment under the means test requires additional analysis.

Conversely, expenses paid by other household members should not automatically be attributed entirely to the debtor.

The figures reported on Schedule J should reflect the actual financial arrangement and comply with the official form's instructions.

Differences between Schedule J and the means-test forms may be appropriate, but they should be explainable.

16. Evidence That May Be Important

A household-size determination may require more than a statement identifying who lives at the residence.

Relevant evidence can include household expense records, bank statements, utility bills, grocery expenditures, rent contributions, employment information, and documentation of financial support.

Tax returns may be relevant, although they do not necessarily control.

The debtor should be prepared to explain who pays the mortgage or rent, who purchases food, whether household members share transportation, and how expenses are allocated.

In cases involving adult children or relatives, a clear explanation of the financial arrangement can be particularly important.

17. Can Household Size Change Before Filing?

Yes.

A child may leave home, a relative may move in, spouses may separate, or a household member may begin contributing toward expenses.

The appropriate household size ordinarily must reflect the relevant circumstances under the applicable law and forms.

A debtor should not artificially alter living arrangements solely to create a misleading means-test result.

However, genuine changes in household composition may properly affect bankruptcy eligibility.

The filing date, current living arrangements, and reasonably anticipated changes should all be considered.

18. Why Household Size Should Be Evaluated Before Choosing a Bankruptcy Chapter

Household size can determine whether a debtor falls below the Maryland median-income threshold.

For above-median debtors, it can affect allowable expenses and the resulting means-test calculation.

In Chapter 13, household composition may also influence projected disposable income and the feasibility of a proposed repayment plan.

Consequently, a debtor with adult children, dependent relatives, shared custody arrangements, or unusual living circumstances should not assume that household size is self-evident.

A careful analysis may materially change the debtor's available options.

Conclusion

Household size in bankruptcy is not always determined by counting bedrooms, reviewing a tax return, or identifying everyone who receives mail at the debtor's address.

In Maryland, the Fourth Circuit's economic-unit approach provides important guidance by focusing on how individuals actually function together financially.

Adult children, elderly parents, former spouses, and unrelated residents may present very different circumstances.

The relevant questions concern residence, financial support, shared expenses, economic integration, and the requirements of the particular bankruptcy calculation.

A properly supported household-size determination can make a significant difference in whether a debtor qualifies for Chapter 7 and how household expenses are treated.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 101(10A) — Definition of current monthly income, including certain household contributions.
- 11 U.S.C. § 707(b) — Chapter 7 means testing and abuse analysis.
- 11 U.S.C. § 1325(b) — Disposable-income requirements in Chapter 13.

Official forms and administrative materials

- United States Trustee Program — Means Testing — State median-income figures and expense standards.
- United States Courts — Bankruptcy Forms — Official Forms 122A-1, 122A-2, and Schedules I and J.

Selected decisions

- *Johnson v. Zimmer*, 686 F.3d 224 (4th Cir. 2012) — Adopts the economic-unit approach to household size in a Chapter 13 means-test context.
- *In re Robinson*, 449 B.R. 473 (Bankr. E.D. Va. 2011) — Discusses household-size approaches and economic interdependence.
- *In re Morrison*, 443 B.R. 378 (Bankr. M.D.N.C. 2011) — Examines household size and the treatment of children residing in more than one household.
- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Addresses consideration of known or virtually certain financial changes in calculating projected disposable income in Chapter 13.

Maryland Bankruptcy Exemptions: What Property Can You Keep When You File Chapter 7?

BELSKY BANKRUPTCY LEGAL LIBRARY | PROPERTY AND EXEMPTIONS

By Alan J. Belsky, Attorney at Law

Filing Bankruptcy Does Not Mean Giving Up Everything You Own

One of the greatest fears people have about filing Chapter 7 bankruptcy is that they will lose their home, automobile, furniture, bank accounts, or retirement savings.

In reality, most individual Chapter 7 cases are completed without the trustee selling any property. That is largely because federal and state exemption laws protect qualifying assets from liquidation.

Maryland's exemption laws are particularly important because Maryland has chosen not to permit most bankruptcy debtors to use the alternative federal bankruptcy exemption schedule.

Recent changes have substantially increased the protection available for residential property. Effective June 1, 2026, Maryland increased its bankruptcy residential-property exemption to $125,000, making Chapter 7 a more realistic option for many homeowners.

But the homestead exemption is only one component of Maryland's exemption system.

Understanding what property is protected, which exemptions apply, and how they interact can determine whether Chapter 7 provides a safe and effective solution.

1. What Is a Bankruptcy Exemption?

When a Chapter 7 petition is filed, most of the debtor's legal and equitable interests in property become part of the bankruptcy estate under 11 U.S.C. § 541.

The estate may include real estate, vehicles, bank accounts, household furnishings, investments, business interests, tax refunds, and legal claims.

A Chapter 7 trustee is appointed to investigate and administer estate property for the benefit of creditors.

Exemption laws permit the debtor to remove qualifying interests from the pool of assets available for administration.

The debtor ordinarily claims exemptions on Schedule C of the bankruptcy petition.

A properly claimed exemption may prevent the trustee from selling property or may entitle the debtor to receive a protected amount from the proceeds of a sale.

The distinction between exempting an entire interest and exempting a specified dollar amount can be important.

2. Maryland Has Opted Out of the Federal Bankruptcy Exemptions

Under 11 U.S.C. § 522(b), states may prohibit their residents from electing the federal bankruptcy exemptions listed in § 522(d).

Maryland has exercised that option.

Accordingly, debtors subject to Maryland exemption law generally must use Maryland exemptions, together with applicable federal nonbankruptcy exemptions and other protections recognized by federal law.

This does not mean federal law is irrelevant.

The Bankruptcy Code governs how exemptions are claimed, how objections are made, and how exempt property is treated.

Federal provisions also protect certain benefits and other property interests independently of Maryland's exemption schedule.

A debtor who recently moved to Maryland may be subject to another state's exemption law because of the Bankruptcy Code's domicile rules.

3. The New $125,000 Residential-Property Exemption

Maryland's most significant recent exemption change concerns owner-occupied residential property.

Effective June 1, 2026, Maryland increased the bankruptcy residential-property exemption under Courts and Judicial Proceedings Article § 11-504(f) to $125,000.

The increase substantially expands the protection previously available under that provision.

The exemption applies to qualifying interests in owner-occupied residential property, subject to the statute's requirements.

It also addresses certain residences held through revocable trusts.

When multiple debtors in the same proceeding claim the exemption for the same property, the combined amount is limited to $125,000.

The statute provides for future inflation adjustments beginning in fiscal year 2028.

Equity, rather than market value

The relevant financial concept is the debtor's equity.

A residence worth $500,000 with a $400,000 mortgage may have approximately $100,000 in equity.

Assuming the debtor qualifies and no other complications exist, that equity may be protected under the new exemption.

A residence worth $350,000 with no mortgage presents a very different situation because the equity substantially exceeds the statutory limit.

The calculation must also account for ownership interests, enforceable liens, and the actual economic consequences of a potential sale.

The increased exemption does not eliminate a mortgage lien or prevent a secured lender from enforcing its rights when permitted by law.

4. The General Maryland Exemption for Cash and Other Property

Maryland Courts and Judicial Proceedings Article § 11-504(b)(6) provides the $6,000 cash or property exemption. Subsection (b)(5) separately protects up to $500 in a qualifying depository account without election in a garnishment; the combined amount claimed under those two items may not exceed $6,000.

This provision is especially useful because it is not limited to one particular category of property.

It may be used to protect otherwise nonexempt interests, subject to the statutory limit and applicable requirements.

The commonly applicable amount under this provision is $6,000.

A debtor may be able to allocate the exemption among several assets rather than applying it to only one.

For example, a debtor might use portions of the exemption to protect funds in a checking account and equity in a vehicle.

The exemption must be considered together with other applicable provisions and the total value of the property interests claimed.

5. Maryland's Additional Bankruptcy Exemption

Maryland Courts and Judicial Proceedings Article § 11-504(f)(1)(i)1 separately permits an eligible bankruptcy debtor to exempt up to $5,000 in personal property. This is distinct from the residential property exemption in subsection (f)(1)(i)2 and is not an additional $5,000 exemption for real estate.

It can be particularly valuable when the debtor has modest assets that exceed the protection available under more specific exemptions.

The relationship between the general exemption, additional bankruptcy exemption, and residential exemption requires careful attention to the current statutory language.

A debtor should not assume that every exemption amount can be combined without restriction or applied to every category of property.

6. Household Goods, Furniture, and Personal Belongings

Maryland law provides exemptions for qualifying household furnishings, household goods, appliances, clothing, and other personal property.

These protections are important because the value of used household property is ordinarily much lower than its original purchase price.

A dining room set purchased for $5,000 may have a relatively modest resale value several years later.

The bankruptcy valuation inquiry generally concerns the debtor's interest in the property as of the petition date, applying the relevant valuation standard.

The debtor should not list original retail prices as though the property were new.

Nor should valuable antiques, collectibles, jewelry, or specialized equipment automatically be treated as ordinary household goods.

Specific statutory categories and monetary limits must be examined.

7. Automobiles and Other Vehicles

Maryland does not provide every debtor with an unlimited exemption for a personally owned automobile.

Vehicle protection often depends on the amount of equity and the availability of general or other applicable exemptions.

Example

A debtor owns a vehicle worth $18,000 with an outstanding loan balance of $14,000.

The debtor has approximately $4,000 in equity.

That equity may be protectable through available exemptions, assuming the debtor has sufficient unused exemption capacity and satisfies the applicable requirements.

A debtor who owns a $35,000 vehicle free and clear may face a different problem.

The trustee may evaluate whether selling the vehicle would produce sufficient nonexempt proceeds to justify administration.

Vehicle valuation, loan payoff balances, title ownership, and liens should be verified.

A debtor should also distinguish between protecting equity in the vehicle and retaining the vehicle against the rights of a secured lender.

8. Bank Accounts and Cash

Funds held in checking and savings accounts generally become property of the bankruptcy estate when the petition is filed, subject to applicable exclusions and exemptions.

The debtor must disclose the accounts and relevant balances.

Cash, prepaid cards, payment-app balances, and other accessible funds may also require disclosure.

Maryland's general exemption provisions may protect qualifying funds.

Additional protections may apply to funds traceable to certain exempt benefits.

But depositing exempt benefits into a bank account can raise tracing and commingling questions.

A debtor should not assume that money becomes exempt simply because it is needed for ordinary living expenses.

9. Social Security Benefits

Social Security benefits receive significant protection under federal law.

Under 42 U.S.C. § 407, qualifying Social Security benefits generally are protected from execution, levy, attachment, garnishment, and other legal process, subject to applicable federal exceptions.

This protection can be particularly important for retirees and disabled individuals.

However, the treatment of accumulated benefits, commingled funds, and transfers requires attention to the governing law.

Keeping records sufficient to identify the source of funds may help establish their protected character.

Social Security benefits also receive special treatment under the Bankruptcy Code's definition of current monthly income, but that is a separate issue from whether the funds themselves are exempt.

10. Retirement Accounts and Pensions

Many retirement accounts receive substantial protection under federal or Maryland law.

Qualified employer-sponsored retirement plans, traditional IRAs, Roth IRAs, and certain pension benefits may qualify for different statutory protections.

Some retirement assets may be excluded from the bankruptcy estate, while others enter the estate but are exempt.

That distinction matters legally even when the practical result is that the debtor retains the funds.

The Bankruptcy Code provides protections for certain tax-exempt retirement funds under § 522(b)(3)(C), subject to statutory conditions and applicable limits.

Inherited retirement accounts require special attention.

In *Clark v. Rameker*, 573 U.S. 122 (2014), the Supreme Court held that funds in an inherited IRA of the type at issue did not qualify as retirement funds for purposes of the federal bankruptcy exemption.

A debtor should not assume that every account bearing the designation IRA receives identical protection.

11. Personal Injury Claims and Settlement Proceeds

A personal injury claim can be one of the most valuable assets in a bankruptcy estate, even when no lawsuit has been filed.

Suppose a debtor was injured in an automobile accident before filing Chapter 7. The debtor has not yet received a settlement and may not know the eventual value of the claim.

Nevertheless, the debtor's rights arising from the accident ordinarily constitute property of the bankruptcy estate under § 541.

Maryland provides significant exemption protection for qualifying compensation arising from sickness, accident, injury, or death under Courts and Judicial Proceedings Article § 11-504(b)(2).

The statutory language and Maryland decisions must be examined to determine which components of a recovery are protected.

The protection is not unlimited against every obligation. Subsection (i) permits execution for child support arrears against 25 percent of the defined net personal injury or workers' compensation indemnity recovery. Federal tax lien rules and other applicable federal exceptions require separate analysis. The exemption should not be described as erasing medical reimbursement liens or other valid interests in the recovery.

Not every settlement is necessarily treated alike

A settlement may compensate an injured person for bodily injury, pain and suffering, medical expenses, lost earnings, or other losses.

The nature of the claim and the basis for the payment can affect the exemption analysis.

For example, a recovery for physical injuries may present different exemption questions from a settlement of a purely economic contract dispute.

The allocation of settlement proceeds cannot be manipulated merely to obtain a bankruptcy advantage.

Who controls the personal injury lawsuit?

When a prepetition cause of action becomes property of the bankruptcy estate, the Chapter 7 trustee ordinarily has authority over its administration, subject to the debtor's exemption rights and applicable procedures.

The trustee may evaluate the claim, retain counsel with court approval, and determine whether prosecution or settlement would benefit the estate.

If the claim is properly exempted in its entirety, the debtor may be able to pursue it independently.

The debtor's personal injury attorney should be informed of the bankruptcy filing, and bankruptcy counsel should be informed of the personal injury claim.

Failure to coordinate the two matters can create serious problems involving ownership, settlement authority, disclosure, and judicial estoppel.

A debtor's right to recover damages for personal injuries may be one of the most valuable assets involved in a bankruptcy case.

Maryland Courts and Judicial Proceedings Article § 11-504(b)(2) provides important exemption protection for certain money payable in the event of sickness, accident, injury, or death, including compensation for loss of future earnings.

The exemption is subject to statutory qualifications, including the treatment of compensation for property damage.

Unlike some exemptions, this protection is not expressed as a simple fixed-dollar ceiling.

Personal injury claims that have not settled

A debtor may have a valuable personal injury claim even though no lawsuit has been filed and no settlement offer has been received.

For example, a debtor injured in an automobile collision may have claims for medical expenses, lost wages, pain and suffering, and permanent impairment.

The claim generally must be disclosed in the bankruptcy schedules if it is property of the estate.

The debtor's failure to disclose the claim can create serious consequences, including disputes over the right to prosecute it and potential judicial estoppel issues.

Are all lawsuit proceeds exempt?

No.

The legal character of the recovery matters.

Compensation for bodily injury may receive different treatment from damages for breach of contract, damage to property, punitive damages, or other economic losses.

Settlement agreements that allocate compensation among different categories may require particular scrutiny.

The exemption analysis should be performed before a settlement is finalized or bankruptcy is filed.

12. Workers' Compensation Benefits

Maryland workers' compensation benefits receive special statutory protection.

Labor and Employment Article § 9-732 generally protects qualifying compensation from assignment and specified creditor collection processes, subject to statutory exceptions.

The treatment of an unpaid workers' compensation claim, an accrued award, and funds already deposited into a bank account may raise different questions.

A debtor should disclose pending workers' compensation claims and identify any benefits received.

The fact that a payment is protected from creditors does not necessarily eliminate the duty to disclose it in bankruptcy.

Workers' compensation benefits may receive protection under Maryland law.

Maryland Labor and Employment Article § 9-732 generally protects compensation payable under the Workers' Compensation Act from assignment and certain creditor claims, subject to statutory exceptions.

The treatment of accrued benefits, settlements, and funds already deposited into bank accounts may require further analysis.

A debtor receiving workers' compensation should disclose the claim and benefits and identify the statutory basis for any claimed exemption.

13. Life Insurance and Annuities

Maryland law provides certain protections for life insurance and annuity interests.

However, the scope of protection depends on the policy, the insured, the beneficiary, ownership rights, and the governing statutory provision.

A term life insurance policy with no cash surrender value generally presents a different asset question from a whole-life policy with substantial accumulated cash value.

Annuities also require individualized analysis.

A debtor should not assume that purchasing an annuity or transferring money into a life insurance product shortly before bankruptcy automatically protects those funds.

Transfers made in anticipation of bankruptcy may raise separate issues concerning fraudulent transfers, exemption planning, and good faith.

Maryland law provides protections for certain life insurance proceeds and policy interests.

The availability of an exemption may depend on the policy owner, insured person, beneficiary, type of policy, and applicable statutory provisions.

Term life insurance, which ordinarily has no cash surrender value, presents different property issues from permanent life insurance with accumulated cash value.

A debtor who owns a whole-life or universal-life policy may possess a valuable property interest even though no death benefit has become payable.

The policy and beneficiary designations should be reviewed before filing.

14. Tools, Equipment, and Business Property

Self-employed individuals may own tools, computers, machinery, inventory, office furniture, or other business assets.

Some property may qualify for a specific exemption, while other assets may require use of general exemption provisions.

The legal distinction between personally owned business property and property belonging to a separate corporation or limited liability company is important.

A debtor who owns an LLC does not necessarily own the company's individual assets. Instead, the debtor generally owns a membership interest, whose value and administration must be evaluated.

Sole proprietorship assets present different considerations because the business and the individual are not separate legal persons.

A self-employed debtor should obtain a careful valuation of business interests and equipment before filing.

A debtor who is self-employed may own tools, equipment, inventory, accounts receivable, and other business assets.

Maryland provides certain protections for qualifying tools, books, instruments, and other property used in an occupation or profession.

However, the exemption does not necessarily protect every asset used in a business.

For example, a self-employed tradesperson's hand tools may present a different exemption question from a commercial truck, expensive machinery, or inventory held for resale.

Ownership also matters.

Assets belonging to a corporation or limited liability company are not automatically treated as personally owned assets of the debtor, although the debtor's ownership interest in the business may itself be property of the bankruptcy estate.

A sole proprietor generally does not have the same legal separation between personal and business property.

15. Tax Refunds

A tax refund may be property of the bankruptcy estate even when the debtor has not yet filed the tax return.

The relevant inquiry includes when the refund was earned or accrued, the tax period involved, and the debtor's ownership interest.

A refund attributable to prepetition tax payments or withholding may be wholly or partly estate property.

Refunds associated with tax years spanning the filing date may require allocation.

Maryland general exemptions may protect qualifying refund interests, subject to available exemption amounts and other applicable law.

A debtor expecting a substantial refund should discuss the timing of the bankruptcy filing and the treatment of the refund before submitting the petition.

A debtor's right to receive a tax refund may become property of the bankruptcy estate even when the return has not yet been filed.

The analysis depends on the tax year, the timing of the bankruptcy petition, and the portion of the refund attributable to prepetition earnings or payments.

A debtor filing in October may have an accrued interest in a refund expected the following spring.

The fact that the refund has not been received does not necessarily mean it is excluded from the estate.

Certain refundable tax credits may receive specific protections under applicable law.

The debtor should disclose anticipated refunds and claim available exemptions where appropriate.

16. Jointly Owned Property

When property is jointly owned, the debtor's interest must be identified and valued.

Joint ownership does not automatically mean that the entire asset belongs to the bankruptcy estate.

Nor does it mean that the trustee is necessarily limited to selling only the debtor's fractional interest.

Under § 363(h), a trustee may, under specified circumstances, sell both the estate's interest and a nondebtor co-owner's interest in certain forms of jointly owned property.

The nondebtor co-owner has statutory protections, including those provided by §§ 363(i) and 363(j).

The form of ownership matters.

Tenancy by the entirety, joint tenancy, and tenancy in common create different rights and potential creditor remedies.

For married Maryland homeowners, tenancy by the entirety can provide substantial protection against individual creditors, but joint debts may affect that protection.

A debtor who owns property with another person must disclose the ownership interest.

The bankruptcy estate generally includes the debtor's legal and equitable interests, not automatically every interest held by a nonfiling co-owner.

However, 11 U.S.C. § 363(h) permits a trustee, under specified conditions, to sell certain jointly owned property, including the interests of nondebtor co-owners.

The trustee must satisfy the statutory requirements, and co-owners possess rights under § 363(i) and (j).

The fact that property is jointly titled therefore does not guarantee protection from sale.

The type of co-ownership is especially important.

Maryland recognizes tenancy by the entirety for qualifying property owned by married spouses.

Under 11 U.S.C. § 522(b)(3)(B), a debtor may exempt an interest in property held as tenants by the entirety to the extent that interest is exempt from process under applicable nonbankruptcy law.

Maryland entireties property ordinarily is protected against creditors holding claims against only one spouse.

But joint creditors can create a significant exception.

In *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985), the Fourth Circuit addressed the extent to which entireties property could be administered for the benefit of joint creditors.

A married debtor with substantial home equity may therefore have significant protection when debts are exclusively individual, but face a different result when the spouses share enforceable obligations.

Divorce can also terminate tenancy-by-the-entirety ownership even when no new deed is recorded.

These issues warrant separate analysis before filing.

17. Property Acquired After Bankruptcy Is Filed

The bankruptcy estate generally includes the debtor's property interests as of the petition date.

However, § 541(a)(5) brings certain property acquired or becoming available within 180 days after filing into the estate, including specified interests arising through inheritance, property settlement agreements, divorce decrees, and life insurance or death benefits.

For example, a debtor who becomes entitled to an inheritance shortly after filing may be required to disclose it, and the property may be administered by the trustee.

The debtor's obligation to disclose qualifying postpetition acquisitions should not be confused with whether the property is ultimately exempt.

The Bankruptcy Code's rules concerning postpetition property differ between Chapter 7 and Chapter 13.

Property acquired after the bankruptcy petition generally is treated differently from property owned at filing.

However, the Bankruptcy Code contains important exceptions.

Under § 541(a)(5), certain interests acquired or becoming available within 180 days after filing may enter the estate, including specified interests arising through inheritance, property settlements, divorce decrees, and life insurance or death benefit arrangements.

Other provisions may affect proceeds, rents, profits, and property derived from estate assets.

The debtor should promptly inform bankruptcy counsel about significant postpetition acquisitions.

18. Exempt Property Must Still Be Disclosed

A debtor must disclose property even when the debtor believes it is fully exempt.

Bankruptcy schedules require comprehensive identification of assets and interests.

Exemptions ordinarily are claimed separately on Schedule C.

A debtor who fails to disclose an asset may lose important procedural protections and face objections, litigation, or more serious consequences.

Intentional concealment may support denial of discharge under § 727(a), depending on the statutory elements.

The correct approach is to disclose the asset and claim the applicable exemption—not omit the asset because it appears protected.

Exemptions ordinarily are claimed on Official Schedule C.

The debtor identifies the property, states the exemption amount or extent, and cites the legal authority supporting the claim.

The trustee and other parties in interest may object.

Under Federal Rule of Bankruptcy Procedure 4003, objections generally must be filed within the applicable deadline, subject to the rule's exceptions and extensions.

The Supreme Court's decision in *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992), illustrates the importance of timely objections.

In *Schwab v. Reilly*, 560 U.S. 770 (2010), the Court explained that the manner in which an exemption is claimed can affect whether the debtor has exempted a specified value or asserted an exemption covering the full interest in an asset.

Exemption schedules should therefore be prepared with precision.

19. Can a Trustee Object to an Exemption?

Yes.

Federal Rule of Bankruptcy Procedure 4003 governs objections to claimed exemptions.

The rule establishes deadlines and procedures, subject to its provisions and applicable exceptions.

A trustee or other party in interest may challenge an exemption because the property does not qualify, the claimed value exceeds a statutory limit, or another legal requirement has not been satisfied.

In *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992), the Supreme Court emphasized the importance of timely objections.

In *Schwab v. Reilly*, 560 U.S. 770 (2010), the Court explained important distinctions concerning exemptions claimed in specified dollar amounts and the trustee's ability to administer property with value exceeding those amounts.

Exemption claims should therefore be drafted accurately, with attention to both the property description and the amount claimed.

A trustee may object when the claimed exemption lacks a statutory basis, exceeds the permitted amount, or otherwise fails to satisfy applicable requirements.

The debtor may be required to establish the exemption's validity, subject to the governing procedural rules and allocation of burdens.

Disputes can concern ownership, valuation, residency, the source of funds, or the legal classification of property.

A debtor should not assume that listing an asset as exempt makes the claim immune from challenge.

20. Can Property Be Transferred Before Filing to Protect It?

A debtor should not transfer property to relatives or friends merely to place it beyond creditors' reach.

Transfers for less than reasonably equivalent value, transfers made with actual intent to hinder creditors, and certain payments to preferred creditors may be challenged under federal or state law.

A trustee may seek to recover property or its value.

Exemption planning is not inherently improper, but the distinction between legitimate planning and an avoidable transfer can be consequential.

For example, selling an asset for fair market value and properly using the proceeds may present a different analysis from giving the asset to a relative shortly before filing.

The debtor should disclose all required prepetition transactions and seek advice before transferring valuable property.

Purchasing property before bankruptcy does not automatically make the property exempt.

The debtor's rights depend on the property's character, the applicable exemption, and the circumstances of the transaction.

Converting nonexempt property into exempt property may be permissible in some circumstances, but transfers or transactions undertaken with fraudulent intent can create serious problems.

The Bankruptcy Code contains provisions addressing fraudulent transfers, concealment, and denial of discharge.

A debtor should not attempt to protect assets through undisclosed transfers to family members or other arrangements designed to mislead creditors or the trustee.

21. When Exemptions Are Not Enough

A debtor may qualify for Chapter 7 under the means test but possess substantial nonexempt assets.

For example, a debtor might own valuable investment property, significant nonretirement savings, or business interests that cannot be fully protected.

In such circumstances, Chapter 13 may offer an alternative to liquidation.

Chapter 13 generally permits eligible debtors to retain property while making payments under a court-approved repayment plan.

The plan must satisfy statutory requirements, including the liquidation-value test under § 1325(a)(4).

That test generally requires unsecured creditors to receive at least as much as they would receive in a hypothetical Chapter 7 liquidation.

Consequently, exemptions remain important even when the debtor files Chapter 13.

An exemption limited to a specified dollar amount may protect only part of the debtor's equity.

Suppose a debtor owns an asset with $20,000 in unencumbered value but can exempt only $11,000 of that value.

The remaining $9,000 may be available for administration.

Whether the trustee will sell the asset depends on the anticipated proceeds, costs of sale, administrative expenses, and potential benefit to creditors.

If the property is sold, the debtor ordinarily is entitled to the protected exemption amount from the proceeds, subject to applicable law.

The trustee may also consider whether a negotiated payment or other resolution would better serve the estate.

A debtor should not assume that a trustee will disregard nonexempt equity merely because the amount appears modest.

22. Why Exemption Planning Should Precede the Bankruptcy Filing

Exemption rights ordinarily are evaluated in relation to the petition date and the governing statutory framework.

A debtor who files without identifying assets and available exemptions may discover problems that cannot easily be corrected afterward.

The evaluation should include real estate values, mortgage balances, vehicle equity, bank balances, anticipated tax refunds, retirement accounts, pending legal claims, and jointly owned property.

For homeowners, Maryland's expanded residential exemption may now provide protection that was unavailable in earlier years.

That development makes it particularly worthwhile for individuals who previously ruled out Chapter 7 because of home equity to obtain an updated analysis.

Bankruptcy exemptions are generally determined in relation to the petition date and applicable law.

The debtor's property interests, account balances, ownership arrangements, and available exemptions should be evaluated before filing.

A debtor who has substantial funds in a checking account on the filing date may present a different exemption problem from a debtor whose funds have been used in the ordinary course for legitimate living expenses before filing.

However, unusual transfers, payments to relatives, or attempts to conceal assets can create separate bankruptcy problems.

Exemption planning should be lawful, transparent, and supported by accurate documentation.

Conclusion

Maryland bankruptcy exemptions allow many individuals to eliminate qualifying debts without losing their homes, vehicles, retirement savings, or ordinary personal property.

The protections arise from several different sources, including Maryland exemption statutes, federal nonbankruptcy law, and special rules concerning property ownership.

The increased residential exemption has substantially improved Chapter 7's potential usefulness for Maryland homeowners.

Maryland's exemption laws permit many Chapter 7 debtors to retain their homes, vehicles, household belongings, retirement funds, and other important property.

The increased $125,000 residential exemption has substantially expanded the availability of Chapter 7 relief for qualifying homeowners.

But exemptions are not automatic, and not every asset is fully protected.

The outcome depends on ownership, valuation, statutory eligibility, the nature of the asset, and the debtor's overall financial circumstances.

The question is not simply what property a debtor owns, but what portion of that property is legally protected from administration in bankruptcy.

A careful exemption analysis before filing can prevent the loss of valuable property and help determine whether Chapter 7 or Chapter 13 is the more appropriate choice.

Related Bankruptcy Cases and Authorities

Maryland statutes

- Maryland Code, Courts and Judicial Proceedings § 11-504 — Principal Maryland exemption statute, including personal property and residential-property exemptions.
- Maryland Code, Labor and Employment § 9-732 — Protection of workers' compensation benefits.
- Maryland Code, Insurance § 16-111 — Certain protections involving life insurance proceeds.

Federal statutes and rules

- 11 U.S.C. § 522 — Bankruptcy exemptions.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 363 — Use, sale, or lease of estate property.
- 42 U.S.C. § 407 — Protection of Social Security benefits.
- Federal Rule of Bankruptcy Procedure 4003 — Exemption claims and objections.

Selected decisions

- *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992) — Consequences of failing to object timely to an exemption claim.
- *Schwab v. Reilly*, 560 U.S. 770 (2010) — Distinguishes exemptions of specified values from claims to exempt an entire property interest.
- *Law v. Siegel*, 571 U.S. 415 (2014) — Limits bankruptcy courts' equitable authority to override statutory exemptions.

- *Clark v. Rameker*, 573 U.S. 122 (2014) — Addresses the treatment of inherited IRAs under federal bankruptcy exemption law.
- *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985) — Addresses entireties property and joint creditors.
- *In re Butcher*, 189 B.R. 357 (Bankr. D. Md. 1995), aff'd, 125 F.3d 238 (4th Cir. 1997) — Addresses Maryland's exemption for personal injury compensation and its constitutional application.

What Happens to Your Car in Chapter 7 Bankruptcy? Reaffirmation, Redemption, Surrender, and Repossession

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By Alan J. Belsky, Attorney at Law

Filing Bankruptcy Does Not Necessarily Mean Losing Your Car

For many people considering bankruptcy, keeping a reliable automobile is nearly as important as keeping their home. A vehicle may be essential for employment, medical appointments, childcare, and ordinary daily activities.

Chapter 7 bankruptcy does not automatically require a debtor to surrender a vehicle. Many debtors retain their cars after filing, including vehicles subject to outstanding loans.

But the legal analysis involves two separate questions: whether the bankruptcy trustee can administer the debtor's equity in the vehicle and whether a secured lender can enforce its lien.

A debtor may have sufficient exemptions to protect the vehicle from the trustee but still face repossession if the lender's secured rights are not properly addressed.

Conversely, a debtor may owe nothing on a vehicle yet possess so much nonexempt equity that the trustee has an incentive to sell it.

Understanding these distinctions is essential before deciding whether to reaffirm a loan, redeem a vehicle, surrender it, or pursue another legally available arrangement.

1. Two Different Interests in a Financed Automobile

When a debtor finances the purchase of a vehicle, the debtor ordinarily owns the automobile subject to a security interest held by the lender.

The lender's lien secures repayment of the loan.

The debtor's equity is generally the difference between the vehicle's value and the amount of enforceable secured debt against it.

For example, a vehicle worth $20,000 with a $16,000 loan balance has approximately $4,000 in equity.

That equity may be protected by applicable exemptions.

But protecting the equity does not extinguish the lender's lien or eliminate the contractual consequences of failing to make payments.

Chapter 7 may discharge the debtor's personal liability on the loan while leaving the lien enforceable against the automobile.

This distinction explains why a debtor can receive a bankruptcy discharge yet still lose a financed vehicle through repossession.

2. Can the Chapter 7 Trustee Sell My Car?

A Chapter 7 trustee may administer nonexempt property for the benefit of creditors.

Whether a vehicle is at risk depends upon its value, loan balance, available exemptions, and the costs of administration.

Maryland does not provide every debtor with an unlimited exemption for automobiles.

Instead, vehicle equity often must be protected through available general or other applicable exemptions under Maryland Courts and Judicial Proceedings Article § 11-504.

Example: A financed vehicle with modest equity

A debtor owns a car worth $17,000 and owes $14,000.

The debtor has approximately $3,000 in equity.

If sufficient exemptions are available, the equity may be fully protected.

The trustee ordinarily would have no economic reason to sell the vehicle merely to recover exempt equity.

Example: A paid-off vehicle

A debtor owns a car worth $28,000 free and clear.

The entire value represents equity.

If the debtor cannot exempt all of that equity, the trustee may consider selling the vehicle and distributing the nonexempt proceeds to creditors.

The debtor may receive the amount of any valid exemption from the sale proceeds.

Whether a sale actually occurs depends on the financial benefit to the estate.

3. What Happens to the Car Loan When Chapter 7 Is Filed?

Filing Chapter 7 ordinarily triggers the automatic stay under 11 U.S.C. § 362.

The stay generally prevents the lender from repossessing the vehicle while the protection remains effective.

But the stay does not permanently eliminate the lender's security interest.

A secured creditor may request relief from the stay, particularly when the debtor is not making payments or the collateral is inadequately protected.

The debtor must also address the Bankruptcy Code's requirements concerning secured consumer debts.

These requirements are particularly important when the debtor wishes to retain a financed automobile.

4. The Statement of Intention

Under 11 U.S.C. § 521(a)(2), an individual Chapter 7 debtor whose schedules include debts secured by estate property generally must file a statement of intention concerning that property. Other provisions impose additional requirements for specified personal property and purchase-money claims.

The statement ordinarily identifies whether the debtor intends to surrender or retain the collateral and, when applicable, whether the debtor intends to redeem the property or reaffirm the debt.

Federal Rule of Bankruptcy Procedure 1007 and Official Form 108 address the filing requirements.

The statement of intention generally must be filed within thirty days after the petition or by the date of the meeting of creditors, whichever is earlier, unless the court extends the period.

The debtor ordinarily must perform the stated intention within the statutory period.

Section 521(a)(2)(B) generally requires performance within 30 days after the first date set for the meeting of creditors. Section 521(a)(6) separately addresses qualifying personal property securing an allowed purchase-price claim and uses a 45-day period after the first meeting. Rule 4008 generally requires filing the reaffirmation agreement within 60 days after the first date set for the meeting; the court may extend that filing deadline. These are different requirements, and an agreement still must be made before discharge under § 524(c).

Failure to comply can have consequences for the automatic stay and the debtor's rights in the collateral.

5. Reaffirmation Agreements: Agreeing to Remain Personally Liable

A reaffirmation agreement is a new agreement, subject to Bankruptcy Code requirements, under which the debtor agrees that a particular debt will remain personally enforceable despite the bankruptcy discharge.

Reaffirmation is governed principally by 11 U.S.C. § 524(c) and related provisions.

A valid reaffirmation agreement can permit the debtor to retain a financed vehicle under agreed terms.

But it also restores or preserves personal liability that otherwise might have been discharged.

Why reaffirmation can be dangerous

Suppose a debtor owes $24,000 on a vehicle worth $15,000.

The debtor reaffirms the full loan balance.

Six months after discharge, the debtor loses employment and can no longer afford the payments.

The lender repossesses the car and sells it for $12,000.

After applying the proceeds and permissible charges, a substantial deficiency may remain.

Because the debt was validly reaffirmed, the lender may be able to pursue the debtor personally for that deficiency.

Had the debtor not reaffirmed, the discharge might have eliminated the debtor's personal liability, even though the lender retained its lien and repossession rights.

The decision to reaffirm should therefore be made with an understanding of the vehicle's value, loan balance, payment terms, and the consequences of future default.

6. Requirements for a Valid Reaffirmation Agreement

Reaffirmation agreements must satisfy statutory requirements.

Among other things, the agreement generally must be made before discharge, contain required disclosures, and be filed with the bankruptcy court.

Depending on whether the debtor is represented and the circumstances of the agreement, attorney certification or court review may be required.

The Bankruptcy Code also provides protections when a reaffirmation agreement creates a presumption of undue hardship.

A debtor ordinarily may rescind a reaffirmation agreement before discharge or within sixty days after the agreement is filed with the court, whichever occurs later.

The right of rescission is important because a debtor may reconsider whether retaining personal liability is financially prudent.

7. Can I Keep Making Payments Without Reaffirming?

This question is frequently described as the *ride-through* or *pay-and-retain* issue.

Historically, some debtors retained secured collateral by remaining current on payments without formally reaffirming the debt.

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 substantially changed the statutory framework governing retention of personal property securing consumer debts.

Sections 521(a)(6), 521(d), and 362(h) can affect the debtor's ability to retain collateral without reaffirmation or redemption.

The statutory requirements and applicable case law must be examined carefully.

A lender may voluntarily continue accepting payments without an enforceable reaffirmation agreement.

But the lender's willingness to do so should not be confused with an unconditional legal right to retain the vehicle.

In some circumstances, the creditor may be able to enforce a contractual default provision even though the debtor remains current on payments.

The result can depend on the loan agreement, applicable state law, and the precise statutory circumstances.

8. What If the Lender Refuses to Reaffirm?

A lender is not necessarily required to enter into a reaffirmation agreement.

Some lenders may decline to reaffirm loans under particular circumstances.

Others may require completion of their own documentation or impose conditions permitted by law.

The debtor cannot assume that offering to make payments obligates the lender to accept a reaffirmation agreement.

Nor should the debtor assume that refusal to reaffirm automatically entitles the lender to repossess.

The outcome depends on the relevant statutory provisions, contract terms, and applicable law.

Section 362(h)(1)(B) contains a specific exception when the debtor timely states an intention to reaffirm on the original contract terms but the creditor refuses those terms. That exception is different from a lender voluntarily accepting payments. Its application requires timely compliance with the statement and performance requirements and careful review of the facts.

Where reaffirmation is unavailable or inadvisable, redemption, surrender, refinancing, or another arrangement may need to be considered.

9. Redemption: Keeping the Car by Paying Its Value

Redemption is an alternative to reaffirmation.

Under 11 U.S.C. § 722, an individual Chapter 7 debtor may redeem certain tangible personal property intended primarily for personal, family, or household use by paying the secured creditor the amount of its allowed secured claim, subject to statutory requirements.

Section 722 requires a lien securing a dischargeable consumer debt and property that has been exempted or abandoned by the trustee. It requires payment of the allowed secured claim in full at redemption; bankruptcy does not compel the creditor to accept a new installment arrangement.

For a qualifying vehicle, this ordinarily involves paying the creditor the applicable value of its secured interest rather than the full outstanding loan balance.

Example

A debtor owes $22,000 on a vehicle worth $14,000.

If the applicable redemption value is $14,000 and the statutory requirements are satisfied, the debtor may be able to redeem the vehicle by paying that amount.

The remaining unsecured portion of the debt may be discharged, assuming no exception applies.

Redemption generally requires a lump-sum payment unless the creditor agrees otherwise.

Some debtors obtain financing from lenders specializing in bankruptcy redemptions.

But redemption financing may carry substantial interest rates and fees.

The debtor should compare the total cost of redemption financing with the cost of reaffirmation or replacement transportation.

10. How Is Redemption Value Determined?

Valuation disputes can arise when the debtor and creditor disagree about the vehicle's worth.

Under 11 U.S.C. § 506(a)(2), personal property securing an allowed claim in an individual Chapter 7 or Chapter 13 case is generally valued based on replacement value as of the petition date, without deduction for costs of sale or marketing.

For property acquired for personal, family, or household purposes, replacement value ordinarily means the price a retail merchant would charge for property of that kind considering its age and condition.

Published vehicle valuation guides may provide useful evidence, but they do not necessarily determine the legal value conclusively.

Mileage, mechanical condition, accident history, equipment, and local market conditions can affect valuation.

A debtor seeking redemption should be prepared to substantiate the proposed value.

11. Surrendering the Vehicle

A debtor who cannot afford the payments or who owes substantially more than the vehicle is worth may choose to surrender it.

Surrender ordinarily means making the collateral available to the secured creditor rather than attempting to retain it.

The creditor may then exercise applicable rights to repossess and dispose of the vehicle.

If the underlying personal liability is discharged, the lender ordinarily cannot collect a resulting deficiency from the debtor personally.

However, surrender does not necessarily eliminate every obligation associated with the vehicle.

For example, postpetition conduct, separate agreements, or nondischargeable obligations may require further analysis.

A debtor should also consider the practical cost of obtaining replacement transportation.

12. What If the Car Was Repossessed Before Bankruptcy?

Filing bankruptcy after repossession may not automatically result in the return of the vehicle.

The debtor's remaining ownership and redemption rights depend upon applicable state law and the status of the repossession process.

The Supreme Court held in *City of Chicago v. Fulton*, 592 U.S. 154 (2021), that merely retaining possession of property seized before bankruptcy does not itself violate § 362(a)(3).

Other Bankruptcy Code provisions, including turnover under § 542, may still be relevant.

In Maryland, the debtor's rights may also depend on applicable provisions of the Commercial Law Article, the loan agreement, and whether the collateral has already been sold.

Timing is critical.

A debtor should not assume that filing bankruptcy after the vehicle has been sold will restore ownership.

13. What If the Car Is Repossessed After Filing?

If the automatic stay applies, a postpetition repossession may violate § 362.

A willful violation can expose a creditor to damages under § 362(k), including actual damages, attorney's fees, and potentially punitive damages in appropriate circumstances.

But the stay may have terminated under § 362(h), been modified by court order, or otherwise ceased to protect the collateral.

Consequently, the mere fact that repossession occurred after filing does not conclusively establish a violation.

The relevant dates, notices, statement of intention, and court orders must be examined.

14. Does Bankruptcy Eliminate a Vehicle Deficiency Balance?

A deficiency arises when the amount owed exceeds the proceeds obtained from disposition of the collateral, after applying applicable charges and credits.

An ordinary prepetition vehicle-loan deficiency is generally dischargeable in Chapter 7.

This can be particularly valuable when a vehicle has already been repossessed or totaled.

For example, a debtor may owe $19,000 on a vehicle that produces only $11,000 in sale proceeds.

The remaining deficiency may be discharged if it is an ordinary unsecured obligation and no exception to discharge applies.

The analysis can differ if the debtor has entered into a valid reaffirmation agreement or the obligation is subject to another legal exception.

15. What If the Vehicle Was Totaled Before Bankruptcy?

A total-loss accident can create several distinct legal issues.

The debtor may owe more on the loan than the vehicle's insurance settlement.

The insurer may pay the lienholder directly, leaving an unsecured deficiency.

If the debtor has GAP coverage, that coverage may reduce or eliminate the deficiency, subject to the contract's terms and exclusions.

GAP coverage is not universal, and exclusions may apply when the vehicle was being used for commercial or delivery purposes.

The debtor may also have an insurance claim, personal injury claim, or other property interest requiring disclosure.

A deficiency remaining after application of insurance proceeds may be dischargeable in Chapter 7.

16. Leased Vehicles Are Different

A vehicle lease generally is not treated the same as a secured purchase loan.

Under 11 U.S.C. § 365, an unexpired lease may be assumed or rejected subject to applicable statutory provisions.

The debtor must consider the lease terms, ongoing payment obligations, and the consequences of rejection.

A debtor who wishes to retain a leased vehicle may need to satisfy requirements different from those applicable to reaffirmation of a purchase-money vehicle loan.

The classification of the agreement matters because some transactions described as leases may, under applicable law, actually create security interests.

17. Co-Signers and Joint Vehicle Loans

A Chapter 7 discharge generally protects the debtor personally but does not automatically discharge a nonfiling cosigner's separate contractual liability.

If a parent cosigned a child's vehicle loan, the child's bankruptcy may eliminate the child's personal liability while leaving the parent responsible.

The lender may pursue the cosigner according to the contract and applicable law.

The Chapter 7 automatic stay generally does not provide the broad codebtor protection available in certain Chapter 13 consumer cases under § 1301.

A debtor considering surrender or discharge of a jointly obligated vehicle loan should understand the consequences for any cosigner.

18. What About a Vehicle Used for Work?

A vehicle used for business may present different exemption and secured-debt questions.

For example, a debtor who uses a pickup truck for contracting work or a vehicle for rideshare or delivery services may face issues concerning the nature of the debt, the use of collateral, and available exemptions.

The statutory redemption provisions applicable to personal, family, or household property may not apply in the same manner to business property.

The loan agreement may also contain restrictions on commercial use.

A debtor should disclose the vehicle's actual use and examine the loan and insurance agreements before filing.

19. Should You Reaffirm a Vehicle Loan?

Reaffirmation is not automatically the best choice merely because the debtor wants to keep the vehicle.

Relevant considerations include whether the payments are affordable, whether the vehicle is reliable, how much is owed relative to its value, the remaining loan term, and the availability of alternative transportation.

A debtor who reaffirms an expensive loan on an aging vehicle may emerge from bankruptcy with a substantial continuing financial burden.

On the other hand, a debtor with a reliable vehicle, manageable payments, and favorable loan terms may reasonably conclude that reaffirmation is appropriate.

The important point is that reaffirmation creates consequences extending beyond the bankruptcy discharge.

The debtor should understand those consequences before signing.

20. Why Vehicle Decisions Should Be Made Before Filing

A debtor who waits until after filing to consider reaffirmation, redemption, or surrender may encounter statutory deadlines and practical difficulties.

The statement of intention, automatic stay, creditor communications, and reaffirmation requirements all operate within relatively short time periods.

A debtor also must evaluate whether the vehicle's equity is exempt.

The best decision may depend on factors that have little to do with the loan itself, including the debtor's employment needs, family transportation requirements, and expected postbankruptcy budget.

Proper planning should address both the legal and financial consequences.

Conclusion

Chapter 7 bankruptcy often permits debtors to retain their vehicles, but it does not guarantee that result.

The debtor must distinguish between protecting equity from the bankruptcy trustee and satisfying the rights of a secured lender.

Reaffirmation may preserve the loan but also preserve personal liability. Redemption may permit the debtor to retain the vehicle by paying its applicable secured value. Surrender may eliminate an unaffordable obligation but require replacement transportation.

The correct choice depends on the vehicle's value, loan balance, exemption protection, contract terms, and the debtor's financial circumstances.

The objective is not simply to keep the car through bankruptcy. It is to emerge from bankruptcy with transportation that is both reliable and financially sustainable.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 362 — Automatic stay, including § 362(h).
- 11 U.S.C. § 365 — Executory contracts and unexpired leases.
- 11 U.S.C. § 506 — Determination of secured status and valuation.
- 11 U.S.C. § 521 — Debtor duties, statement of intention, and certain secured personal-property requirements.
- 11 U.S.C. § 524 — Reaffirmation agreements.
- 11 U.S.C. § 722 — Redemption.
- 11 U.S.C. § 1301 — Chapter 13 codebtor stay.

Maryland law

- Maryland Code, Courts and Judicial Proceedings § 11-504 — Maryland property exemptions.
- Maryland Commercial Law § 9-609 — Secured creditor's right to take possession of collateral after default, subject to statutory requirements.
- Maryland Commercial Law § 9-610 — Disposition of collateral following default and the requirement of commercial reasonableness.
- Maryland Commercial Law § 9-623 — Right to redeem collateral.
- Maryland Commercial Law § 12-1021 — Repossession and related requirements for qualifying credit transactions governed by Maryland's Credit Grantor Closed End Credit Provisions.

Selected decisions

- *City of Chicago v. Fulton*, 592 U.S. 154 (2021) — Holds that merely retaining property seized before bankruptcy does not, by itself, violate § 362(a)(3).
- *United States v. Whiting Pools, Inc.*, 462 U.S. 198 (1983) — Addresses property seized before bankruptcy and the bankruptcy estate's turnover rights.
- *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997) — Addresses valuation of collateral a Chapter 13 debtor proposes to retain.
- *DaimlerChrysler Financial Services Americas LLC v. Jones (In re Jones)*, 591 F.3d 308 (4th Cir. 2010) — Addresses the consequences of failing to comply with the Bankruptcy Code's requirements for retaining secured personal property.
- *In re Donald*, 343 B.R. 524 (Bankr. E.D.N.C. 2006) — Discusses reaffirmation and the post-2005 statutory treatment of secured personal property.

Reaffirmation Agreements in Chapter 7 Bankruptcy: Why Keeping a Debt After Bankruptcy Can Be a Costly Mistake

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By Alan J. Belsky, Attorney at Law

Bankruptcy Can Eliminate a Debt. Reaffirmation Can Bring It Back.

The principal purpose of Chapter 7 bankruptcy is to relieve qualifying debtors of personal liability for debts they cannot afford to pay. A reaffirmation agreement is an important exception to that objective.

Through reaffirmation, a debtor voluntarily agrees to remain personally liable for a particular debt that otherwise might be discharged in bankruptcy.

Reaffirmation most commonly arises with automobile loans, but it can involve other obligations. The decision deserves careful consideration because it can expose the debtor to collection activity, lawsuits, judgments, and wage garnishment after bankruptcy.

A debtor may understandably wish to retain a reliable vehicle or other essential property. But retaining property and remaining personally liable for its purchase debt are not necessarily the same thing.

The critical question is whether reaffirmation is legally necessary, financially sensible, and consistent with the fresh start that bankruptcy is intended to provide.

1. What Is a Reaffirmation Agreement?

A reaffirmation agreement is a legally regulated agreement between a debtor and creditor concerning a debt that is otherwise dischargeable.

Under 11 U.S.C. § 524(c), a qualifying reaffirmation agreement may remain enforceable notwithstanding the debtor's bankruptcy discharge.

The agreement must satisfy specific statutory requirements. A debtor and creditor cannot necessarily make a discharged debt enforceable merely by signing an informal promise to pay.

Reaffirmation ordinarily must occur before the discharge is entered.

The Bankruptcy Code also requires disclosures designed to ensure that the debtor understands the financial consequences of reaffirmation.

Unlike an ordinary loan modification, reaffirmation concerns the continued enforceability of a debt in the face of a bankruptcy discharge.

2. Why Do Creditors Request Reaffirmation?

A secured lender ordinarily possesses two distinct rights.

First, it may have a contractual right to collect money from the borrower personally.

Second, it may hold a lien against property securing repayment.

A Chapter 7 discharge generally eliminates personal liability for a dischargeable debt, but it does not automatically eliminate a valid lien.

Consequently, a vehicle lender may retain the right to repossess collateral after bankruptcy even though the debtor is no longer personally liable for a deficiency.

Reaffirmation preserves personal liability according to the enforceable terms of the agreement.

For the creditor, this can provide a significant benefit.

For the debtor, the benefit may be continued access to collateral, preservation of particular loan arrangements, or avoidance of certain contractual consequences.

Whether those benefits justify renewed personal liability is a separate question.

3. The Danger of Reaffirming an Underwater Vehicle Loan

Consider a debtor who owes $27,000 on a vehicle worth $16,000.

The debtor files Chapter 7 and receives a discharge of substantial credit card and medical debt.

To keep the vehicle, the debtor signs a valid reaffirmation agreement covering the full outstanding automobile loan.

A year later, the debtor loses employment and defaults.

The lender repossesses the vehicle and sells it for $12,000.

After application of the sale proceeds and any permissible expenses, the debtor may remain personally liable for a substantial deficiency.

Because the loan was reaffirmed, the bankruptcy discharge may not protect the debtor from collection of that deficiency.

The debtor has effectively preserved a substantial financial obligation that might otherwise have been eliminated.

This is why the affordability of the monthly payment is only one consideration. The amount owed, vehicle value, reliability, remaining loan term, and risk of future default also matter.

4. Is Reaffirmation Required to Keep a Car?

Not in every circumstance, but the answer is more complicated than simply continuing to make payments.

Before the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, some debtors retained secured property by remaining current on their loans without reaffirming the underlying debt.

This arrangement was commonly called *ride-through* or *pay and retain*.

The 2005 amendments substantially restricted that approach for personal property securing consumer debts.

Sections 521(a)(2), 521(a)(6), 521(d), and 362(h) impose requirements and consequences concerning a debtor's intentions and actions regarding secured personal property.

A creditor may voluntarily accept payments and permit the debtor to retain collateral without reaffirmation. But the debtor should not assume that this arrangement creates an unconditional right to keep the property.

The loan agreement, applicable state law, the creditor's practices, and compliance with the Bankruptcy Code all matter.

Section 362(h)(1)(B) contains a specific exception when the debtor timely states an intention to reaffirm on the original contract terms but the creditor refuses those terms. That exception is different from a lender voluntarily accepting payments. Its application requires timely compliance with the statement and performance requirements and careful review of the facts.

5. The Statement of Intention

An individual Chapter 7 debtor whose schedules include debts secured by estate property generally must file a statement of intention under § 521(a)(2). Additional requirements apply to specified secured personal property.

Official Form 108 identifies the debtor's intended treatment of the collateral.

The debtor generally must file the statement within thirty days after filing or by the date first set for the meeting of creditors, whichever is earlier, unless the court extends the deadline.

The debtor must ordinarily perform the stated intention within the applicable statutory period.

Section 521(a)(2)(B) generally requires performance within 30 days after the first date set for the meeting of creditors. Section 521(a)(6) separately addresses qualifying personal property securing an allowed purchase-price claim and uses a 45-day period after the first meeting. Rule 4008 generally requires filing the reaffirmation agreement within 60 days after the first date set for the meeting; the court may extend that filing deadline. These are different requirements, and an agreement still must be made before discharge under § 524(c).

Failure to comply may result in termination of the automatic stay concerning the property and other consequences under § 362(h).

A debtor who intends to retain a vehicle should therefore consider reaffirmation and redemption before filing rather than waiting until the discharge is imminent.

6. What Makes a Reaffirmation Agreement Enforceable?

Section 524(c) establishes requirements that must be satisfied before a reaffirmation agreement becomes enforceable.

The agreement generally must be made before discharge, contain the required disclosures, be filed with the bankruptcy court, and satisfy the applicable attorney-certification or court-approval requirements.

The debtor must also retain the statutory right to rescind the agreement.

A creditor's preparation of a reaffirmation agreement does not establish that it is enforceable. Nor does the debtor's signature alone necessarily satisfy the statute.

These safeguards reflect Congress's recognition that reaffirmation can undermine the financial relief bankruptcy is intended to provide.

7. The Bankruptcy Attorney's Certification

When an attorney represents the debtor during negotiation of a reaffirmation agreement, § 524(c)(3) generally requires the attorney to certify that the agreement is fully informed and voluntary, does not impose an undue hardship, and that the attorney has explained its legal consequences, including the consequences of default.

This certification is substantive, not a mere formality.

An attorney may reasonably conclude that reaffirming a particular debt would impose an undue hardship, especially where the debtor's budget shows insufficient income to make the payments.

The attorney should not certify affordability simply because the debtor insists on keeping the collateral.

A debtor's desire to retain a vehicle is understandable, but it does not eliminate counsel's independent professional responsibilities.

8. Reaffirmation Agreements That Create Undue Hardship

Section 524(m) establishes a rebuttable presumption of undue hardship for certain reaffirmation agreements when the debtor's available monthly income, after expenses, is insufficient to make the scheduled payments.

The presumption ordinarily requires judicial review and may be rebutted through an appropriate written explanation identifying additional funds available to make the payments.

If the presumption is not satisfactorily rebutted, the court may disapprove the agreement after the required notice and hearing.

There is an important statutory exception: the § 524(m) presumption does not apply to reaffirmation agreements with qualifying credit unions.

That exception does not eliminate the other requirements governing reaffirmation.

9. Reaffirmation Without an Attorney's Certification

When a debtor was not represented by an attorney during negotiation of the reaffirmation agreement, court approval ordinarily is required for an agreement involving consumer debt secured by personal property.

The court must determine that the agreement does not impose an undue hardship and is in the debtor's best interest.

Section 524(c)(6)(B) provides an exception to that particular approval requirement for consumer debts secured by real property.

Whether an attorney represented the debtor during the reaffirmation negotiations is therefore important. The absence of an attorney's certification is not necessarily equivalent to the absence of representation.

10. The Right to Rescind a Reaffirmation Agreement

A debtor may rescind a reaffirmation agreement before discharge or within sixty days after the agreement is filed with the bankruptcy court, whichever is later.

Rescission is accomplished by giving notice to the creditor.

The debtor should preserve evidence that the notice was timely delivered.

Rescission eliminates the agreement's reaffirmation effect, but it does not necessarily eliminate the creditor's underlying lien or the consequences of default under applicable law.

Because the deadline is statutory, a debtor who develops concerns about reaffirmation should act promptly.

11. Redemption as an Alternative

Under 11 U.S.C. § 722, an individual Chapter 7 debtor may redeem qualifying tangible personal property intended primarily for personal, family, or household use by paying the creditor the amount of its allowed secured claim.

Section 722 requires a lien securing a dischargeable consumer debt and property that has been exempted or abandoned by the trustee. It requires payment of the allowed secured claim in full at redemption; bankruptcy does not compel the creditor to accept a new installment arrangement.

For an automobile, redemption may allow the debtor to retain the vehicle without reaffirming an underwater loan.

Suppose a vehicle is worth $13,000 but the outstanding loan balance is $21,000.

A qualifying redemption may permit the debtor to retain the vehicle by paying the applicable secured value rather than the entire contractual balance.

Redemption generally requires payment in full unless the creditor agrees to another arrangement.

Specialized redemption financing may be available, but the debtor must evaluate the new loan's interest rate, fees, and total repayment cost.

12. Voluntary Payments Are Not Necessarily Reaffirmation

Section 524(f) expressly permits a debtor to voluntarily repay a discharged debt.

A debtor may therefore choose to make payments on an obligation without necessarily entering into an enforceable reaffirmation agreement.

But voluntary repayment does not automatically require the creditor to maintain a particular credit relationship or permit retention of collateral.

Nor may a creditor use the possibility of voluntary repayment as a means to coerce collection of a discharged personal obligation.

The distinction between voluntary payment and enforceable personal liability is central to the discharge's protection.

13. Credit Unions and Cross-Collateralization

Credit union loans deserve special attention because some credit agreements contain cross-collateralization provisions.

A vehicle may secure not only the automobile loan but also other obligations owed to the credit union.

For example, a debtor might owe $14,000 on an automobile loan and $6,000 on a credit card issued by the same credit union.

Depending on the agreements and applicable law, the credit union may assert that the automobile also secures the credit card obligation.

The debtor should not assume that paying the automobile loan alone necessarily satisfies every lien affecting the vehicle.

Cross-collateralization provisions must be examined for validity, scope, and enforceability.

The credit union's special treatment under § 524(m)(2) adds another reason to examine reaffirmation proposals carefully.

14. Should a Debtor Reaffirm a Mortgage?

Mortgage reaffirmation presents different considerations from reaffirmation of an automobile loan.

A bankruptcy discharge generally eliminates personal liability on a dischargeable mortgage obligation while leaving the mortgage lien enforceable against the property.

A homeowner may therefore remain obligated to make payments to prevent foreclosure without necessarily remaining personally liable for a postforeclosure deficiency.

Reaffirming a mortgage may restore personal liability that would otherwise be discharged.

A homeowner should not assume that mortgage reaffirmation is required merely to continue making payments or retain the residence.

The mortgage documents, lender practices, applicable law, and any proposed reaffirmation terms should be examined.

15. Reaffirmation and Credit Reporting

Some debtors consider reaffirmation because they believe it will improve their credit scores.

A creditor may report payments on a reaffirmed obligation, but reaffirmation does not guarantee favorable credit reporting or an improved credit score.

Conversely, a creditor may decline to report voluntary payments on a discharged debt.

The debtor should not assume that reaffirmation is necessary or advisable solely to obtain payment-history reporting.

The possibility of a credit-reporting benefit should be weighed against the legal consequences of preserving personal liability.

16. What Happens if the Debtor Defaults After Reaffirmation?

A valid reaffirmation agreement generally allows the creditor to enforce the reaffirmed debt according to its terms and applicable law.

For secured debts, that may include repossession or foreclosure.

If the collateral is sold and a deficiency remains, the creditor may be entitled to pursue the debtor personally, subject to applicable limitations.

The creditor may seek a judgment and employ lawful collection remedies.

This is the principal financial danger of reaffirmation: a debt that could have been discharged remains enforceable after bankruptcy.

17. What if the Reaffirmation Agreement Is Invalid?

An agreement that fails to satisfy § 524(c) may be unenforceable as a reaffirmation agreement.

The debtor's underlying personal liability may therefore remain discharged.

However, the creditor may still possess enforceable lien rights.

A dispute over reaffirmation enforceability may require examination of the agreement, filing date, discharge date, disclosures, attorney certification, and any court approval.

A creditor's attempt to collect personal liability under an unenforceable agreement may also raise discharge-injunction issues.

18. Reaffirmation Should Be Evaluated Against the Debtor's Postbankruptcy Budget

A debtor's financial condition after discharge should be the starting point for evaluating reaffirmation.

The debtor should consider whether the monthly payment is affordable, whether the collateral is worth retaining, and whether a future interruption in income would create substantial exposure.

An automobile loan that was manageable before bankruptcy may remain unnecessarily burdensome afterward.

The debtor should also compare the remaining debt with the vehicle's value and expected useful life.

A reliable vehicle with favorable financing presents a different decision from an aging vehicle requiring expensive repairs and carrying a substantial negative-equity balance.

Conclusion

Reaffirmation agreements are among the most consequential decisions a Chapter 7 debtor may make.

They can preserve access to essential collateral, but they can also preserve personal liability that bankruptcy otherwise would eliminate.

The debtor should understand the difference between the creditor's lien and the debtor's personal obligation, the availability of redemption or other alternatives, and the financial consequences of future default.

A bankruptcy discharge is intended to provide a fresh start. Reaffirmation should not unnecessarily recreate the financial burden the debtor sought to escape.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 524 — Reaffirmation agreements, disclosures, rescission, attorney certification, court approval, and undue hardship.
- 11 U.S.C. § 521 — Statement of intention and requirements concerning secured personal property.
- 11 U.S.C. § 362(h) — Termination of the stay concerning certain personal property.
- 11 U.S.C. § 722 — Redemption of qualifying personal property.
- Federal Rule of Bankruptcy Procedure 4008 — Filing reaffirmation agreements.
- Federal Rule of Bankruptcy Procedure 4004 — Discharge procedures and relevant timing.

Selected decisions

- *In re Jones*, 591 F.3d 308 (4th Cir. 2010) — Addresses the post-BAPCPA requirements for retaining secured personal property and the consequences of noncompliance.
- *In re Donald*, 343 B.R. 524 (Bankr. E.D.N.C. 2006) — Examines reaffirmation and the treatment of secured personal property following the 2005 amendments.
- *City of Chicago v. Fulton*, 592 U.S. 154 (2021) — Addresses the automatic stay and retention of property seized before bankruptcy.
- *Taggart v. Lorenzen*, 587 U.S. 554 (2019) — Establishes the civil contempt standard for violating the bankruptcy discharge injunction.

Which Debts Can and Cannot Be Discharged in Chapter 7 Bankruptcy?

BELSKY BANKRUPTCY LEGAL LIBRARY | DISCHARGE AND DEBT RELIEF

By Alan J. Belsky, Attorney at Law

Bankruptcy Eliminates Many Debts, But Not Every Debt

The principal benefit of Chapter 7 bankruptcy is the discharge of qualifying debts. A discharge generally eliminates the debtor's personal legal obligation to pay debts covered by the discharge and prohibits creditors from attempting to collect those obligations as personal liabilities.

Most ordinary unsecured consumer debts are dischargeable. Credit card balances, medical bills, personal loans, and many civil judgments can ordinarily be eliminated.

But some obligations survive bankruptcy because Congress has determined that they should not be discharged, or because a creditor establishes a statutory exception.

The distinction is not always obvious. A debt arising from a lawsuit may be dischargeable even though a judgment has been entered. Conversely, a debt that has never been reduced to judgment may be nondischargeable because of the circumstances in which it arose.

The nature of the obligation—not merely the creditor's name or the form of the debt—determines whether it can be discharged.

1. What Does a Bankruptcy Discharge Actually Do?

Under 11 U.S.C. § 727, an eligible Chapter 7 debtor ordinarily receives a discharge of debts arising before the bankruptcy petition, except as provided by the Bankruptcy Code.

Section 524(a) makes the discharge effective as an injunction against attempts to collect discharged debts as personal liabilities.

A discharged creditor generally cannot continue collection calls, file a lawsuit to recover the discharged personal debt, garnish wages, or enforce a personal judgment for that obligation.

However, discharge of personal liability does not necessarily eliminate a valid lien against property.

A mortgage lender may retain the right to foreclose, and a vehicle lender may retain repossession rights, even though the debtor's personal liability has been discharged.

The distinction between personal liability and secured rights is fundamental to understanding bankruptcy.

2. Credit Card Debts

Ordinary credit card balances are generally dischargeable in Chapter 7.

This includes balances arising from purchases, cash advances, interest, and fees, subject to applicable exceptions.

However, credit card debt may become nondischargeable when it was incurred through fraud.

For example, a debtor who makes purchases while knowingly misrepresenting an intention to repay may face a dischargeability challenge.

The Bankruptcy Code also creates presumptions of nondischargeability for certain luxury purchases and cash advances incurred shortly before bankruptcy, subject to periodically adjusted dollar thresholds.

The creditor must satisfy the applicable statutory requirements.

The mere fact that a debtor used a credit card shortly before filing does not automatically establish fraud.

3. Medical Bills

Medical bills are generally dischargeable unsecured debts.

This includes many obligations arising from hospital treatment, physician services, emergency care, diagnostic testing, and other healthcare expenses.

A debtor may discharge medical debt even when the treatment was necessary or the creditor is a hospital or medical professional.

However, discharge of an unpaid medical bill does not necessarily resolve separate issues involving insurance, liens, reimbursement rights, or ongoing contractual relationships.

For example, a medical provider may assert a statutory or contractual lien against a personal injury recovery. The validity and enforceability of that lien require separate analysis.

4. Personal Loans and Finance Company Debts

Ordinary unsecured personal loans are generally dischargeable.

This includes many bank loans, finance company obligations, online installment loans, and debts owed to individuals.

However, a creditor may challenge dischargeability when the loan was obtained through materially fraudulent representations or other conduct falling within § 523.

A loan secured by collateral also raises separate lien issues.

Discharge of the personal obligation ordinarily does not eliminate a valid security interest.

5. Judgments and Lawsuit Debts

A common misconception is that a debt cannot be discharged once a creditor obtains a judgment.

That is generally incorrect.

A judgment based on an ordinary credit card account, personal loan, or other dischargeable obligation ordinarily remains dischargeable.

The judgment does not automatically change the underlying character of the debt.

However, a judgment lien against property may survive unless avoided or otherwise affected under applicable law.

Judgments arising from fraud, intentional injuries, or other statutory exceptions may present different issues.

The nature of the underlying claim is therefore more important than the fact that judgment was entered.

6. Deficiency Balances After Repossession or Foreclosure

A deficiency occurs when collateral is sold for less than the amount owed.

For example, a debtor may owe $20,000 on a vehicle repossessed and sold for $12,000.

The remaining deficiency may constitute an unsecured debt.

Ordinary prepetition deficiency balances are generally dischargeable in Chapter 7.

The result may differ if the debtor entered into a valid reaffirmation agreement or the obligation falls within another exception.

A foreclosure deficiency may likewise be dischargeable, although the underlying mortgage lien and foreclosure rights must be analyzed separately.

7. Debts Owed to Family Members and Friends

Loans from relatives and friends are generally treated as debts under the Bankruptcy Code.

The debtor must disclose them even if the creditor has never demanded repayment.

A genuine unsecured family loan may be dischargeable just like a bank loan.

But payments made to relatives before bankruptcy can raise preference issues because insiders are subject to an extended preference lookback period under § 547.

A debtor should not omit a family obligation from the schedules simply because the debtor intends to repay it voluntarily.

Section 524(f) permits voluntary repayment of discharged debts, but the creditor generally cannot compel payment after discharge.

8. Student Loans

Student loans receive special treatment under 11 U.S.C. § 523(a)(8).

Certain educational loans and obligations are excepted from discharge unless repayment would impose an undue hardship on the debtor and the debtor's dependents.

The exception does not necessarily cover every debt associated with education.

Whether a particular private educational loan qualifies under § 523(a)(8) may require examining the loan's terms, purpose, and statutory classification.

Undue hardship

The Fourth Circuit applies the *Brunner* framework to undue-hardship determinations.

In *Educational Credit Management Corp. v. Frushour*, 433 F.3d 393 (4th Cir. 2005), the court addressed the demanding requirements for discharging student loans.

The debtor generally must establish an inability to maintain a minimal standard of living while repaying the loans, additional circumstances indicating that the condition is likely to persist, and good-faith efforts to repay.

Student loan discharge ordinarily requires an adversary proceeding.

Federal procedures introduced in 2022 also provide a framework for potentially resolving certain federal student loan undue-hardship cases through stipulated facts and coordinated review by the Department of Justice and Department of Education.

Student loans are therefore not categorically impossible to discharge, but they require separate legal analysis.

9. Income Taxes

Some income tax debts may be discharged in Chapter 7.

The result depends on the type of tax, the relevant tax year, the filing and assessment dates, and other statutory requirements.

A simplified description often refers to three-year, two-year, and 240-day timing rules.

However, these rules contain exceptions, tolling provisions, and additional conditions.

For example, a debtor may face different consequences when a return was filed late, a tax assessment occurred recently, or the debtor engaged in fraudulent conduct or willful tax evasion.

Tax liens may also survive discharge even when personal liability for the underlying tax is eliminated.

A debtor should not assume that all old tax debts are dischargeable merely because several years have passed.

10. Payroll Taxes and Trust Fund Obligations

Certain taxes collected or withheld from others and required to be paid to the government receive special treatment.

Trust fund taxes may include amounts withheld from employee wages.

Under § 523(a)(1) and the priority provisions of § 507(a)(8), qualifying trust fund tax obligations generally are not dischargeable.

Business owners and responsible persons may face personal liability for certain unpaid employment taxes.

The fact that a business has closed does not necessarily eliminate those obligations.

11. Child Support and Alimony

Domestic support obligations generally are not dischargeable in Chapter 7.

The Bankruptcy Code defines domestic support obligations in § 101(14A).

Qualifying obligations can include child support, alimony, maintenance, and other debts meeting the statutory definition.

The label assigned to an obligation in a divorce agreement is not always controlling.

A payment described as a property settlement may, depending on its substance and legal characteristics, constitute support.

Domestic support obligations also receive priority treatment in bankruptcy.

12. Property Settlement Obligations Arising From Divorce

Chapter 7 generally does not discharge debts to a spouse, former spouse, or child that fall within § 523(a)(15), even when they are not domestic support obligations.

This provision covers certain obligations incurred in connection with divorce, separation, or related court orders.

The distinction between support and property settlement obligations remains important for priority, enforcement, and other bankruptcy purposes.

However, both categories generally survive an ordinary Chapter 7 discharge.

The treatment of certain non-support divorce obligations can differ in Chapter 13, making chapter selection especially important for debtors with substantial marital settlement obligations.

13. Debts Arising From Fraud

Section 523(a)(2) excepts certain debts obtained through false pretenses, false representations, or actual fraud.

The statute contains different requirements for certain statements concerning financial condition.

A creditor alleging fraud generally must establish the applicable elements in an adversary proceeding.

A mere breach of contract ordinarily does not establish fraud.

Likewise, a debtor's inability to repay a loan does not necessarily mean the debtor fraudulently obtained it.

The circumstances surrounding the transaction are critical.

14. Fraud or Defalcation While Acting in a Fiduciary Capacity

Section 523(a)(4) addresses debts arising from fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny.

The meaning of fiduciary capacity under this provision is narrower than the broad fiduciary concepts used in some other areas of law.

In *Bullock v. BankChampaign, N.A.*, 569 U.S. 267 (2013), the Supreme Court addressed the mental-state requirement for defalcation.

Not every negligent accounting error or breach of an ordinary contractual duty establishes nondischargeability.

The nature of the fiduciary relationship and the debtor's conduct must be examined.

15. Willful and Malicious Injury

Under § 523(a)(6), certain debts arising from willful and malicious injury by the debtor to another person or another person's property are excepted from discharge.

The Supreme Court addressed the meaning of willful injury in *Kawaauhau v. Geiger*, 523 U.S. 57 (1998).

The Court distinguished intentional injury from conduct that merely produces an unintended injury.

Ordinary negligence and even some forms of reckless conduct do not automatically satisfy the statutory standard.

This distinction is particularly important for civil judgments arising from accidents, professional negligence, and other tort claims.

16. Automobile Accident Judgments

A judgment arising from an automobile accident is not automatically nondischargeable.

An ordinary negligence judgment generally may be discharged.

However, § 523(a)(9) excepts qualifying debts for death or personal injury caused by the debtor's operation of a motor vehicle, vessel, or aircraft when the operation was unlawful because the debtor was intoxicated by alcohol, a drug, or another substance.

The statutory requirements must be satisfied.

A judgment for ordinary negligent driving therefore presents a different dischargeability issue from a qualifying intoxicated-driving injury claim.

17. Fines, Penalties, and Restitution

Certain fines, penalties, forfeitures, and restitution obligations are excepted from discharge.

Section 523(a)(7) addresses qualifying governmental fines and penalties that are not compensation for actual pecuniary loss.

Criminal restitution obligations may also survive bankruptcy under applicable statutory provisions and controlling decisions.

The treatment of civil penalties, regulatory assessments, and restitution depends on the nature of the obligation.

The fact that a payment is owed to a government agency does not automatically determine its dischargeability.

18. Debts Not Properly Scheduled

Section 523(a)(3) addresses certain debts that were neither listed nor scheduled in time to permit the creditor to protect its rights, subject to statutory qualifications.

The consequences of omitting a creditor can differ depending on whether the case is a no-asset case, whether a claims deadline was established, and whether the debt involves fraud or another exception requiring creditor action.

In re Stecklow, 144 B.R. 314 (Bankr. D. Md. 1992), is a Maryland bankruptcy court decision, not a Fourth Circuit decision at 144 F.3d 221. It explains why reopening a no-asset Chapter 7 case merely to add an omitted creditor does not itself change whether the debt was discharged. Section 523(a)(3), the existence of a claims deadline, notice, and the character of the debt still control.

A debtor should never intentionally omit a creditor from the schedules.

Complete disclosure is required regardless of whether an omitted debt might ultimately be discharged.

19. Which Debts Require a Creditor to File an Adversary Proceeding?

Not every exception to discharge operates through the same procedure.

Under § 523(c) and Federal Rule of Bankruptcy Procedure 4007(c), creditors seeking determinations under certain provisions—principally § 523(a)(2), (4), and (6)—generally must file a timely dischargeability complaint.

The ordinary deadline is sixty days after the first date set for the meeting of creditors, subject to the rule's requirements and possible timely extensions.

Other debts, including many domestic support obligations, qualifying taxes, and certain student loans, may be excepted from discharge without the creditor first obtaining a judgment within that same deadline.

A debtor should not assume that the absence of a creditor objection means every debt has been discharged.

20. Denial of Discharge Is Different From Nondischargeability of a Particular Debt

There is a fundamental distinction between denying discharge of one debt and denying the debtor's entire Chapter 7 discharge.

Section 523 generally addresses whether particular obligations survive.

Section 727 addresses circumstances in which the debtor may be denied a discharge altogether.

Grounds for denial can include specified fraudulent transfers, concealment of property, false oaths, destruction or withholding of records, and other misconduct.

A debtor who loses the right to a general discharge may remain liable for numerous debts that otherwise would have been dischargeable.

This is one reason accurate schedules, complete disclosure, and cooperation with the trustee are essential.

21. What Happens When a Creditor Tries to Collect a Discharged Debt?

Section 524(a) generally prohibits collection of discharged debts as personal liabilities.

A creditor that knowingly pursues prohibited collection may face enforcement proceedings.

In *Taggart v. Lorenzen*, 587 U.S. 554 (2019), the Supreme Court held that civil contempt sanctions may be appropriate when there is no fair ground of doubt as to whether the discharge order prohibited the creditor's conduct.

A debtor should preserve collection letters, account statements, communications, and other evidence of post-discharge collection efforts.

But the debtor must first determine whether the particular debt was actually discharged and whether the creditor is enforcing personal liability or a surviving lien.

22. Why Debt Classification Should Be Reviewed Before Filing

A debtor's financial problems may involve a combination of dischargeable and nondischargeable obligations.

For example, an individual may owe $70,000 in credit card debt, $20,000 in recent income taxes, and $15,000 in domestic support arrears.

Chapter 7 may eliminate the credit card debt while leaving significant tax and support obligations.

The debtor's financial condition may improve substantially, but the remaining obligations still require attention.

In some circumstances, Chapter 13 may offer a better mechanism for managing priority debts or curing arrears.

The proper chapter should therefore be selected only after the debts have been classified.

Conclusion

Chapter 7 bankruptcy can eliminate many ordinary unsecured obligations, including credit card balances, medical bills, personal loans, and numerous civil judgments.

But Congress has created exceptions for particular debts, including certain taxes, domestic support obligations, student loans, fraud-related debts, intentional injuries, and specified penalties.

Some exceptions apply without a creditor filing a timely adversary proceeding. Others require the creditor to act within strict procedural deadlines.

The debtor must also distinguish between discharge of personal liability and the continued enforceability of liens.

The central question is not merely how much a debtor owes, but which obligations bankruptcy can legally eliminate and which will remain afterward.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 524 — Effect of discharge and discharge injunction.
- 11 U.S.C. § 727 — Chapter 7 discharge and grounds for denial.
- 11 U.S.C. § 507 — Priority claims.
- Federal Rule of Bankruptcy Procedure 4007 — Determination of dischargeability.

Selected decisions

- *Grogan v. Garner*, 498 U.S. 279 (1991) — Establishes the preponderance-of-the-evidence standard for dischargeability exceptions.
- *Cohen v. de la Cruz*, 523 U.S. 213 (1998) — Addresses the scope of debt arising from fraud.
- *Kawaauhau v. Geiger*, 523 U.S. 57 (1998) — Distinguishes intentional injury from negligent or reckless conduct under § 523(a)(6).
- *Bullock v. BankChampaign, N.A.*, 569 U.S. 267 (2013) — Addresses the mental-state requirement for fiduciary defalcation.
- *Educational Credit Management Corp. v. Frushour*, 433 F.3d 393 (4th Cir. 2005) — Addresses undue hardship for student loan discharge.
- *Taggart v. Lorenzen*, 587 U.S. 554 (2019) — Establishes the civil contempt standard for violations of the discharge injunction.

Discharging Income Taxes in Chapter 7 Bankruptcy: The Three-Year, Two-Year, and 240-Day Rules—and Their Exceptions

BELSKY BANKRUPTCY LEGAL LIBRARY | TAX DEBTS AND DISCHARGEABILITY

By Alan J. Belsky, Attorney at Law

Bankruptcy Can Discharge Some Income Taxes

A common misconception is that income taxes cannot be discharged in bankruptcy. In fact, certain federal and Maryland income tax obligations may be eliminated through Chapter 7, provided the applicable statutory requirements are satisfied.

The rules are considerably more complicated than simply determining how old the tax debt is.

A tax obligation may relate to a return filed several years ago but remain nondischargeable because of a recent assessment, a late-filed return, a prior bankruptcy, or another event affecting the statutory periods.

Conversely, an individual who owes substantial income taxes may be able to discharge those obligations while retaining property protected by applicable exemptions.

The analysis requires examining each tax year separately, identifying the relevant return and assessment dates, and determining whether any exceptions or tolling provisions apply.

The governing provisions include 11 U.S.C. §§ 507(a)(8), 523(a)(1), and 507(a)(8)'s accompanying timing rules.

1. The Difference Between Discharging Tax Liability and Eliminating a Tax Lien

Two separate questions must be considered.

First, can bankruptcy eliminate the debtor's personal liability for the tax?

Second, does the taxing authority possess a valid lien that survives the discharge?

A Chapter 7 discharge may eliminate personal liability for qualifying income taxes without necessarily extinguishing a properly perfected prepetition tax lien.

For example, the IRS may have recorded a federal tax lien against the debtor's property before bankruptcy.

Even if the underlying personal tax obligation is discharged, the lien may remain enforceable against property to which it validly attached, subject to applicable law.

Thus, a debtor may emerge from bankruptcy free of personal liability but still need to address a surviving lien before selling or refinancing property.

The existence and scope of federal or Maryland tax liens should be examined before filing.

2. The Three-Year Rule

Under 11 U.S.C. § 507(a)(8)(A)(i), certain income taxes receive priority treatment when the relevant return was last due, including extensions, within three years before the bankruptcy petition.

Because qualifying priority taxes are generally excepted from discharge under § 523(a)(1)(A), the three-year period is a fundamental part of the analysis.

Example

A debtor owes federal income taxes for tax year 2022.

The ordinary return due date was April 18, 2023.

If the debtor files bankruptcy before the applicable three-year period has expired, the tax may remain nondischargeable under the priority provisions.

If the debtor files after the period has expired, the three-year rule alone may no longer prevent discharge.

However, the debtor must still satisfy the other applicable requirements.

Extensions matter

If the debtor obtained an extension of time to file the return, the extended due date generally controls the three-year calculation.

A debtor who assumes the original April filing deadline applies despite an extension may file bankruptcy prematurely.

The actual return due date, including extensions, should be verified.

3. The Two-Year Rule

Section 523(a)(1)(B)(ii) generally excepts from discharge taxes for which a required return or equivalent report or notice was filed or given after its due date and within two years before the bankruptcy petition.

This provision is particularly important for taxpayers who filed delinquent returns.

Example

A debtor's 2020 income tax return was due in 2021 but was not filed until July 1, 2025.

The debtor files Chapter 7 on October 1, 2026.

Although the tax year is relatively old, the late return was filed less than two years before bankruptcy.

The tax may therefore remain nondischargeable.

Waiting until the applicable two-year period has expired may change the result, but only if the filing qualifies as a return for bankruptcy purposes and all other discharge requirements are satisfied.

4. The 240-Day Assessment Rule

Section 507(a)(8)(A)(ii) generally grants priority status to certain income taxes assessed within 240 days before the bankruptcy filing.

The assessment date is not necessarily the date the return was filed or the date the tax became due.

An assessment is a formal tax administration event.

The IRS may assess additional taxes following an audit, amended return, or other determination.

Example

A debtor timely filed a 2020 return but was later audited.

The IRS assessed additional income tax on June 1, 2026.

The debtor files Chapter 7 on October 1, 2026.

The additional assessment occurred fewer than 240 days before filing.

The assessed tax may therefore remain nondischargeable even though the original return was due years earlier.

The 240-day period can also be suspended or extended under statutory provisions.

5. All Applicable Requirements Must Be Satisfied

The three-year, two-year, and 240-day rules are not alternative ways to qualify for discharge.

A debtor generally must satisfy all applicable requirements.

A tax that is old enough under the three-year rule may still be nondischargeable because the return was filed late within two years of bankruptcy.

A tax associated with a return filed more than two years earlier may still be nondischargeable because of a recent assessment.

And even when the timing requirements appear satisfied, fraud, willful evasion, or a failure to file a legally qualifying return may prevent discharge.

A proper analysis should therefore be performed tax year by tax year.

The three timing rules are not the entire statute. Section 507(a)(8)(A)(iii) also addresses qualifying income taxes not assessed before filing but still assessable afterward, except for the specified unfiled-return and fraud or evasion categories. An unresolved audit or open assessment period must therefore be checked even when no assessment appears within the preceding 240 days.

6. Late-Filed Returns: A Particularly Difficult Issue

The treatment of late-filed income tax returns has generated substantial litigation.

The Bankruptcy Code defines the term *return* for purposes of § 523(a) through language added by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.

The definition requires satisfaction of applicable nonbankruptcy law, including applicable filing requirements, while addressing certain returns prepared under Internal Revenue Code § 6020.

Courts have disagreed about whether, and under what circumstances, a delinquent return qualifies as a return for dischargeability purposes.

Some courts have adopted interpretations under which a return filed even one day late may fail to qualify, subject to statutory exceptions.

Other courts have applied different approaches, including consideration of whether the filing represents an honest and reasonable attempt to comply with tax law.

The governing jurisdiction is critical.

A debtor should never assume that filing a delinquent return and waiting two years necessarily makes the associated tax dischargeable.

7. Substitute Returns Prepared by the IRS

When a taxpayer fails to file a required return, the IRS may prepare a substitute for return under Internal Revenue Code § 6020(b).

A substitute return permits the IRS to determine and assess tax liability based on available information. It does not necessarily have the same bankruptcy consequences as a return voluntarily filed by the taxpayer.

Section 523(a)'s definition of a return specifically excludes returns made under § 6020(b), while recognizing qualifying returns prepared under § 6020(a).

This distinction can be decisive.

A taxpayer who permits the IRS to assess taxes through a substitute return and subsequently files a Form 1040 may face substantial difficulty establishing dischargeability.

The Fourth Circuit's decision in *In re Moroney*

In *In re Moroney*, 352 F.3d 902 (4th Cir. 2003), the Fourth Circuit considered whether Forms 1040 filed after the IRS had already assessed deficiencies based on substitute returns qualified as returns for bankruptcy discharge purposes.

Applying the pre-2005 statutory framework, the court concluded that the debtor's belated filings did not constitute an honest and reasonable attempt to satisfy tax-law requirements.

The decision remains important to understanding the Fourth Circuit's treatment of late-filed returns, although its application must be evaluated in light of the statutory amendments enacted in 2005.

For Maryland debtors, a history of unfiled returns and substitute assessments requires particularly careful review.

When a taxpayer fails to file a required federal income tax return, the IRS may prepare a substitute for return under Internal Revenue Code § 6020(b).

A substitute return allows the IRS to determine and assess a tax liability, but it generally does not satisfy the Bankruptcy Code's definition of a return filed by the taxpayer.

The distinction matters because § 523(a)(1)(B)(i) excepts from discharge taxes for which a required return was not filed or given.

Section 523(a)'s definition of a return expressly excludes returns made under § 6020(b), while recognizing certain returns prepared under § 6020(a).

A taxpayer who subsequently files an actual return after the IRS has assessed a substitute return may face additional dischargeability questions.

The Fourth Circuit's decision in *In re Moroney*, 352 F.3d 902 (4th Cir. 2003), addressed late-filed returns following IRS assessments under the law then applicable.

Because *Moroney* preceded the 2005 statutory amendments, its application must be considered alongside the amended statutory definition and subsequent decisions.

The practical problem

A taxpayer may believe that filing a delinquent return corrects the problem created by the IRS substitute return.

It may correct or reduce the assessed tax liability, but it does not necessarily establish that the debt will become dischargeable after two years.

The complete filing and assessment history must be reviewed.

8. Fraudulent Returns and Willful Tax Evasion

Even when the ordinary timing requirements are satisfied, § 523(a)(1)(C) excepts from discharge tax debts associated with fraudulent returns or willful attempts to evade or defeat the tax.

The statute addresses two distinct categories of misconduct: making a fraudulent return and willfully attempting to evade or defeat tax liability.

The second category can involve conduct beyond the filing of a false return.

Examples potentially relevant to the inquiry include concealment of assets, misleading financial transactions, and other affirmative efforts to avoid tax obligations.

However, the mere inability to pay taxes is not necessarily equivalent to willful evasion.

In re Griffith

In *In re Griffith*, 206 F.3d 1389 (11th Cir. 2000) (en banc), the court addressed willful attempts to evade tax payment, illustrating that dischargeability can depend on conduct occurring after the tax liability arose.

The applicable Fourth Circuit authorities and the debtor's actual conduct must be examined before concluding that the exception applies.

A debtor who honestly reports income but lacks sufficient resources to pay may present a materially different case from one who intentionally conceals assets to prevent collection.

Even when the ordinary timing requirements are satisfied, certain tax debts remain nondischargeable because of the debtor's conduct.

Under § 523(a)(1)(C), a tax debt is excepted from discharge if the debtor made a fraudulent return or willfully attempted in any manner to evade or defeat the tax.

The provision can apply to conduct beyond filing a fraudulent tax return.

Courts may consider affirmative acts intended to evade tax obligations, including concealment of assets, misleading financial transactions, or other conduct demonstrating the requisite willfulness.

Mere inability to pay does not necessarily constitute willful evasion.

The distinction between financial hardship and intentional evasion is important.

In *In re Fegeley*, 118 F.3d 979 (3d Cir. 1997), the court examined willful tax evasion in the dischargeability context.

Fourth Circuit authority and the particular factual circumstances must be considered when evaluating these issues in Maryland.

9. Prior Bankruptcy Filings Can Extend the Tax Periods

One of the most easily overlooked issues is the effect of a prior bankruptcy case.

A previous bankruptcy may suspend certain tax-priority periods, preventing the passage of time from making the taxes dischargeable as quickly as expected.

Section 507(a)(8) includes suspension provisions applicable to specified tax claims.

Under the statutory language, certain periods may be suspended while a prior bankruptcy stay prevents collection, with an additional ninety days.

The Supreme Court's decision in *Young v. United States*, 535 U.S. 43 (2002), addressed equitable tolling of the three-year lookback period in the context of successive bankruptcy filings.

The decision preceded later statutory amendments expressly addressing certain suspensions.

A debtor who filed Chapter 13, obtained a dismissal, and then considers Chapter 7 should not calculate tax dischargeability by simply counting calendar years from the original return due date.

The dates and duration of prior proceedings must be examined.

The ordinary three-year and 240-day periods are subject to statutory suspension provisions.

A debtor cannot safely determine dischargeability by simply counting calendar days from the return due date or assessment date.

Events affecting the calculation may include prior bankruptcy proceedings, offers in compromise, and certain collection due process proceedings.

The applicable statutes must be consulted to determine which period is suspended, for how long, and whether additional days are added.

Prior bankruptcy cases

A previous bankruptcy may suspend certain tax-priority periods.

Section 507(a)(8) contains provisions addressing periods during which collection was prohibited because of a prior bankruptcy, together with additional statutory time.

A debtor who previously filed Chapter 13 and later seeks Chapter 7 relief may therefore discover that an old tax debt remains nondischargeable.

Offers in compromise

A pending offer in compromise may affect the 240-day assessment period under § 507(a)(8)(A)(ii).

The statute specifies the applicable suspension and additional period.

The precise dates of submission, rejection, withdrawal, or termination may matter.

Collection due process proceedings

Certain collection due process proceedings can also affect the calculation.

A debtor should obtain the relevant IRS records rather than relying solely on personal recollection.

10. Offers in Compromise and Collection Proceedings

An offer in compromise may affect the 240-day assessment period.

Section 507(a)(8)(A)(ii) provides for suspension of that period during the time an offer in compromise concerning the tax is pending or in effect, plus thirty days.

Other statutory suspension provisions may apply when collection is prohibited by a prior bankruptcy or another legally relevant proceeding.

The mere passage of 240 calendar days after assessment therefore does not always satisfy the rule.

A taxpayer who has pursued an offer in compromise, filed previous bankruptcies, or participated in collection litigation should obtain a detailed review of the relevant dates.

11. IRS Tax Account Transcripts: Why They Are Essential

A tax return or collection notice ordinarily does not provide all the information necessary to determine dischargeability.

IRS account transcripts can identify important events, including return processing, assessments, additional assessments, payments, and certain administrative activity.

For each tax year, counsel should determine the original and extended return due dates, actual filing date, assessment dates, and events potentially suspending the applicable periods.

An IRS account transcript is an important starting point, but it may not conclusively establish every relevant fact.

Additional records may be necessary to determine whether a return qualifies under bankruptcy law, whether a prior proceeding affected the calculation, or whether the IRS asserts fraud or willful evasion.

Maryland income tax liabilities require corresponding information from the Comptroller of Maryland.

An IRS account transcript can identify important events affecting dischargeability, including return processing, assessments, payments, and certain account adjustments.

Additional records may be needed to determine whether an extension was granted, whether an offer in compromise was pending, or whether other events suspended the statutory periods.

A proper tax-discharge analysis may require:

- Account transcripts for each tax year.
- Return transcripts or copies of filed returns.
- Assessment dates and audit records.
- Information concerning filing extensions.
- Records of prior bankruptcy proceedings.
- Offers in compromise and collection due process proceedings.
- Federal tax lien notices.

An account transcript is useful evidence, but it should not be assumed to resolve every legal issue concerning dischargeability.

12. Federal and Maryland Income Taxes

Federal income taxes and Maryland income taxes are governed by different tax administration systems, but their dischargeability in bankruptcy is generally determined under the applicable provisions of the federal Bankruptcy Code.

The Maryland Comptroller may have different assessment procedures, collection records, and statutory lien rights from the IRS.

Accordingly, a debtor should not assume that federal and Maryland liabilities for the same tax year have identical assessment dates or dischargeability consequences.

Each obligation should be evaluated separately.

The debtor may also owe local income taxes administered through Maryland's income tax system.

Those liabilities must be identified and classified rather than assumed to follow the federal assessment history.

Maryland income tax debts may also be dischargeable under the Bankruptcy Code.

The federal dischargeability provisions apply to qualifying state income taxes, subject to the particular tax obligations and applicable filing and assessment rules.

The Comptroller of Maryland may assess taxes, pursue collection, and assert liens under Maryland law.

A debtor may owe both federal and Maryland income taxes for the same year, but the dischargeability analysis should be performed separately for each taxing authority.

The relevant assessment dates, return-filing history, and collection proceedings may differ.

A determination that federal income taxes are dischargeable does not automatically establish that the corresponding Maryland taxes are dischargeable.

13. Tax Liens May Survive Bankruptcy

Even when personal liability for income taxes is discharged, a valid prepetition tax lien may remain enforceable against property to which it attached.

This distinction can be especially important for homeowners.

Suppose a debtor owes $40,000 in otherwise dischargeable federal income taxes, but the IRS previously recorded a valid notice of federal tax lien.

The Chapter 7 discharge may eliminate the debtor's personal liability without automatically eliminating the lien.

The lien's continued enforceability depends on federal tax lien law, the property involved, and the circumstances of the bankruptcy.

A debtor who intends to sell or refinance a residence may need to address a surviving tax lien notwithstanding the discharge.

The effect of exemptions on federal tax liens also requires special attention. Section 522(c)(2)(B) preserves certain tax-lien rights notwithstanding exemptions.

A valid prepetition tax lien may survive bankruptcy even when personal liability for the underlying tax is discharged.

Federal tax liens arise under Internal Revenue Code §§ 6321 and 6322 when the statutory requirements are satisfied.

The extent to which the lien attaches to property, and the effect of bankruptcy on that lien, require separate examination.

For example, a debtor may own a residence with substantial equity and owe old federal income taxes that otherwise qualify for discharge.

If the IRS possesses an enforceable prepetition lien against the property, the discharge may not eliminate that lien.

The debtor may still need to address the lien in connection with a sale, refinancing, or other disposition.

The bankruptcy discharge generally does not permit the IRS to collect discharged personal liability through ordinary post-discharge collection remedies, but surviving in rem rights must be distinguished.

14. What About Taxes Secured by a Judgment or Other Lien?

A taxing authority may possess collection rights arising from statutory liens, recorded instruments, or other enforcement mechanisms.

The existence of a lien does not necessarily establish that the underlying personal tax debt is nondischargeable.

Conversely, dischargeability of the personal debt does not necessarily invalidate the lien.

The analysis requires distinguishing the underlying obligation, the taxing authority's secured rights, and the property subject to enforcement.

A debtor should not assume that listing the tax debt as unsecured in the bankruptcy schedules eliminates an existing lien.

The existence of a lawsuit or judgment does not, by itself, determine whether the underlying income tax is dischargeable.

The Bankruptcy Code's tax-discharge provisions generally focus on the nature of the tax, filing history, assessment dates, and applicable exceptions.

However, litigation may create additional issues concerning liens, judgments, and the government's enforcement rights.

A debtor should not assume that a tax becomes nondischargeable simply because the IRS has obtained a judgment.

Nor should the debtor assume that discharging personal liability eliminates all consequences of the judgment.

15. Estimated Taxes and Self-Employment Taxes

Self-employed individuals frequently accumulate income tax liabilities because insufficient estimated payments were made during the year.

Ordinary federal income taxes attributable to self-employment may be dischargeable if the applicable requirements are satisfied.

The self-employment tax component of federal income taxation also requires proper classification under the Bankruptcy Code.

A self-employed debtor may additionally owe employment or withholding taxes arising from employees.

Those obligations can receive materially different treatment.

The important distinction is not simply whether the debtor operated a business, but the legal nature of the particular tax.

16. Trust Fund Taxes Are Different

Employers generally must withhold certain taxes from employees' wages and remit those amounts to the government.

Qualifying trust fund taxes receive special priority treatment under § 507(a)(8)(C).

They generally are not dischargeable under § 523(a)(1)(A).

Responsible individuals may also face personal liability for certain unpaid trust fund taxes.

The fact that a business has ceased operating, dissolved, or filed bankruptcy does not necessarily eliminate the responsible person's liability.

A debtor with employment tax problems should not assume that the passage of three years makes those obligations dischargeable.

Not all tax obligations are governed by the ordinary income-tax timing rules.

Taxes required to be collected or withheld from others and paid to the government may receive priority treatment under § 507(a)(8)(C).

These obligations can include certain employment withholding taxes.

Trust fund taxes generally are not dischargeable under the ordinary three-year, two-year, and 240-day framework.

A business owner or other responsible person may also face personal liability under federal tax law for certain unpaid trust fund taxes.

The closing of a business does not necessarily eliminate those obligations.

The classification of the tax is therefore essential.

17. Tax Penalties and Interest

Tax penalties and interest require separate analysis.

Interest on a tax debt may receive treatment related to the underlying tax obligation, subject to applicable law.

Penalties may be dischargeable or nondischargeable depending on their character, the underlying transaction, and the applicable provisions of § 523(a)(7).

The treatment of penalties is not always identical to that of the underlying tax.

A debtor's tax account should therefore be examined by component rather than treating the entire balance as a single obligation.

The dischargeability of interest generally follows the treatment of the underlying tax obligation, subject to applicable law and the nature of the interest.

Penalties may be governed by different provisions, including § 523(a)(7).

Certain penalties may be dischargeable even when the associated tax receives different treatment, depending on their nature and the applicable statutory requirements.

A debtor should not assume that every component of a tax account has the same discharge status.

The principal tax, interest, and penalties should be identified separately.

18. Does Filing Chapter 7 Stop IRS Collection?

The automatic stay generally prohibits many tax collection activities while it remains effective.

For example, the IRS ordinarily may not continue an ordinary levy against estate property merely because the debtor owes prepetition income taxes.

However, § 362(b)(9) excepts certain tax-related activities, including specified audits, assessments, notices, and demands for returns.

Filing bankruptcy does not prohibit every communication or administrative action by a taxing authority.

Moreover, the automatic stay does not permanently eliminate collection rights relating to nondischargeable taxes.

After the stay terminates, the taxing authority may resume lawful collection of surviving obligations, subject to applicable restrictions.

19. When Chapter 13 May Be Better for Tax Debt

Chapter 7 may be particularly effective when the debtor's income taxes qualify for discharge and the debtor's property is adequately protected.

But Chapter 13 can be useful when the debtor owes priority taxes that cannot be discharged immediately.

A Chapter 13 plan generally must provide for payment in full of allowed priority claims unless the holder agrees to different treatment, subject to the governing statutory provisions.

This can permit certain tax obligations to be paid over the plan period.

Chapter 13 may also help a debtor address secured tax claims, protect property, and manage collection activity through a court-supervised repayment arrangement.

The appropriate chapter depends on the classification of the taxes, the debtor's income, available assets, and other debts.

Yes.

Chapter 13 can provide a structured mechanism for paying certain priority tax obligations over the life of a repayment plan.

Priority claims generally must receive the treatment required by § 1322(a)(2), unless the holder agrees otherwise.

Chapter 13 may be useful when a debtor has substantial nondischargeable taxes but sufficient income to fund a repayment plan.

Chapter 7 may eliminate qualifying older income taxes more quickly, but it does not provide the same multiyear repayment structure for taxes that survive discharge.

The appropriate chapter depends on the amount and classification of the tax debts, available income, assets, liens, and other obligations.

20. Timing Can Determine Whether Thousands of Dollars Are Discharged

Consider a debtor who owes $35,000 in federal income taxes for an older tax year.

The debtor believes the liability is dischargeable because the return was due more than three years earlier.

But the IRS made an additional assessment only 180 days before the proposed bankruptcy filing.

Filing immediately may leave the recently assessed tax nondischargeable.

Waiting until the applicable 240-day period has expired, accounting for any suspensions, may produce a different result.

However, delaying bankruptcy can expose the debtor to garnishments, levies, liens, and other collection activity.

The correct filing date should be determined through a complete review rather than a simple calculation based on the age of the tax year.

Consider a debtor who owes $45,000 in federal income taxes.

The relevant return and assessment dates suggest that the debt may become dischargeable in several months.

The debtor also owes $60,000 in credit card debt and is considering Chapter 7.

Filing immediately may discharge the credit card debt while leaving the tax obligation intact.

Waiting until the applicable tax-discharge requirements are satisfied may permit discharge of both categories.

But delay carries risks.

Creditors may continue lawful collection activity, the taxing authority may enforce liens, and the debtor's financial circumstances may change.

The decision should therefore be based on a comprehensive analysis rather than a mechanical calculation of the tax-discharge date.

21. Determining Dischargeability Before Filing

A debtor with significant tax obligations should not enter Chapter 7 without a tax-year-by-tax-year analysis.

The review should identify the nature of each tax, the original and extended return due dates, the actual filing date, all relevant assessments, prior bankruptcy proceedings, offers in compromise, and possible fraud or evasion issues.

It should also determine whether the taxing authority possesses liens and whether those liens affect property the debtor wishes to retain.

When the facts or law are disputed, an adversary proceeding may be appropriate to obtain a judicial determination of dischargeability under Federal Rule of Bankruptcy Procedure 7001(6).

Unlike certain fraud-based dischargeability complaints, proceedings to determine the dischargeability of many tax debts are not governed by the ordinary sixty-day deadline in Rule 4007(c).

A debtor who files Chapter 7 expecting to eliminate substantial tax debt may discover afterward that the obligation survives.

The consequences can be serious because the debtor ordinarily cannot simply repeat Chapter 7 immediately to correct the timing mistake.

The Bankruptcy Code restricts successive discharges.

Before filing, counsel should identify each tax year, verify the return and assessment history, determine whether the required statutory periods have expired, and investigate any circumstances that may prevent discharge.

Where the amount is substantial or the legal issue uncertain, a determination of dischargeability may require litigation in the bankruptcy court.

Conclusion

Income taxes are not categorically excluded from Chapter 7 discharge.

Many older federal and Maryland income tax obligations can be eliminated when the applicable statutory requirements are satisfied.

But the three-year, two-year, and 240-day rules must be applied together, with careful attention to late-filed returns, assessment dates, prior bankruptcy proceedings, offers in compromise, fraud, and statutory suspension provisions.

Tax liens may survive even when personal liability is discharged.

For debtors with substantial income tax obligations, the timing of a Chapter 7 filing can make the difference between eliminating the debt and remaining personally liable for it after bankruptcy.

The appropriate analysis should be completed before filing, using reliable tax records and the law applicable to each obligation.

Income taxes are not categorically excluded from Chapter 7 discharge.

Certain older federal and Maryland income tax obligations may be eliminated when the applicable statutory requirements are satisfied.

But the familiar three-year, two-year, and 240-day rules are only the beginning of the analysis.

Late returns, substitute returns, recent assessments, prior bankruptcy cases, offers in compromise, fraudulent conduct, and tax liens can materially change the result.

The critical question is not simply how old the tax debt is. It is whether every applicable statutory requirement for discharge has been satisfied as of the bankruptcy filing date.

Related Bankruptcy Cases and Authorities

Federal statutes

Federal bankruptcy statutes

- 11 U.S.C. § 507(a)(8) — Priority treatment of qualifying tax claims and relevant timing provisions.
- 11 U.S.C. § 523(a)(1) — Exceptions to discharge for certain taxes.
- 11 U.S.C. § 523(a)(7) — Certain fines and penalties.
- 11 U.S.C. § 1322(a)(2) — Treatment of priority claims in Chapter 13.

Internal Revenue Code

- 26 U.S.C. § 6020 — Returns prepared by the Secretary.
- 26 U.S.C. § 6321 — Federal tax liens.
- 26 U.S.C. § 6322 — Period of federal tax liens.

Selected decisions

- *Young v. United States*, 535 U.S. 43 (2002) — Addresses equitable tolling of the three-year tax-priority period during a prior bankruptcy under the law then applicable.
- *In re Moroney*, 352 F.3d 902 (4th Cir. 2003) — Addresses delinquent tax returns filed after IRS assessments; predates the 2005 statutory definition of a return.
- *In re McCoy*, 666 F.3d 924 (5th Cir. 2012) — Addresses late-filed returns under the post-2005 statutory definition.
- *In re Mallo*, 774 F.3d 1313 (10th Cir. 2014) — Addresses the treatment of late-filed income tax returns.
- *In re Fegeley*, 118 F.3d 979 (3d Cir. 1997) — Discusses willful attempts to evade tax obligations.
- *United States v. Hatton*, 220 F.3d 1057 (9th Cir. 2000) — Addresses whether certain taxpayer conduct satisfies the requirement of filing a return.

Student Loans and Bankruptcy: When Educational Debt Can Be Discharged and How the Undue Hardship Process Works

BELSKY BANKRUPTCY LEGAL LIBRARY | STUDENT LOANS AND DISCHARGEABILITY

By Alan J. Belsky, Attorney at Law

Student Loans Are Not Automatically Excluded From Bankruptcy Relief

One of the most persistent misconceptions about bankruptcy is that student loans can never be discharged.

That is incorrect.

Federal bankruptcy law permits discharge of qualifying educational debt when repayment would impose an *undue hardship* on the debtor and the debtor's dependents.

The difficulty is that Congress has not provided a comprehensive statutory definition of undue hardship. Courts have developed standards for applying the exception, and the resulting litigation can be demanding.

For Maryland debtors, the Fourth Circuit's decisions are particularly important.

Recent federal administrative procedures have also made it possible to resolve some federal student loan hardship cases through a more standardized review process.

These developments do not make student loans automatically dischargeable, but they provide reasons for financially distressed borrowers to reconsider assumptions about their available options.

1. What Does the Bankruptcy Code Say About Student Loans?

The principal provision is 11 U.S.C. § 523(a)(8).

It excepts specified educational debts from discharge unless repayment would impose an undue hardship on the debtor and the debtor's dependents.

The provision covers several categories of educational obligations, including certain governmental or nonprofit educational loans, obligations to repay funds received as educational benefits, and qualifying private educational loans.

But not every debt associated with education necessarily falls within the statutory exception.

The classification of the obligation is the first step in the analysis.

2. Federal Student Loans

Federal student loans generally fall within § 523(a)(8).

These may include Direct Loans, certain older Federal Family Education Loan Program obligations, and other qualifying federally supported educational loans.

A borrower seeking to discharge these obligations ordinarily must establish undue hardship in an adversary proceeding.

The debtor's financial circumstances, repayment history, earning capacity, health, dependents, and other relevant factors may be considered.

The availability of federal repayment programs can also affect the analysis, although participation in a particular program is not necessarily an absolute prerequisite to discharge.

3. Private Student Loans

Private educational loans require a more careful classification.

Section 523(a)(8)(B) excepts qualifying educational loans as defined by reference to the Internal Revenue Code.

A loan does not automatically qualify merely because a lender calls it a student loan.

For example, a loan used for expenses outside the statutory definition of qualified higher education expenses may raise different issues.

Similarly, loans associated with educational programs or institutions that do not satisfy applicable statutory requirements may fall outside the exception.

Courts have examined whether particular private loans actually satisfy the statutory language.

A debtor should not assume that every private loan associated with schooling requires proof of undue hardship.

A privately originated loan can also qualify under § 523(a)(8)(A)(i) if it was made under a program funded in whole or in part by a governmental unit or nonprofit institution. Failure to meet the qualified-education-loan definition in subsection (B) does not by itself establish dischargeability if another statutory category applies.

4. The Difference Between Dischargeability and Undue Hardship

Two separate questions must be answered.

First, is the obligation the type of educational debt described in § 523(a)(8)?

If not, it may be discharged under the ordinary bankruptcy discharge provisions, subject to other applicable exceptions.

Second, if the obligation falls within § 523(a)(8), would requiring repayment impose an undue hardship?

Only the second question requires application of the undue-hardship standard.

This distinction can be especially important for private educational loans.

5. The *Brunner* Test

The Fourth Circuit applies the three-part test associated with *Brunner v. New York State Higher Education Services Corp.*, 831 F.2d 395 (2d Cir. 1987).

The debtor generally must establish:

- That repayment would prevent the debtor from maintaining a minimal standard of living for the debtor and dependents.
- That additional circumstances indicate the debtor's financial difficulties are likely to persist for a significant portion of the repayment period.
- That the debtor has made good-faith efforts to repay the loans.

The test is demanding, but it does not categorically prohibit discharge.

The inquiry is fact-specific and requires evidence concerning the debtor's financial condition and realistic future prospects.

6. The Fourth Circuit's Decision in *Frushour*

In *Educational Credit Management Corp. v. Frushour*, 433 F.3d 393 (4th Cir. 2005), the Fourth Circuit applied the *Brunner* framework and emphasized the demanding nature of the undue-hardship standard.

The court examined the debtor's financial circumstances, employment prospects, and repayment efforts.

The decision also discussed the significance of income-contingent repayment options in evaluating good faith.

However, the availability of a repayment program does not mean that every debtor who declines participation automatically loses an undue-hardship claim.

The circumstances surrounding the debtor's decisions remain relevant.

7. What Is a Minimal Standard of Living?

The first *Brunner* requirement does not demand that a debtor live in complete destitution.

The question is whether the debtor can maintain a minimal standard of living while making the required student loan payments.

Reasonable housing, food, utilities, transportation, healthcare, and other necessary expenses are relevant.

A debtor's household circumstances may also matter.

For example, an elderly debtor with fixed income and substantial medical expenses may present a different case from a younger debtor with similar current income but significant future earning potential.

The analysis is not limited to whether any money remains at the end of the month.

The court examines whether the debtor's budget is reasonable and whether repayment can realistically be accommodated.

8. Additional Circumstances and Future Financial Prospects

The second *Brunner* requirement focuses on whether the debtor's financial difficulties are likely to persist.

Relevant circumstances may include age, health limitations, disabilities, employment history, education, vocational skills, caregiving obligations, and realistic earning potential.

Temporary unemployment may not establish persistent hardship.

Conversely, a debtor approaching retirement with limited income and little realistic prospect of increased earnings may have stronger evidence of continuing financial difficulty.

Medical and vocational evidence may be important in appropriate cases.

The debtor's future circumstances should be evaluated realistically rather than through unsupported assumptions about potential earnings.

9. Good-Faith Efforts to Repay

The third *Brunner* requirement examines the debtor's efforts to address the student loan obligation.

Courts may consider payment history, attempts to obtain employment, efforts to maximize income, reasonable expense management, communications with lenders, and consideration of available repayment options.

A debtor who made payments when financially able may have favorable evidence.

But an inability to make substantial payments does not necessarily establish bad faith.

The debtor's conduct must be considered in light of actual financial circumstances.

10. The Department of Justice's Streamlined Process

In November 2022, the Department of Justice and Department of Education announced a process intended to promote more consistent and efficient handling of federal student loan undue-hardship cases.

The process uses an attestation form and specified financial information to evaluate whether the government should stipulate to relevant facts and support discharge.

It does not amend § 523(a)(8) or eliminate the requirement for judicial determination.

Nor does it automatically apply to every private educational loan.

The process may reduce litigation burdens in qualifying federal student loan cases, but its availability and current implementation should be verified when the proceeding is commenced.

11. What Is an Adversary Proceeding?

A student loan undue-hardship determination ordinarily requires an adversary proceeding within the bankruptcy case.

An adversary proceeding is a separate lawsuit governed by Part VII of the Federal Rules of Bankruptcy Procedure.

The debtor files a complaint seeking a determination that the student loan debt is dischargeable.

The creditor or appropriate governmental entity is served and may respond.

The proceeding may involve discovery, financial documentation, motions, settlement negotiations, and, if necessary, trial.

The debtor bears the burden of establishing undue hardship under the applicable standard.

12. Can Student Loans Be Partially Discharged?

The possibility of partial relief has been addressed differently by courts.

Some courts permit discharge of a qualifying portion of educational debt when the applicable undue-hardship requirements are proved for that portion. General equitable authority does not permit a court to bypass § 523(a)(8). DOJ guidance permits recommendations for partial relief in appropriate federal cases, but the bankruptcy court must apply the governing statute and circuit law.

The Fourth Circuit's decisions and the limits imposed by the Bankruptcy Code must be examined before assuming partial discharge is available.

A debtor should not assume that inability to repay the entire balance necessarily establishes a right to discharge only part of it.

The requested relief must be supported by governing law.

13. Parent PLUS Loans

Parent PLUS loans can create particularly difficult financial problems.

A parent may borrow substantial amounts to finance a child's education and remain personally obligated long after the child graduates.

The legal borrower ordinarily is the parent, not the student.

A private family agreement under which the child promises to make payments generally does not, by itself, release the parent from liability to the federal loan holder.

For bankruptcy purposes, the parent must evaluate the obligation as the parent's own debt.

Example

A parent approaching retirement owes $180,000 in Parent PLUS loans.

The parent's income is declining, retirement savings are limited, and the monthly payments substantially exceed the parent's realistic ability to pay.

The debtor may have grounds to examine undue hardship, particularly where the evidence demonstrates limited future earning capacity and persistent financial difficulties.

The amount of the debt alone does not establish undue hardship.

But the debtor's age, income, expenses, employment prospects, and available repayment arrangements may be highly relevant.

14. What If a Divorce Agreement Requires the Other Spouse to Pay?

Divorce agreements sometimes allocate responsibility for student loans between former spouses.

For example, one spouse may agree to pay half of a Parent PLUS loan even though the other spouse remains the only borrower under the federal loan documents.

Such an agreement ordinarily does not alter the federal lender's contractual rights.

The lender may continue to pursue the named borrower.

The divorce agreement may create separate obligations between the former spouses, potentially implicating § 523(a)(15) or other bankruptcy provisions.

Consequently, the dischargeability of the student loan and the enforceability of the former spouse's reimbursement obligation are separate legal questions.

15. Student Loans and Chapter 13

Chapter 13 may provide temporary protection from student loan collection through the automatic stay while the debtor makes payments under a confirmed repayment plan.

However, completion of a Chapter 13 plan does not ordinarily discharge student loans covered by § 523(a)(8) unless the debtor establishes undue hardship.

Interest may continue accruing during the case, depending on the loan and applicable law.

A debtor may therefore emerge from Chapter 13 still owing a substantial educational debt.

The plan's treatment of student loans and other unsecured creditors must comply with the Bankruptcy Code.

16. Should a Debtor Wait Until After Bankruptcy to Seek Student Loan Relief?

Not necessarily.

An undue-hardship adversary proceeding can be pursued in connection with the bankruptcy case.

The timing should reflect the debtor's financial circumstances, available evidence, and procedural considerations.

In some cases, it may be appropriate to seek a determination while the main bankruptcy case remains open.

In others, later proceedings may be possible.

A debtor should not assume that student loan dischargeability must be resolved before the ordinary Chapter 7 discharge is entered.

17. What Evidence Is Important?

A successful undue-hardship case ordinarily requires more than a statement that the payments are unaffordable.

Relevant evidence may include income records, tax returns, household budgets, medical documentation, employment history, vocational limitations, retirement projections, student loan payment history, and communications concerning repayment options.

The debtor's testimony may be important, but documentary support can strengthen the claim.

A careful assessment should also distinguish temporary financial hardship from conditions likely to persist.

18. Alternatives to Bankruptcy Discharge

Federal student loan borrowers may have access to income-driven repayment arrangements, deferment, forbearance, disability-related discharge, or other federal relief programs.

Eligibility and program terms change over time.

Private student loans generally do not offer the same range of federal protections, although lenders may provide contractual hardship arrangements.

These alternatives should be considered when evaluating bankruptcy strategy.

However, the existence of a repayment program does not necessarily mean it provides meaningful relief for every borrower.

A program requiring little or no current payment may still leave the debtor facing a substantial long-term obligation.

Conclusion

Student loans are not categorically immune from bankruptcy discharge.

The Bankruptcy Code permits discharge of qualifying educational obligations when repayment would impose an undue hardship.

In Maryland, the Fourth Circuit's application of the *Brunner* test governs the principal undue-hardship analysis.

Private educational loans may also require careful examination to determine whether they fall within § 523(a)(8) at all.

The Department of Justice's federal student loan review process provides an additional avenue for potentially resolving qualifying undue-hardship cases.

A debtor burdened by substantial educational debt should not assume that bankruptcy offers no possible relief without first examining the nature of the loans and the debtor's actual financial circumstances.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 523(a)(8) — Educational debt exceptions and undue hardship.
- 11 U.S.C. § 727 — Chapter 7 discharge.
- Federal Rule of Bankruptcy Procedure 7001 — Adversary proceedings.
- Federal Rule of Bankruptcy Procedure 4007 — Determination of dischargeability.

Federal administrative guidance

- Department of Justice — Student Loan Bankruptcy Discharge Guidance — Guidance concerning federal student loan undue-hardship proceedings.
- Federal Student Aid — Federal student loan programs and repayment information.

Selected decisions

- *Brunner v. New York State Higher Education Services Corp.*, 831 F.2d 395 (2d Cir. 1987) — Establishes the three-part undue-hardship framework.
- *Educational Credit Management Corp. v. Frushour*, 433 F.3d 393 (4th Cir. 2005) — Applies the *Brunner* test in the Fourth Circuit.
- *In re Mosko*, 515 F.3d 319 (4th Cir. 2008) — Addresses good faith and undue hardship in student loan dischargeability.
- *In re Spence*, 541 F.3d 538 (4th Cir. 2008) — Addresses the demanding requirements for establishing undue hardship.
- *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010) — Addresses student loan discharge provisions in a confirmed Chapter 13 plan and the consequences of procedural error.

The Chapter 7 Bankruptcy Trustee: What the Trustee Investigates, What Property Can Be Sold, and What Happens When Problems Are Discovered

BELSKY BANKRUPTCY LEGAL LIBRARY | CHAPTER 7 PROCEDURE

By Alan J. Belsky, Attorney at Law

The Trustee Is Not Your Attorney—and Does Not Represent Your Interests

When an individual files Chapter 7 bankruptcy, a trustee is appointed to administer the bankruptcy estate.

The trustee's responsibilities are frequently misunderstood. Some debtors assume the trustee is a government employee whose role is to help them obtain a discharge. Others believe the trustee is an adversary whose objective is to take as much property as possible.

Neither description is accurate.

The Chapter 7 trustee is a fiduciary charged with administering the bankruptcy estate according to federal law. The trustee must investigate the debtor's financial affairs, identify and collect nonexempt estate property when appropriate, and distribute available proceeds according to the Bankruptcy Code.

The trustee does not represent the debtor. Nor does the trustee represent any individual creditor exclusively.

The trustee's duties are owed to the estate and its administration, including the interests of creditors.

Understanding the trustee's authority and responsibilities can help debtors prepare accurate filings, avoid unnecessary complications, and recognize when a seemingly routine bankruptcy may become an asset case.

1. Who Appoints the Chapter 7 Trustee?

Chapter 7 trustees ordinarily serve as members of a panel maintained under the supervision of the United States Trustee Program.

The United States Trustee Program is a component of the Department of Justice responsible for supervising the administration of bankruptcy cases and private trustees in most federal judicial districts.

When a Chapter 7 case is filed, an interim trustee ordinarily is appointed under 11 U.S.C. § 701.

At the meeting of creditors, creditors may elect a trustee under the circumstances prescribed by § 702. In most routine consumer cases, no election occurs, and the interim trustee becomes the permanent trustee.

The bankruptcy judge does not ordinarily select the trustee personally for each routine case.

2. The Trustee's Principal Duties

Section 704 establishes the principal duties of a Chapter 7 trustee.

Among them are collecting and reducing estate property to money, investigating the debtor's financial affairs, examining proofs of claim when appropriate, accounting for property received, and furnishing information concerning the estate and its administration.

The trustee also must determine whether the estate contains property that can be administered for the benefit of creditors.

The trustee is not required to sell every nonexempt asset.

The economic benefit of administration must be considered.

For example, a vehicle with a small amount of nonexempt equity may not be worth selling after accounting for liens, sale expenses, and administrative costs.

3. What Is the Bankruptcy Estate?

Under 11 U.S.C. § 541, filing bankruptcy generally creates an estate consisting of the debtor's legal and equitable interests in property as of the commencement of the case.

The estate may include assets that the debtor does not physically possess.

Examples include bank accounts, real estate, vehicles, business interests, anticipated tax refunds, contract rights, and causes of action.

The estate may also include certain interests acquired after filing under specific statutory provisions.

The fact that an asset is part of the estate does not necessarily mean it will be sold.

Exemptions, exclusions, liens, ownership limitations, and the costs of administration all affect the trustee's rights.

4. What Does the Trustee Review Before the Meeting of Creditors?

The trustee ordinarily reviews the petition, schedules, statement of financial affairs, and other required filings.

The trustee may also examine tax returns, bank statements, pay records, deeds, vehicle titles, and other documents.

In Maryland, trustees may request additional records depending on the circumstances.

The trustee's review commonly focuses on the accuracy of reported assets and liabilities, the debtor's income and expenses, property transfers, payments to creditors, and the availability of exemptions.

A debtor with a straightforward financial history and fully exempt assets may require relatively little additional investigation.

A debtor with substantial real estate equity, business interests, recent transfers, or inconsistent financial records may face more extensive scrutiny.

5. The Meeting of Creditors

Under 11 U.S.C. § 341, the debtor ordinarily must attend a meeting of creditors and answer questions under oath.

The trustee conducts the examination.

The bankruptcy judge does not preside.

The trustee generally verifies the debtor's identity and asks questions concerning the accuracy of the bankruptcy filings, ownership of property, debts, income, expenses, and recent financial transactions.

Creditors may attend and ask appropriate questions, although their participation is uncommon in many routine consumer cases.

The meeting is not ordinarily a trial, but the debtor's testimony is under oath and can have legal consequences.

6. What Documents Can the Trustee Demand?

The debtor has statutory duties to cooperate with the trustee and surrender property and records relating to the estate as required by law.

Under § 521(a)(3) and (4), the debtor must cooperate as necessary to enable the trustee to perform the trustee's duties and surrender qualifying estate property and related documents.

A trustee may request bank statements, tax returns, pay records, financial account information, business records, insurance documents, and other materials relevant to the estate.

The precise requirements depend on the case.

A debtor should not assume that documents not expressly requested before the meeting will never be required.

7. What Is a No-Asset Case?

A no-asset case is one in which the trustee determines that there is no property available for meaningful distribution to unsecured creditors.

This does not mean the debtor owns nothing.

The debtor may own a home, vehicle, furniture, retirement accounts, and other property, but those assets may be exempt, fully encumbered, excluded from the estate, or otherwise not economically worthwhile to administer.

Many consumer Chapter 7 cases are no-asset cases.

However, a case initially identified as no-asset may later become an asset case if the trustee discovers property or receives information changing the administration analysis.

8. What Happens in an Asset Case?

When the trustee identifies property that can be administered, the trustee may collect, sell, settle, or otherwise liquidate the estate's interest.

The trustee must comply with applicable statutory and procedural requirements.

For example, a trustee proposing to sell estate property outside the ordinary course generally must comply with § 363 and the relevant bankruptcy rules.

Creditors and other parties in interest may have notice and objection rights.

After payment of applicable administrative expenses and other priority obligations, remaining proceeds are distributed according to the Bankruptcy Code's priority system.

An asset case may remain open considerably longer than a routine no-asset case.

9. Can the Trustee Sell a Home?

Potentially.

The trustee must examine the debtor's ownership interest, fair market value, liens, exemptions, and anticipated sale expenses.

Maryland's 2026 increase in its bankruptcy residential-property exemption to $125,000 significantly expands the protection available to qualifying homeowners.

However, equity exceeding the available exemption may still present a liquidation issue.

Joint ownership, tenancy by the entirety, divorce, and the presence of joint creditors can materially affect the analysis.

A debtor should not assume that a house is protected simply because the mortgage payments are current.

Nor should the debtor assume that the trustee can sell every residence containing equity.

10. Can the Trustee Sell a Vehicle?

A trustee may administer nonexempt vehicle equity.

The relevant factors include the vehicle's value, outstanding secured debt, available exemptions, and costs of sale.

A debtor who owns a modestly valued financed vehicle may have little or no nonexempt equity.

A debtor who owns an expensive vehicle free and clear may present a different situation.

The trustee's interest concerns the value available to the estate, not the debtor's ability to continue making loan payments.

Secured lenders possess separate rights that must also be addressed.

11. Tax Refunds and Other Unexpected Assets

Tax refunds are a frequent source of bankruptcy estate assets.

A debtor may have an interest in a refund attributable to prepetition earnings or payments even though the tax return has not yet been filed.

The trustee may request the return when it becomes available and determine whether any portion of the refund belongs to the estate.

Other unexpected assets may include inheritances, insurance proceeds, contract rights, and legal claims.

Certain interests acquired within 180 days after filing may become estate property under § 541(a)(5).

The debtor should promptly disclose significant postpetition developments to bankruptcy counsel.

12. Personal Injury Claims and Other Lawsuits

A cause of action belonging to the debtor when bankruptcy is filed generally becomes property of the bankruptcy estate, even if no lawsuit has been filed.

This includes potentially valuable personal injury, employment, contract, and other claims.

The trustee may have authority to prosecute, settle, or abandon the claim.

Maryland law provides significant exemption protection for qualifying personal injury compensation, but the availability and extent of protection depend on the nature of the recovery.

A debtor who fails to disclose a pending or potential lawsuit may face serious consequences.

The failure may also affect the debtor's ability to pursue the claim after bankruptcy.

13. Preferential Payments

Under § 547, a trustee may avoid certain transfers made before bankruptcy that favor one creditor over others.

The ordinary preference period is ninety days before filing.

Transfers benefiting insiders may be subject to a one-year lookback period.

For example, a debtor who repays a substantial loan to a family member shortly before filing may expose that payment to recovery by the trustee.

A preference does not necessarily require fraudulent intent.

The statutory elements and defenses must be examined.

14. Fraudulent Transfers

Under § 548, a trustee may avoid certain transfers made with actual fraudulent intent or for less than reasonably equivalent value under specified financial circumstances.

The federal statutory lookback period is generally two years.

Section 544 may permit the trustee to invoke applicable state-law avoidance rights, potentially involving different limitation periods.

Transfers to relatives, sales for nominal consideration, and changes in ownership shortly before bankruptcy may receive particular scrutiny.

Not every prepetition transfer is fraudulent.

The legal consequences depend on the circumstances and applicable law.

15. Can the Trustee Recover Property From Family Members?

Yes, under appropriate circumstances.

A trustee may pursue transfers made to relatives when the statutory requirements for preference or fraudulent-transfer recovery are satisfied.

For example, repayment of a genuine family loan shortly before bankruptcy may be preferential even though the debtor intended only to honor an obligation.

A transfer of valuable property to a child for nominal consideration may raise fraudulent-transfer concerns.

The trustee may seek recovery from the initial transferee or other parties as permitted by § 550.

Family members should not assume that receiving property before bankruptcy insulates it from later recovery.

16. What Happens When the Trustee Discovers an Undisclosed Asset?

An undisclosed asset may lead to additional investigation, amendment of the schedules, objections to exemptions, or litigation.

The consequences depend on whether the omission was inadvertent, negligent, reckless, or intentional.

A debtor who discovers an error should promptly consult counsel about correcting the filing.

Intentional concealment can create grounds for denial or revocation of discharge under § 727.

It may also expose the debtor to criminal consequences under applicable federal law.

The trustee's discovery of an omitted asset does not automatically establish fraud, but it can significantly complicate the case.

17. The Trustee's Authority to Examine Financial Affairs

The trustee may investigate the debtor's financial history and request information relevant to estate administration.

Federal Rule of Bankruptcy Procedure 2004 authorizes broad examinations concerning the debtor's acts, conduct, property, liabilities, financial condition, and matters affecting administration.

A Rule 2004 examination may involve testimony and document production.

The examination is often described as broader than ordinary civil discovery, although it is subject to procedural limitations and judicial oversight.

The trustee may seek such an examination when the ordinary schedules and meeting testimony leave material questions unresolved.

18. Can the Trustee Object to Exemptions?

Yes.

The trustee may object to an exemption claimed without a valid statutory basis or in an amount exceeding the applicable limit.

Federal Rule of Bankruptcy Procedure 4003 governs exemption objections and applicable deadlines.

The trustee may challenge the debtor's valuation of property or the legal characterization of an asset.

For example, a dispute may arise over whether settlement proceeds qualify as exempt personal injury compensation or whether a residence satisfies the requirements of Maryland's residential exemption.

The debtor should claim exemptions accurately and retain supporting documentation.

19. Can the Trustee Object to Discharge?

The trustee may investigate circumstances that could support denial of discharge under § 727.

Grounds can include specified fraudulent transfers, concealment of property, false oaths, failure to preserve records, and other misconduct.

A discharge objection is different from an objection to the dischargeability of a particular debt.

Denial of discharge may leave the debtor personally liable for numerous obligations that otherwise would have been eliminated.

The trustee may bring an adversary proceeding seeking denial of discharge when the statutory grounds exist.

20. The Trustee and the United States Trustee Are Different

The Chapter 7 trustee and the United States Trustee serve different functions.

The Chapter 7 trustee administers the estate in the particular case.

The United States Trustee supervises aspects of bankruptcy administration, monitors compliance, and may investigate abuse or misconduct.

The United States Trustee may also seek dismissal of certain Chapter 7 cases under § 707(b) or pursue other remedies authorized by law.

A debtor should not confuse routine document requests from the case trustee with a separate investigation by the United States Trustee.

Both may be important, but their roles are distinct.

21. Can the Trustee Abandon Property?

Yes.

Under § 554, a trustee may abandon property that is burdensome to the estate or of inconsequential value and benefit.

Abandonment generally removes the property from estate administration, subject to applicable law.

For example, a trustee may abandon a vehicle with insufficient nonexempt equity to justify a sale.

Certain scheduled property that remains unadministered when the case closes may be abandoned by operation of § 554(c), subject to statutory conditions.

Property that was not properly scheduled may remain property of the estate even after the case closes.

This is another reason complete disclosure is essential.

22. What Happens When the Trustee Completes Administration?

In a no-asset case, the trustee ordinarily files a report indicating that no assets are available for distribution.

In an asset case, the trustee may liquidate property, resolve claims, distribute proceeds, and file a final report and accounting.

The bankruptcy court ultimately closes the case when administration is complete.

The debtor's discharge may occur before the trustee completes asset administration.

Receiving a discharge therefore does not necessarily mean that the trustee's authority over estate property has ended.

Conclusion

The Chapter 7 trustee plays a central role in bankruptcy administration.

The trustee investigates the debtor's financial affairs, identifies estate property, evaluates exemptions, and administers assets when doing so will benefit creditors.

Most consumer cases do not involve liquidation, but the trustee possesses substantial authority when nonexempt property, avoidable transfers, or other estate assets are identified.

Accurate schedules, complete disclosure, proper exemption planning, and cooperation with the trustee can substantially reduce unnecessary complications.

The safest Chapter 7 case is not one in which the debtor hopes the trustee will overlook an asset. It is one in which the debtor's property and financial affairs have been fully evaluated before filing.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 704 — Duties of the Chapter 7 trustee.
- 11 U.S.C. § 521 — Debtor's duties.

- 11 U.S.C. § 363 — Sale and administration of estate property.
- 11 U.S.C. § 547 — Preferential transfers.
- 11 U.S.C. § 548 — Fraudulent transfers.
- 11 U.S.C. § 550 — Recovery of avoided transfers.
- 11 U.S.C. § 554 — Abandonment of estate property.
- Federal Rule of Bankruptcy Procedure 2004 — Examination.
- Federal Rule of Bankruptcy Procedure 4003 — Exemption objections.

Selected decisions

- *United States v. Whiting Pools, Inc.*, 462 U.S. 198 (1983) — Addresses the scope of estate property and turnover.
- *Schwab v. Reilly*, 560 U.S. 770 (2010) — Addresses exemption claims and the trustee's rights in property exceeding claimed exemption amounts.
- *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992) — Explains the consequences of failing to object timely to exemptions.
- *Law v. Siegel*, 571 U.S. 415 (2014) — Limits equitable interference with statutory exemptions.
- *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985) — Addresses administration of Maryland entireties property for joint creditors.
- *In re Butcher*, 125 F.3d 238 (4th Cir. 1997) — Addresses Maryland's exemption for personal injury compensation.

The Chapter 7 Meeting of Creditors: What the Trustee Will Ask, What Documents You Need, and What Can Go Wrong

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By Alan J. Belsky, Attorney at Law

The Meeting of Creditors Is Usually Brief, but It Is Not a Formality

Every individual who files Chapter 7 bankruptcy ordinarily must attend a meeting of creditors under 11 U.S.C. § 341.

The meeting is sometimes called the *341 meeting* or *trustee meeting*. Although the name suggests that creditors will gather to question the debtor, creditors rarely attend routine consumer bankruptcy meetings.

Instead, the meeting ordinarily consists of an examination conducted by the Chapter 7 trustee.

The trustee verifies the debtor's identity, confirms the accuracy of the bankruptcy documents, and asks questions concerning the debtor's assets, debts, income, expenses, and financial transactions.

Most straightforward meetings are relatively short. Nevertheless, the debtor testifies under oath, and inaccurate or incomplete answers can have serious consequences.

Proper preparation is therefore important even when the case appears uncomplicated.

1. What Is the Purpose of the Meeting?

The meeting allows the trustee and creditors to examine the debtor concerning financial affairs and property of the bankruptcy estate.

Under § 341, the United States Trustee convenes and presides over the meeting through the appropriate administrative arrangements.

In a Chapter 7 case, the appointed panel trustee ordinarily conducts the examination.

The trustee uses the meeting to determine whether the schedules are accurate, whether additional information is required, and whether the estate contains property available for administration.

The meeting also provides an opportunity to investigate potentially avoidable transfers, undisclosed assets, or other issues requiring further attention.

2. Is the Bankruptcy Judge Present?

No.

Section 341(c) prohibits the bankruptcy judge from presiding at or attending the meeting of creditors.

The meeting is not a courtroom trial.

The trustee administers an oath and asks questions, but the trustee does not adjudicate contested legal disputes as a judge would.

If a dispute requires judicial resolution, it ordinarily must be presented to the bankruptcy court through an appropriate motion, objection, or adversary proceeding.

3. When Does the Meeting Occur?

Rule 2003 ordinarily sets the Chapter 7 meeting no fewer than 21 and no more than 40 days after the order for relief, with specified exceptions permitting a later date. The actual notice governs the scheduled appearance; a later continuation does not generally restart deadlines measured from the first date set.

In a voluntary Chapter 7 case, the filing of the petition ordinarily constitutes the order for relief.

The meeting commonly occurs several weeks after filing.

The precise date depends on the court's scheduling practices and the trustee's calendar.

The debtor receives notice of the meeting, ordinarily through the bankruptcy court's official notice.

The date is important because several bankruptcy deadlines are calculated by reference to the first date set for the meeting.

4. Are Meetings Conducted in Person or Remotely?

The United States Trustee Program states that almost all § 341 meetings are held virtually using Zoom. Follow the official notice and the assigned trustee’s instructions, including any authorized alternative arrangement.

The applicable instructions should be reviewed for the particular case and trustee.

A debtor appearing remotely should use a reliable internet connection, a functioning camera and microphone when required, and a private location free from interruptions.

The debtor should not attempt to participate while driving.

The trustee must be able to verify identity and administer the examination effectively.

5. What Identification Must the Debtor Provide?

The trustee ordinarily must verify the debtor's identity and Social Security number or other applicable identifying information.

The United States Trustee Program's procedures generally require acceptable photographic identification and satisfactory evidence of the Social Security number.

Examples of potentially acceptable documents include government-issued photo identification and a Social Security card or other approved evidence.

The exact requirements should be confirmed through the trustee's instructions.

A debtor who cannot provide satisfactory identification may have the meeting continued.

Identification documents should be handled through the trustee's approved procedures rather than transmitted insecurely.

6. What Documents Does the Trustee Review?

Before the meeting, the trustee ordinarily receives the bankruptcy petition, schedules, statement of financial affairs, and other required filings.

The trustee may also review tax returns, bank statements, pay records, deeds, vehicle titles, and other documents.

In Maryland, individual trustees may have specific document requirements.

A debtor should provide requested materials promptly and completely.

Section 521(e)(2) ordinarily requires the most recent filed federal income tax return, or qualifying transcript, to be supplied to the trustee at least seven days before the first date set for the meeting. Current UST meeting instructions generally request identity and Social Security number evidence securely at least 14 days before the meeting, or within another timeframe the trustee specifies. These document deadlines are distinct.

Failure to supply required documents can result in a continued meeting, additional investigation, or other procedural consequences.

7. What Questions Does the Trustee Usually Ask?

The trustee's questions vary, but many routine examinations address similar subjects.

Common questions include:

- Did you review the bankruptcy petition, schedules, and statements before signing them?
- Is the information true and correct to the best of your knowledge?
- Have you listed all your assets and debts?
- Do you own or have an interest in any real estate?
- Have you transferred property or repaid relatives before filing?
- Are you entitled to any inheritance, lawsuit proceeds, insurance recovery, or tax refund?
- Have you previously filed bankruptcy?
- Are there any errors or omissions that need correction?

The trustee may ask additional questions based on the debtor's circumstances.

The debtor should answer truthfully, directly, and completely.

8. What If the Debtor Does Not Understand a Question?

The debtor should ask the trustee to repeat or clarify the question.

There is no benefit in guessing.

If the debtor does not know an answer, the debtor should say so rather than provide an unsupported estimate.

The debtor's attorney may assist with appropriate clarification or legal issues, but the debtor ordinarily must provide the factual testimony personally.

The meeting is not an occasion for counsel to answer every question on the debtor's behalf.

9. Do Creditors Usually Attend?

In many routine consumer Chapter 7 cases, no creditors attend.

Creditors receive notice and have the right to participate, but attendance may not be economically worthwhile when the case appears to be a no-asset case.

A creditor may attend when there is a dispute concerning fraud, property ownership, recent transactions, or other matters.

The absence of creditors does not establish that every debt is dischargeable or that no creditor will later file an objection.

Creditors may pursue available remedies within the applicable statutory and procedural deadlines.

10. What Happens If a Creditor Appears?

A creditor may ask relevant questions concerning the debtor's financial affairs.

The trustee ordinarily controls the examination and may limit inappropriate or repetitive questioning.

A creditor seeking extensive testimony or document production may need to pursue a Rule 2004 examination or other appropriate procedure.

The meeting is not ordinarily a trial concerning the creditor's claim.

A debtor should answer appropriate questions truthfully while relying on counsel to address legal objections or procedural issues.

11. What If the Debtor Forgot to List an Asset?

The debtor should disclose the omission promptly.

An omitted asset may require an amendment to the bankruptcy schedules and additional exemption analysis.

The consequences depend on the asset's nature, value, and the circumstances of the omission.

A genuine mistake does not automatically establish fraud.

However, intentional concealment or false testimony can create grounds for denial of discharge and other serious consequences.

A debtor should never attempt to conceal an omission merely because the trustee has not discovered it.

12. What If the Debtor Forgot to List a Creditor?

An omitted creditor should be disclosed and the schedules amended when appropriate.

The legal consequences depend on the type of debt, whether the case is an asset or no-asset case, and whether the creditor received sufficient notice to protect its rights.

Section 523(a)(3) governs certain omitted debts.

The debtor should not assume that omission automatically makes a debt nondischargeable or that it has no consequences.

Accurate creditor schedules are essential.

13. What If the Trustee Discovers a Recent Transfer?

The trustee may investigate transfers made before bankruptcy.

Examples include selling property to a relative, giving away valuable assets, changing title to a vehicle, or repaying a family loan.

Some transfers may be avoidable as preferences under § 547 or fraudulent transfers under § 548 or applicable state law.

A transfer does not necessarily become fraudulent merely because it occurred before bankruptcy.

The trustee must examine the applicable statutory requirements.

The debtor should disclose the transaction and provide relevant documentation.

14. Can the Trustee Ask About a Personal Injury Claim?

Yes.

A pending or potential personal injury claim may constitute property of the bankruptcy estate.

The trustee may ask whether the debtor has been involved in an accident, suffered an injury, filed a lawsuit, or expects an insurance settlement.

The claim must be disclosed when required, even if no lawsuit has been filed or the amount of recovery is uncertain.

Maryland provides important exemption protection for qualifying personal injury compensation, but the trustee may need information to evaluate the claim.

Failure to disclose the claim can create serious problems in both the bankruptcy and the underlying litigation.

15. What Happens If the Trustee Needs More Information?

The trustee may continue the meeting to a later date.

A continuation may be necessary when documents are missing, valuations are uncertain, or financial transactions require further investigation.

A continued meeting does not automatically mean the debtor has done anything wrong.

However, the debtor must comply with lawful requests and attend further examinations when required.

The trustee may also seek additional information through other procedures.

16. Can the Trustee Conduct a More Extensive Examination?

Yes.

Federal Rule of Bankruptcy Procedure 2004 permits examinations concerning the debtor's acts, conduct, property, liabilities, financial condition, and matters affecting estate administration.

A Rule 2004 examination may involve testimony under oath and document production.

It can be broader than the routine § 341 meeting.

The procedure is subject to court authorization and applicable limitations.

A trustee may seek such an examination when significant questions remain unresolved.

17. What Happens If the Debtor Fails to Attend?

Failure to attend the meeting can delay the case and may result in dismissal or other relief.

The debtor should promptly notify counsel if illness, emergency, or another serious circumstance prevents attendance.

The trustee or appropriate authority may permit rescheduling or other arrangements under applicable procedures.

A debtor should not simply fail to appear and assume the meeting will be rescheduled automatically.

18. Can the Debtor Be Required to Produce More Documents After the Meeting?

Yes.

The trustee's investigation does not necessarily end when the meeting concludes.

The trustee may request additional bank statements, tax returns, account records, business documents, or other information relevant to the estate.

The debtor's statutory duty to cooperate continues.

The trustee may also investigate property or transactions discovered after the meeting.

19. What Happens After the Meeting Is Concluded?

In a routine no-asset case, the trustee may file a report indicating that no property is available for distribution.

The debtor may then proceed toward discharge, assuming the remaining requirements are satisfied and no successful objections arise.

In an asset case, the trustee may continue administering property and resolving claims.

The debtor's discharge may be entered before the trustee completes administration.

Thus, completion of the meeting does not necessarily mean the bankruptcy case is finished.

20. Why Preparation Matters

A debtor who understands the petition and schedules is generally better prepared for the trustee's examination.

Before the meeting, the debtor should review the filings, confirm that all assets and debts have been disclosed, and identify any corrections.

The debtor should also understand significant transactions disclosed in the statement of financial affairs.

The objective is not to memorize answers.

It is to provide accurate testimony based on a genuine understanding of the debtor's financial circumstances.

Conclusion

The Chapter 7 meeting of creditors is ordinarily a brief administrative examination, not a trial.

Nevertheless, the debtor testifies under oath, and the trustee has substantial authority to investigate financial affairs and estate property.

Most routine meetings conclude without significant difficulty when the bankruptcy documents are accurate and the debtor is prepared.

Problems are more likely to arise when assets are omitted, financial transactions are inadequately explained, required documents are missing, or the debtor provides inaccurate testimony.

The best preparation is a complete and accurate bankruptcy filing, followed by a careful review of the documents before the meeting.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 341 — Meeting of creditors.
- 11 U.S.C. § 343 — Examination of the debtor.
- 11 U.S.C. § 521 — Debtor's duties.
- 11 U.S.C. § 704 — Chapter 7 trustee's duties.
- Federal Rule of Bankruptcy Procedure 2003 — Meeting of creditors.
- Federal Rule of Bankruptcy Procedure 2004 — Examinations.
- Federal Rule of Bankruptcy Procedure 1007 — Required lists, schedules, statements, and other documents.

Administrative guidance

- United States Trustee Program — Trustee supervision and meeting procedures.
- United States Courts — Bankruptcy Basics — General explanation of Chapter 7 procedure and the meeting of creditors.

Selected decisions

- *United States v. Whiting Pools, Inc.*, 462 U.S. 198 (1983) — Addresses property of the bankruptcy estate and trustee administration.
- *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992) — Addresses exemption objections and applicable deadlines.
- *Law v. Siegel*, 571 U.S. 415 (2014) — Limits equitable interference with statutory exemption protections.
- *In re Kestell*, 99 F.3d 146 (4th Cir. 1996) — Discusses abuse of bankruptcy relief and debtor conduct.

Preferential Payments Before Bankruptcy: Why Paying Family Members or Favored Creditors Can Create Serious Problems

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By Alan J. Belsky, Attorney at Law

Paying a Legitimate Debt Before Bankruptcy Can Create an Unexpected Problem

Most people believe that paying their debts is responsible conduct. Ordinarily, it is. But bankruptcy law contains a counterintuitive rule: certain payments made to creditors before filing may be recovered by the Chapter 7 trustee, even when the debt was legitimate, the payment was voluntary, and neither party intended to do anything improper.

These transactions are called *preferential transfers*.

The purpose of preference law is to prevent a financially distressed debtor from favoring particular creditors shortly before bankruptcy at the expense of creditors who receive nothing.

The rule can produce particularly unpleasant consequences when a debtor repays a parent, sibling, adult child, or friend before filing.

The debtor may believe that the family loan has been responsibly repaid. The recipient may believe the transaction is finished. Yet the trustee may later demand that the recipient return the money to the bankruptcy estate.

Preference law does not require proof that the debtor intended to defraud anyone.

It is therefore essential to distinguish a preferential payment from a fraudulent transfer.

1. What Is a Preferential Transfer?

Section 547(b) of the Bankruptcy Code permits a trustee to avoid certain transfers of the debtor's interest in property made to or for the benefit of a creditor on account of an antecedent debt.

The trustee generally must establish that the transfer:

- Was made to or for the benefit of a creditor.
- Was made on account of a debt owed before the transfer.
- Was made while the debtor was insolvent.
- Occurred within the applicable preference period.
- Enabled the creditor to receive more than the creditor would have received in a hypothetical Chapter 7 liquidation without the transfer.

All statutory elements must be satisfied.

Even when those elements are established, the recipient may have defenses under § 547(c).

2. The Ordinary Ninety-Day Preference Period

For most creditors, the relevant preference period is ninety days before the bankruptcy filing.

A payment made within that period may be avoidable if the other statutory requirements are met.

The ninety-day period is not a general prohibition against paying bills before bankruptcy.

Many ordinary payments are not preferential, and statutory defenses may apply.

For example, paying a utility bill for current service presents different issues from making an extraordinary lump-sum payment on an old unsecured loan.

The nature, timing, and circumstances of the payment matter.

3. The One-Year Period for Insiders

The preference period is generally extended to one year when the creditor was an insider at the time of the transfer.

Under § 101(31), insiders of an individual debtor include certain relatives and other persons or entities having specified relationships with the debtor.

The statutory definition is not necessarily exhaustive.

A person who exercises substantial control over the debtor's affairs may present insider issues even without a traditional family relationship.

Example: Repayment to a parent

A debtor borrowed $18,000 from a parent several years earlier.

Eight months before filing Chapter 7, the debtor repays $12,000.

Because the parent is an insider, the payment falls within the one-year preference period.

If the other statutory elements are satisfied and no defense applies, the trustee may seek recovery of the payment.

The fact that the parent genuinely loaned the money does not prevent the transaction from being preferential.

4. Why Family Loans Receive Particular Scrutiny

Debtors frequently feel a moral obligation to repay relatives before seeking bankruptcy relief.

They may be embarrassed about discharging a family loan or concerned about damaging personal relationships.

But preference law does not give family creditors priority because of emotional or moral considerations.

Indeed, the extended insider period reflects Congress's concern that debtors may favor persons with whom they have close relationships.

A debtor who intends to file bankruptcy should disclose significant payments to relatives and obtain advice before making additional payments.

The appropriate response is not to conceal the loan or the repayment.

5. Insolvency and the Presumption of Insolvency

A preferential transfer generally must have been made while the debtor was insolvent.

Under § 101(32), insolvency for most individuals is generally determined through a balance-sheet analysis comparing debts with the fair value of property, subject to statutory exclusions.

A debtor may be unable to pay monthly bills but still possess assets exceeding liabilities.

Conversely, a debtor who continues making minimum payments may nevertheless be insolvent.

Section 547(f) creates a presumption that the debtor was insolvent during the ninety days immediately preceding bankruptcy.

For transfers outside that period, including many insider transfers, the trustee may need to establish insolvency without relying on that presumption.

This distinction can be significant in defending an insider preference action.

6. The Creditor Must Have Received More Than in Chapter 7

A transfer is not preferential merely because it occurred during the lookback period.

The trustee must establish that the payment enabled the creditor to receive more than it would have received under the statutory hypothetical Chapter 7 liquidation analysis.

Payments to fully secured creditors may present different issues from payments to unsecured creditors.

If a creditor would have received full payment from its collateral in a Chapter 7 liquidation, the transfer may not satisfy the preference requirements.

The relevant analysis depends on the creditor's secured status, collateral value, priority, and the estate's likely distribution.

7. Ordinary-Course Payments

Section 547(c)(2) provides a defense for certain transfers made in payment of debts incurred in the ordinary course of business or financial affairs of the debtor and creditor.

The statute permits consideration of whether the transfer was made in the ordinary course of the parties' financial affairs or according to ordinary business terms.

The defense can protect routine payments that do not represent unusual favoritism.

For example, regular monthly payments on an established obligation may present a stronger ordinary-course defense than an extraordinary lump-sum payment made after collection threats.

The defense is fact-specific.

8. Contemporaneous Exchanges for New Value

Section 547(c)(1) protects certain transfers intended by the parties to be contemporaneous exchanges for new value and that are substantially contemporaneous.

For example, a debtor who pays cash for groceries ordinarily receives new value at the time of payment.

That transaction is fundamentally different from paying an old unsecured debt.

The contemporaneous-exchange defense helps prevent preference law from interfering unnecessarily with ordinary exchanges of equivalent value.

9. Subsequent New Value

Section 547(c)(4) provides a defense when, after receiving a potentially preferential transfer, the creditor gives qualifying new value to or for the benefit of the debtor.

The statutory requirements must be satisfied.

This defense is particularly relevant in commercial relationships involving repeated payments and extensions of credit.

For example, a supplier may receive payment on an old invoice and then deliver additional goods on credit.

The later extension of new value may reduce the creditor's preference exposure.

The precise calculation can be complex.

10. Wage Garnishments

Payments obtained through wage garnishment may constitute preferential transfers.

The fact that the creditor collected the money involuntarily does not automatically prevent preference recovery.

However, garnishment presents difficult timing questions.

Under § 547(e), the date of a transfer may depend on when the creditor's interest became effective against relevant parties under applicable law.

Maryland garnishment procedures and federal bankruptcy law must be considered together.

A debtor who has experienced significant wage garnishment shortly before filing may have potential avoidance rights, although recovery is not automatic.

11. Can the Debtor Recover Garnished Wages?

In some circumstances, § 522(h) permits a debtor to avoid certain transfers that the trustee does not pursue.

The debtor must satisfy statutory requirements, including those relating to the nature of the transfer and the availability of an exemption.

The debtor cannot assume that every prepetition garnishment is recoverable.

The amount, timing, exemption rights, and trustee's actions must be evaluated.

A debtor seeking recovery should preserve pay statements, garnishment records, and information concerning when the creditor received the funds.

12. Payments to Credit Card Companies

Large payments to credit card companies shortly before bankruptcy may raise preference questions.

For example, a debtor may pay $8,000 toward one credit card while leaving several other unsecured creditors unpaid.

If the payment satisfies the statutory requirements and no defense applies, the trustee may seek recovery.

However, ordinary minimum payments may qualify for defenses depending on the circumstances.

The trustee's economic incentive to pursue recovery also matters.

Preference analysis should not be reduced to the proposition that every credit card payment within ninety days is recoverable.

13. Payments to Secured Creditors

Payments to secured creditors require separate analysis.

A payment to a fully secured creditor may not satisfy the requirement that the creditor received more than it would have received in a Chapter 7 liquidation.

But payments to undersecured creditors, transfers creating or perfecting liens, and unusual transactions may present different issues.

For example, granting a previously unsecured creditor a lien shortly before bankruptcy may constitute a transfer subject to avoidance.

The existence of collateral does not automatically eliminate preference concerns.

14. Transfers Involving Joint Debts

Payments on joint obligations can raise additional questions.

Suppose a debtor pays a loan owed jointly with a spouse or family member.

The payment may benefit not only the creditor but also a co-obligor whose liability is reduced.

Under appropriate circumstances, the trustee may examine whether the transfer benefited an insider or another party.

The statutory treatment depends on the nature of the obligation, the recipient, the beneficiary, and applicable limitations on recovery.

The analysis can become especially complicated when one spouse files bankruptcy and the other does not.

15. The Small-Transfer Limitations

Section 547(c)(8) provides a limitation for certain transfers involving debtors whose debts are primarily consumer debts.

For primarily consumer-debt cases, § 547(c)(8) bars avoidance where the aggregate value of the qualifying transfer or transfers is less than $600. That $600 figure is not adjusted under § 104. Section 547(c)(9) separately provides an inflation-adjusted nonconsumer threshold of $8,575 for cases filed on or after April 1, 2025, subject to later statutory changes. The aggregation must be evaluated for the relevant creditor or beneficiary, rather than combining unrelated creditors to clear the threshold.

16. Who Must Return the Preferential Payment?

Under § 550, the trustee may recover an avoided transfer from specified transferees or beneficiaries, subject to statutory limitations and defenses.

In a family-loan situation, the trustee may seek recovery from the relative who received the payment.

The debtor's discharge does not necessarily protect the recipient.

This can produce an unexpected result: the debtor receives a bankruptcy discharge, but a family member becomes a defendant in litigation seeking return of money received before filing.

The recipient may have defenses and should not assume the trustee's demand conclusively establishes liability.

17. Does the Debtor Get in Trouble for Making a Preference?

A preferential payment is not necessarily fraudulent or wrongful conduct by the debtor.

Preference law often operates without proof of dishonest intent.

However, concealment of the payment, false statements about it, or other misconduct can create separate problems.

A debtor who accurately discloses a legitimate prepetition payment may face no personal wrongdoing allegation even though the trustee seeks recovery from the recipient.

The distinction between the avoidability of a transfer and misconduct by the debtor is important.

18. Preference Versus Fraudulent Transfer

Preferences and fraudulent transfers are separate legal concepts.

A preference generally concerns payment or security given on account of an existing debt that favors a creditor over others.

A fraudulent transfer may involve actual intent to hinder, delay, or defraud creditors or a transfer for less than reasonably equivalent value under specified circumstances.

The federal fraudulent-transfer provisions generally appear in § 548.

A transaction may implicate one doctrine, both doctrines, or neither.

For example, repaying a genuine family loan may be preferential without being fraudulent.

Giving valuable property to a relative for no consideration may raise fraudulent-transfer issues even when no antecedent debt exists.

19. What Happens After the Trustee Recovers a Preference?

Recovered funds generally become available for administration through the bankruptcy estate.

The trustee may use them to pay allowable administrative expenses and distribute remaining proceeds according to the Bankruptcy Code.

The creditor who returned the payment may have a claim in the bankruptcy case, subject to applicable statutory provisions.

Section 502(h) addresses claims arising from recovery of property under specified avoidance provisions.

The recipient's ultimate recovery may therefore be only a fraction of the amount returned.

20. Why Preference Planning Matters Before Filing

Preference issues should be examined before a bankruptcy petition is filed.

The debtor should identify substantial payments made during the preceding ninety days and payments to insiders during the preceding year.

The analysis should also include unusual lien transactions, garnishments, and payments on joint obligations.

A debtor should not assume that waiting until a particular date automatically eliminates every avoidance issue.

Fraudulent-transfer provisions, state-law remedies, and other statutory rules may still apply.

Nor should the debtor attempt to manipulate transactions or conceal payments.

The objective is to understand the legal consequences of legitimate financial activity and select an appropriate filing strategy.

Conclusion

Preference law is one of the more counterintuitive aspects of bankruptcy.

A debtor may pay a legitimate obligation in good faith, only to have the Chapter 7 trustee seek recovery from the recipient.

The risk is particularly significant when family members or other insiders receive substantial payments within one year before filing.

Preferences do not necessarily involve fraud, and creditors may have statutory defenses.

But the consequences can be substantial.

Before filing Chapter 7, significant payments to creditors—especially relatives and other insiders—should be carefully reviewed to determine whether they may be recoverable by the trustee.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 547 — Preferential transfers and defenses.
- 11 U.S.C. § 550 — Recovery of avoided transfers.
- 11 U.S.C. § 502(h) — Claims arising from recovery of property.
- 11 U.S.C. § 522(h) — Debtor avoidance of certain transfers.
- 11 U.S.C. § 548 — Fraudulent transfers.
- 11 U.S.C. § 101(31)–(32) — Definitions of insider and insolvent.

Selected decisions

- *Barnhill v. Johnson*, 503 U.S. 393 (1992) — Addresses when a transfer by check occurs for preference purposes.
- *Union Bank v. Wolas*, 502 U.S. 151 (1991) — Addresses the ordinary-course-of-business defense.
- *Begier v. IRS*, 496 U.S. 53 (1990) — Addresses the requirement that a preference involve an interest of the debtor in property.
- *Palmer Clay Products Co. v. Brown*, 297 U.S. 227 (1936) — Discusses the hypothetical liquidation comparison underlying preference law.
- *In re Barefoot*, 952 F.2d 795 (4th Cir. 1991) — Addresses preference avoidance and the transfer of an interest in property.
- *In re ESA Environmental Specialists, Inc.*, 709 F.3d 388 (4th Cir. 2013) — Discusses the contemporaneous-exchange-for-new-value defense.

Fraudulent Transfers Before Bankruptcy: Gifts, Property Transfers to Relatives, and the Risk of Losing a Discharge

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By Alan J. Belsky, Attorney at Law

Giving Property Away Before Bankruptcy Can Make Matters Much Worse

A person overwhelmed by debt may be tempted to protect valuable property by transferring it to a spouse, child, parent, or friend before filing bankruptcy.

The reasoning may seem straightforward: if the property is no longer titled in the debtor's name, perhaps the bankruptcy trustee cannot reach it.

That assumption can be dangerously mistaken.

Federal bankruptcy law gives trustees substantial authority to challenge certain transfers made before bankruptcy, recover transferred property or its value, and pursue remedies against recipients.

In serious cases, the debtor's conduct may also result in denial of the entire bankruptcy discharge.

The term *fraudulent transfer* can be misleading because not every avoidable transfer requires proof that the debtor intended to defraud anyone.

Some transfers are avoidable because the debtor received less than reasonably equivalent value while insolvent or under other specified financial conditions.

Understanding the distinction between actual fraud, constructive fraud, and ordinary preferential payments is essential.

1. What Is a Fraudulent Transfer?

Under 11 U.S.C. § 548, a bankruptcy trustee may avoid certain transfers of the debtor's interest in property made within two years before the bankruptcy petition.

The statute recognizes two principal categories.

An *actually fraudulent transfer* involves a transfer made with actual intent to hinder, delay, or defraud creditors.

A *constructively fraudulent transfer* may be avoidable even without fraudulent intent when the debtor received less than reasonably equivalent value and specified financial conditions existed.

The trustee must establish the applicable statutory elements.

A transfer is not automatically fraudulent merely because it occurred before bankruptcy or involved a relative.

2. Actual Fraud: Intent to Hinder, Delay, or Defraud Creditors

Section 548(a)(1)(A) permits avoidance of certain transfers made with actual intent to hinder, delay, or defraud creditors.

The statute is phrased in the alternative.

A transfer intended to hinder or delay creditors may satisfy the provision even when the debtor does not believe the conduct constitutes fraud in the ordinary sense.

Example

A debtor owns a valuable vehicle free and clear.

After receiving notice of a collection lawsuit, the debtor transfers title to an adult child without receiving payment.

The debtor continues driving and maintaining the vehicle.

The timing, lack of consideration, close relationship, and continued use may support an inference that the transfer was intended to place the asset beyond creditors' reach.

The trustee may seek to avoid the transfer.

Depending on the circumstances, the conduct may also create grounds for denial of discharge.

3. Constructive Fraud: Intent Is Not Always Required

Under § 548(a)(1)(B), certain transfers may be avoided when the debtor received less than reasonably equivalent value and satisfied one of the statute's specified financial conditions.

Those conditions include insolvency, becoming insolvent because of the transfer, unreasonably small capital, or intending or believing that debts would be incurred beyond the debtor's ability to pay.

Example

A debtor owns equipment worth $30,000.

The debtor sells it to a relative for $5,000 while insolvent.

Even if the debtor genuinely believes the transaction is permissible, the trustee may argue that the debtor received less than reasonably equivalent value.

The absence of an express admission of fraudulent intent does not necessarily protect the transaction.

4. What Is Reasonably Equivalent Value?

Reasonably equivalent value is not necessarily identical to fair market value in every circumstance.

Courts examine the economic substance of the transaction and the value received by the debtor.

Relevant considerations may include the property's market value, the consideration paid, the circumstances of the transaction, and any indirect economic benefits.

A sale to an unrelated purchaser following genuine market exposure may present different evidence from a private transfer to a family member for nominal consideration.

The Supreme Court addressed reasonably equivalent value in the foreclosure context in *BFP v. Resolution Trust Corp.*, 511 U.S. 531 (1994).

The Court held that the price received at a noncollusive foreclosure sale conducted in accordance with applicable state law satisfied the reasonably equivalent value requirement for the mortgage foreclosure at issue.

That holding does not mean every forced sale or private transaction necessarily produces reasonably equivalent value.

5. Transfers to Family Members

Transfers to spouses, children, parents, siblings, and other relatives often receive close scrutiny.

Family relationships can be relevant evidence when evaluating the circumstances of a transaction.

However, a transfer to a relative is not automatically avoidable.

A genuine sale for reasonably equivalent value may be legitimate.

Conversely, a transaction with an unrelated person may be fraudulent if the statutory requirements are satisfied.

The focus remains on the debtor's intent, the consideration received, financial condition, and other relevant facts.

6. Transferring a House Before Bankruptcy

Real estate transfers can create particularly serious consequences.

Suppose a debtor owns a home with substantial equity and transfers the property to an adult child shortly before filing Chapter 7.

The debtor receives little or no payment and continues residing in the property.

The trustee may investigate whether the transfer was actually or constructively fraudulent.

The trustee may seek to recover the property or its value, subject to applicable law.

The debtor may also face a discharge objection if the transfer involved the intent required under § 727(a)(2).

A debtor should not assume that recording a deed makes the transfer immune from bankruptcy scrutiny.

7. Adding a Relative to a Deed

A debtor may believe that adding a child or other relative to the deed is less problematic than transferring the entire property.

But conveying a partial ownership interest can itself constitute a transfer.

For example, a debtor who owns a residence individually may execute a deed adding an adult child as a joint owner without receiving consideration.

That transaction may reduce the debtor's ownership interest and potentially affect creditors' rights.

The trustee may investigate the transfer's value, timing, purpose, and legal effect.

The fact that the debtor remains on the deed does not eliminate avoidance concerns.

8. Transfers Between Spouses

Transfers between spouses require careful analysis.

A debtor may transfer property to a spouse for legitimate estate-planning, marital, or financial reasons.

But transfers designed to shield assets from creditors may be challenged.

The analysis may also involve Maryland tenancy-by-the-entirety law, divorce proceedings, marital settlement agreements, and the nature of the spouses' debts.

A transfer made pursuant to a divorce agreement is not automatically immune from avoidance.

The trustee may examine the consideration exchanged, the debtor's financial condition, and the transaction's economic substance.

9. Divorce and Property Settlement Agreements

A divorce can involve transfers of real estate, retirement assets, bank accounts, and other property.

Such transfers may arise from legitimate marital property rights.

Nevertheless, bankruptcy courts may examine whether a particular transfer is avoidable under federal or state law.

The fact that a transfer was incorporated into a marital settlement agreement or divorce judgment does not necessarily resolve every fraudulent-transfer question.

Relevant issues may include the value of the property transferred, the obligations assumed by the other spouse, the timing, and the debtor's financial condition.

A debtor contemplating bankruptcy during or after divorce should obtain advice concerning both family-law and bankruptcy consequences.

10. Transferring Property to a Trust

Transferring property into a trust may constitute a transfer for bankruptcy purposes.

The consequences depend on the type of trust, the debtor's retained interests, the beneficiaries, and the circumstances of the transaction.

A revocable living trust ordinarily does not automatically remove property from bankruptcy consideration.

The debtor's power to revoke the trust or control its assets may be significant.

Irrevocable trusts require separate analysis.

A debtor should not assume that property becomes inaccessible to creditors merely because legal title is held by a trustee.

11. The Federal Two-Year Lookback Period

Section 548 generally permits avoidance of qualifying transfers made within two years before the bankruptcy filing.

This is an important limitation, but it does not mean that transfers older than two years are necessarily safe.

Section 544(b) may permit the trustee to invoke applicable nonbankruptcy fraudulent-transfer law.

State law may provide different limitation periods or other remedies.

The debtor's conduct may also have consequences under provisions governing concealment, false oaths, or denial of discharge.

The passage of two years does not automatically eliminate every risk.

Section 548(e) also supplies a special ten-year rule for specified transfers to self-settled trusts or similar devices where the debtor is a beneficiary and the required actual intent is established. It is a separate exception to the ordinary two-year discussion, not a ten-year lookback for every trust transfer.

12. Maryland Fraudulent-Transfer Law

Maryland has adopted statutory provisions governing transfers made to hinder, delay, or defraud creditors and certain transfers made without adequate value under specified financial conditions.

These provisions appear in Maryland's Commercial Law Article, Title 15, Subtitle 2.

Maryland’s statute uses the term fair consideration in its constructive-fraud provisions; that state-law test must not be assumed identical in every respect to the federal reasonably-equivalent-value test. Section 15-204 addresses conveyances without fair consideration by a person who is or becomes insolvent, while § 15-207 addresses actual intent to hinder, delay, or defraud present or future creditors.

Maryland law can be relevant when a bankruptcy trustee invokes § 544(b).

The applicable state-law provisions may permit challenges to transfers outside the federal two-year period, subject to statutory limitations and other requirements.

The particular transfer date and applicable version of Maryland law must be examined.

13. The Trustee's Powers Under § 544

Section 544(b) generally permits the trustee to avoid a transfer that an actual qualifying unsecured creditor could avoid under applicable law.

This is sometimes called the trustee's *strong-arm* authority, although § 544 contains several distinct powers.

The trustee's rights under § 544(b) depend on the existence of a qualifying creditor and the applicable nonbankruptcy law.

A trustee cannot necessarily invoke every theoretical state-law claim without satisfying the statutory requirements.

The relationship between federal and state avoidance law can be complex.

14. Recovery From the Recipient

Avoiding a transfer and recovering property are related but distinct steps.

Under § 550, a trustee may recover transferred property or its value from specified transferees or beneficiaries, subject to statutory defenses and limitations.

For example, a trustee who successfully avoids a transfer of money to a relative may seek repayment from that relative.

A recipient who received property in good faith and for value may possess defenses under applicable law.

The recipient's legal position should be evaluated independently of the debtor's conduct.

15. What Happens if the Property Has Been Sold Again?

A transferred asset may have been sold or transferred to another person before the trustee acts.

Section 550 addresses recovery from initial and subsequent transferees, subject to statutory limitations.

The rights of subsequent transferees may depend on good faith, value given, and knowledge of the transfer's avoidability.

A trustee may seek recovery of the property's value when recovery of the property itself is unavailable or inappropriate.

The existence of additional transfers does not necessarily defeat the trustee's claim.

16. Fraudulent Transfers Versus Preferential Payments

A preference generally involves payment or security given on account of an existing debt that favors one creditor over others.

A fraudulent transfer may involve an intentional effort to hinder creditors or a transfer for inadequate value under specified financial conditions.

For example, repaying a genuine loan to a parent shortly before bankruptcy may be preferential without being fraudulent.

Giving a valuable vehicle to a child without payment may present fraudulent-transfer issues.

The doctrines can overlap, but their elements and defenses differ.

17. Can a Fraudulent Transfer Cause Denial of Discharge?

Yes.

Section 727(a)(2) permits denial of discharge under specified circumstances involving transfers, removal, destruction, mutilation, or concealment of property with intent to hinder, delay, or defraud creditors or an officer of the estate.

For certain prepetition conduct, the statute focuses on the one-year period before filing.

The statute also addresses qualifying postpetition conduct involving estate property.

Denial of discharge is a much more severe consequence than avoidance of a particular transfer.

If the debtor is denied a Chapter 7 discharge, numerous otherwise dischargeable debts may remain enforceable.

18. Concealment and Continuing Concealment

A debtor may attempt to avoid scrutiny by transferring title while continuing to exercise control over the property.

For example, a debtor may transfer a residence to a relative but continue living there, paying expenses, and treating the property as personally owned.

Courts may examine whether the debtor retained a concealed beneficial interest.

Under the continuing-concealment doctrine, conduct beginning outside the ordinary one-year period may, in appropriate circumstances, support a discharge objection when concealment continues into the relevant period.

The doctrine is fact-specific and requires careful application of governing precedent.

19. False Oaths and Incomplete Disclosure

Even when a transfer itself is not avoidable, failure to disclose it can create separate problems.

Section 727(a)(4) addresses certain knowing and fraudulent false oaths or accounts.

The statement of financial affairs requires disclosure of specified prepetition transfers.

A debtor who omits a significant transfer may face investigation, amendment requirements, or discharge litigation.

The debtor should disclose the transaction accurately even when the debtor believes it was legitimate.

20. Is Ordinary Estate Planning Prohibited Before Bankruptcy?

No.

Not every estate-planning transaction is fraudulent.

Individuals may create wills, trusts, powers of attorney, and other arrangements for legitimate reasons.

However, transferring valuable property while insolvent or facing substantial creditor claims can raise serious questions.

The legality of a transaction depends on its substance, timing, purpose, consideration, and the debtor's financial circumstances.

A debtor anticipating bankruptcy should obtain advice before transferring assets as part of estate planning.

21. Can Exemption Planning Be Fraudulent?

Bankruptcy law generally permits debtors to claim exemptions authorized by statute.

The mere fact that a debtor lawfully converts one form of property into another does not necessarily establish fraud.

However, transactions undertaken with actual intent to hinder, delay, or defraud creditors may trigger avoidance or discharge issues.

The Bankruptcy Code also contains specific provisions addressing certain transfers and homestead-related misconduct.

The distinction between lawful exemption planning and fraudulent conduct can be significant.

A debtor should not attempt aggressive asset conversion without careful legal analysis.

22. What Should a Debtor Do After Making a Questionable Transfer?

The debtor should disclose the transaction fully to bankruptcy counsel.

Relevant documents may include deeds, titles, bank statements, payment records, contracts, and communications concerning the transfer.

The debtor should not attempt to conceal the transaction, backdate documents, or create misleading explanations.

Whether a transfer can or should be reversed requires legal analysis.

Returning property does not necessarily eliminate every avoidance or discharge issue.

The appropriate response depends on the facts and applicable law.

Conclusion

Fraudulent-transfer law prevents debtors from improperly placing assets beyond creditors' reach before bankruptcy.

Some transfers are avoidable because they were made with actual intent to hinder, delay, or defraud creditors.

Others may be avoided because the debtor received less than reasonably equivalent value under specified financial circumstances.

Transfers to family members, changes in real estate ownership, trust arrangements, and divorce-related transfers can present substantial risks.

The consequences may include recovery of property from recipients, litigation, and—in serious cases—denial of the debtor's entire discharge.

A debtor considering bankruptcy should disclose and evaluate significant prior transfers rather than assuming that property no longer titled in the debtor's name is beyond the trustee's reach.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 548 — Fraudulent transfers and obligations.
- 11 U.S.C. § 544 — Trustee's avoidance powers under applicable law.
- 11 U.S.C. § 550 — Recovery of avoided transfers.
- 11 U.S.C. § 727 — Denial of discharge.
- 11 U.S.C. § 522 — Exemptions and certain homestead-related limitations.

Maryland law

- Maryland Commercial Law Article, Title 15, Subtitle 2 — Maryland fraudulent conveyance and transfer provisions.

Selected decisions

- *BFP v. Resolution Trust Corp.*, 511 U.S. 531 (1994) — Addresses reasonably equivalent value in qualifying mortgage foreclosure sales.
- *Husky International Electronics, Inc. v. Ritz*, 578 U.S. 355 (2016) — Addresses actual fraud in the dischargeability context, including fraudulent-transfer schemes.
- *Stern v. Marshall*, 564 U.S. 462 (2011) — Addresses constitutional limits on bankruptcy courts' authority to enter final judgments on certain claims.
- *In re Bane*, 720 F.3d 465 (4th Cir. 2013) — Addresses denial of discharge arising from transfers intended to hinder, delay, or defraud creditors.

Bankruptcy and Divorce in Maryland: What Happens to the House, Joint Debts, Support Obligations, and Property Settlement Agreements?

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By Alan J. Belsky, Attorney at Law

Divorce and Bankruptcy Can Produce Unexpected Financial Consequences

Divorce and bankruptcy are separate legal proceedings, but they frequently affect the same property, debts, and financial obligations.

A divorce may determine which spouse is entitled to occupy the marital home, who must pay the mortgage, how retirement accounts are divided, and which spouse is responsible for particular debts.

Bankruptcy, however, is governed by federal law. A divorce decree or marital settlement agreement does not necessarily control how creditors, bankruptcy trustees, or the bankruptcy court must treat those obligations.

The distinction can have serious consequences.

A former spouse may be awarded the marital residence but remain exposed to foreclosure because both parties are liable on the mortgage. A debtor may be required to pay a joint credit card under a divorce agreement even though the creditor retains the right to collect from both spouses.

And a divorce can terminate tenancy-by-the-entirety ownership, eliminating an important form of property protection even when the deed has never been changed.

Understanding these interactions is essential when bankruptcy is contemplated before, during, or after divorce.

1. Divorce Does Not Automatically Eliminate Joint Debts

A divorce decree may allocate responsibility for debts between spouses.

For example, a marital settlement agreement may require the husband to pay a joint credit card balance and hold the wife harmless from collection.

That agreement generally does not release the wife from her contractual obligation to the credit card company.

The creditor was not necessarily a party to the divorce agreement and ordinarily retains its rights against both borrowers.

If the husband later files bankruptcy, the creditor may continue pursuing the wife, subject to applicable law.

The wife may possess a separate claim against the husband under the marital settlement agreement.

The dischargeability of that obligation requires analysis under the Bankruptcy Code.

2. Joint Credit Cards and Authorized Users

Not every credit card used during marriage creates joint liability.

A spouse may be a joint account holder, an authorized user, or otherwise contractually obligated.

The distinction matters.

An authorized user ordinarily does not become personally liable merely because the user was permitted to make purchases.

A joint account holder may remain liable for the entire balance according to the account agreement.

A divorce decree allocating responsibility does not necessarily alter the creditor's rights.

Before filing bankruptcy, the parties should determine precisely who is contractually liable for each obligation.

3. Domestic Support Obligations Are Generally Nondischargeable

Under 11 U.S.C. § 523(a)(5), domestic support obligations generally are not dischargeable in Chapter 7.

The Bankruptcy Code defines domestic support obligations in § 101(14A).

Qualifying obligations can include child support, alimony, maintenance, and certain other debts owed to or recoverable by specified persons or governmental units.

The substance of the obligation matters.

A payment labeled a property settlement may nevertheless qualify as support if its actual legal character satisfies the statutory definition.

Domestic support obligations also receive priority treatment under § 507(a)(1).

4. Property Settlement Obligations in Chapter 7

Section 523(a)(15) generally excepts from Chapter 7 discharge certain debts owed to a spouse, former spouse, or child that were incurred in the course of divorce or separation or in connection with a divorce decree, separation agreement, or other qualifying court order.

These obligations may include property division payments, indemnification obligations, and certain agreements to assume marital debts.

Unlike domestic support obligations, they may not receive the same priority treatment.

But they generally survive Chapter 7 discharge.

For example, a husband who agrees to reimburse his former wife for a specified marital debt may remain obligated under the divorce agreement even after receiving a Chapter 7 discharge.

The creditor's claim and the former spouse's reimbursement claim are legally distinct.

5. Chapter 13 May Treat Certain Divorce Debts Differently

Chapter 13 provides a different discharge framework.

Under § 1328(a), some obligations described in § 523(a)(15) may be dischargeable upon completion of a qualifying Chapter 13 plan.

Domestic support obligations generally remain nondischargeable.

This distinction can materially affect chapter selection.

A debtor with substantial property settlement obligations may have different options under Chapter 13 than under Chapter 7.

However, the debtor must satisfy Chapter 13 eligibility and plan requirements.

The nature of the divorce obligation must be carefully classified.

6. What Happens to the Marital Home?

The treatment of the marital residence depends on ownership, liens, exemptions, divorce documents, and the timing of the bankruptcy.

A divorce decree may award one spouse possession of the home without immediately changing legal title.

A settlement agreement may require one spouse to refinance the mortgage or execute a deed.

The parties may also agree to continue owning the property jointly.

Bankruptcy law generally looks to the debtor's actual legal and equitable interests in the property.

The trustee may examine the deed, divorce decree, settlement agreement, amendments, and other relevant documents.

A debtor should not assume that a divorce agreement has eliminated an ownership interest unless the agreement and applicable law actually produce that result.

7. Tenancy by the Entirety Before Divorce

Maryland recognizes tenancy by the entirety for qualifying property owned by married spouses.

This form of ownership generally protects the property against creditors holding claims against only one spouse.

The protection may be particularly valuable when one spouse files Chapter 7 individually.

However, joint creditors can affect the exemption.

In *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985), the Fourth Circuit addressed the administration of Maryland entireties property for the benefit of joint creditors.

The protection therefore depends not only on how the home is titled but also on the character of the debts.

8. Divorce Can Terminate Entireties Ownership Without a New Deed

An absolute divorce generally terminates tenancy-by-the-entirety ownership in Maryland.

Unless the property has otherwise been validly disposed of, the former spouses ordinarily become tenants in common.

This change can occur even though the original deed remains recorded and no replacement deed has been executed.

Example

A husband and wife purchase a home while married and take title as tenants by the entirety.

They later divorce.

Their agreement provides that both will continue owning the property and paying the mortgage equally.

No new deed is recorded.

The property generally is no longer held by the entirety because the marital relationship has ended.

Each former spouse ordinarily holds a separate undivided ownership interest as a tenant in common, subject to the terms and legal effect of the divorce documents.

If one former spouse files Chapter 7, that person's ownership interest may become available for administration by the bankruptcy trustee, subject to exemptions and other protections.

The former entireties protection cannot simply be assumed to continue.

9. Why Tenancy in Common Can Be Riskier in Bankruptcy

A tenant in common owns a separate undivided interest in the property.

That interest generally becomes property of the bankruptcy estate when the owner files Chapter 7.

The trustee may seek to administer the debtor's interest.

Under § 363(h), a trustee may, in specified circumstances, sell both the estate's interest and a nondebtor co-owner's interest.

The statute imposes requirements and provides protections for the nondebtor co-owner.

The trustee's authority is not unlimited.

Nevertheless, a former spouse may face the possibility of a sale even though that spouse did not file bankruptcy.

10. Maryland's Increased Homestead Exemption

Maryland's 2026 increase in the bankruptcy residential-property exemption to $125,000 provides additional protection for qualifying homeowners.

This change can be especially important following divorce, when tenancy-by-the-entirety protection no longer applies.

A debtor who owns an undivided interest in a former marital residence may be able to exempt qualifying equity under Maryland Courts and Judicial Proceedings Article § 11-504(f).

However, the statute's owner-occupancy and other requirements must be satisfied.

The exemption does not automatically protect every interest in jointly owned real estate.

11. What If Both Former Spouses Still Owe the Mortgage?

A divorce does not ordinarily release either borrower from a mortgage loan.

Even if one spouse agrees to make all future payments, the lender may retain contractual rights against both borrowers.

If the responsible spouse defaults, the lender may pursue available remedies, including foreclosure.

A bankruptcy discharge may eliminate one debtor's personal liability on a dischargeable mortgage obligation, but the mortgage lien generally survives.

The nonfiling former spouse may remain personally liable.

A divorce agreement requiring refinancing may create additional rights between the former spouses, but it does not necessarily compel the lender to release either borrower.

12. What If the Divorce Agreement Requires Refinancing?

A settlement agreement may require one spouse to refinance the mortgage within a specified period.

If refinancing does not occur, the parties may have contractual or court-enforceable rights under the agreement.

Bankruptcy can complicate enforcement.

The obligation to refinance, indemnify, or hold the other spouse harmless may require analysis under §§ 523(a)(5) and 523(a)(15).

The lender's rights remain separate.

A debtor should not assume that bankruptcy automatically eliminates a refinancing obligation or resolves the other spouse's exposure to the mortgage.

13. Property Transfers Required by Divorce

A divorce decree or settlement agreement may require transfers of real estate, vehicles, retirement accounts, or other assets.

If bankruptcy is filed before the transfer is completed, the debtor's property interests may become part of the bankruptcy estate.

The trustee may examine whether the other spouse possesses enforceable rights in the property.

The timing and legal effect of the divorce documents are critical.

A transfer made shortly before bankruptcy may also raise avoidance questions, depending on the circumstances.

The fact that the transfer occurred in connection with divorce does not automatically resolve every bankruptcy issue.

14. Fraudulent Transfers and Divorce Settlements

A bankruptcy trustee may investigate whether property transferred in connection with divorce was exchanged for reasonably equivalent value or was intended to hinder, delay, or defraud creditors.

Legitimate marital property settlements are not automatically fraudulent.

However, a debtor cannot necessarily insulate valuable property from creditors merely by transferring it to a spouse through an agreement.

The trustee may examine the overall exchange of property and obligations.

Federal avoidance provisions and applicable Maryland law may be relevant.

15. Retirement Accounts and Divorce

Retirement assets may be divided through divorce proceedings.

Qualified domestic relations orders and other legally effective instruments may determine the parties' rights.

The bankruptcy treatment depends on the nature of the retirement plan, the timing of the division, and the debtor's legal and equitable interests.

Many retirement accounts receive substantial bankruptcy protection.

But an obligation to transfer retirement benefits under a divorce decree may present different issues from the exemption of an account already owned by the debtor.

The relevant plan documents and court orders should be reviewed.

16. Parent PLUS Loans and Divorce Agreements

Parent PLUS loans are generally obligations of the parent who borrowed the funds.

A divorce agreement may require the former spouses to share repayment.

But the federal loan holder ordinarily retains its contractual rights against the named borrower.

The former spouse's obligation to contribute may constitute a separate divorce-related debt.

The bankruptcy treatment of that reimbursement obligation requires analysis under § 523(a)(15) and other applicable provisions.

The student loan itself may be subject to § 523(a)(8).

These are distinct legal obligations.

17. The Automatic Stay and Divorce Proceedings

Bankruptcy does not necessarily stop every aspect of a divorce case.

Section 362(b)(2) contains exceptions for specified family-law proceedings, including certain matters involving divorce, child custody, domestic support, and domestic violence.

However, proceedings to divide property that belongs to the bankruptcy estate may be affected by the automatic stay.

A family court may be able to address marital status or support issues while certain property disputes remain subject to bankruptcy restrictions.

The distinction requires careful attention to the relief being requested.

18. Can a Former Spouse Collect Support During Bankruptcy?

Domestic support obligations receive special treatment under the automatic stay provisions.

Certain collection activities involving property that is not property of the bankruptcy estate may continue.

Other statutory exceptions permit specified support-related proceedings and enforcement actions.

The details depend on the chapter, the property involved, and the collection method.

A debtor should not assume that filing bankruptcy stops child support enforcement.

Nor should a former spouse assume that every collection remedy remains available without restriction.

19. What If One Spouse Files Bankruptcy Before Divorce?

Filing before divorce may preserve certain property interests and exemptions that could change after the marriage ends.

For example, tenancy-by-the-entirety protection may be available while the parties remain married but may terminate upon absolute divorce.

However, filing before divorce can also complicate property division and create competing proceedings.

The bankruptcy trustee may acquire rights in estate property that affect what the divorce court can distribute.

The timing of the two proceedings should be coordinated when possible.

20. What If Bankruptcy Is Filed After Divorce?

After divorce, the debtor's ownership interests and obligations must be determined under the divorce judgment, settlement agreements, deeds, and applicable law.

The debtor may own a tenancy-in-common interest in real estate, owe property settlement obligations, or remain liable on joint debts.

The bankruptcy trustee may investigate those interests.

The debtor should provide complete copies of the divorce documents, including amendments and subsequent orders.

An outdated draft agreement may not accurately reflect the parties' final rights.

21. Why Divorce and Bankruptcy Planning Must Be Coordinated

The order in which divorce and bankruptcy occur can materially affect property rights, exemptions, dischargeability, and creditor remedies.

A debtor may benefit from filing before divorce in some circumstances.

In others, completing the divorce first may simplify the financial arrangements.

There is no universal rule.

The appropriate strategy depends on the ownership of property, nature of debts, support obligations, income, exemptions, and anticipated settlement terms.

The decision should be made with a full understanding of both Maryland family law and federal bankruptcy law.

Conclusion

Divorce and bankruptcy frequently intersect in ways that are not apparent from the divorce decree alone.

A marital settlement agreement may allocate responsibility for debts without releasing either spouse from liability to creditors.

Domestic support obligations and many divorce-related property settlement debts generally survive Chapter 7.

Divorce may also terminate tenancy-by-the-entirety ownership, exposing property interests that were previously protected.

Maryland's increased residential exemption provides additional protection for qualifying homeowners, but it does not eliminate every risk.

When divorce and bankruptcy are both possible, the timing of the proceedings and the precise legal effect of property and debt arrangements should be evaluated together.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 101(14A) — Definition of domestic support obligation.
- 11 U.S.C. § 362(b)(2) — Family-law exceptions to the automatic stay.
- 11 U.S.C. § 523(a)(5), (15) — Domestic support and divorce-related exceptions to discharge.
- 11 U.S.C. § 522 — Exemptions, including tenancy-by-the-entirety interests.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 363(h) — Sale of certain jointly owned property.
- 11 U.S.C. § 1328 — Chapter 13 discharge.

Maryland law

- Maryland Code, Family Law Article — Divorce, marital property, and related obligations.
- Maryland Code, Courts and Judicial Proceedings § 11-504 — Maryland exemptions.

Selected decisions

- *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985) — Addresses Maryland tenancy-by-the-entirety property and joint creditors.
- *Bruce v. Dyer*, 309 Md. 421, 524 A.2d 777 (1987) — Discusses tenancy-by-the-entirety ownership.
- Catron v. Catron (In re Catron), 43 F.3d 1465 (4th Cir. 1994) (unpublished table decision) — Applies the pre-2005 support analysis to a marital settlement obligation. It is not binding published circuit precedent and does not replace the present text of § 523(a)(5) or (15).
- *In re Long*, 794 F.2d 928 (4th Cir. 1986) — Discusses dischargeability of obligations arising from marital relationships under the statutory framework then applicable.
- *In re Bane*, 720 F.3d 465 (4th Cir. 2013) — Addresses transfers and denial of discharge.

Preference Recovery Actions by Debtors' Counsel: Recovering Garnished Wages and Other Prepetition Transfers

BELSKY BANKRUPTCY LEGAL LIBRARY | BANKRUPTCY LITIGATION AND DEBTOR REMEDIES

By Alan J. Belsky, Attorney at Law

The Debtor May Have Recovery Rights Even When the Trustee Declines to Act

A Chapter 7 bankruptcy filing ordinarily stops further wage garnishment on prepetition unsecured debts. But what happens to wages already garnished before the bankruptcy petition was filed?

Many debtors assume that money is permanently lost. Others believe that only the Chapter 7 trustee can recover payments made to creditors before bankruptcy.

Neither assumption is necessarily correct.

Under 11 U.S.C. § 522(h), an individual debtor may, in specified circumstances, exercise avoidance powers ordinarily available to the bankruptcy trustee. These rights can permit recovery of wages or other property transferred before bankruptcy, even when the trustee decides not to pursue the transfer.

The debtor's right is limited. Section 522(h) does not authorize unrestricted preference litigation, and not every garnishment or payment is recoverable.

The amount transferred, the dates on which the wages were earned, the identity of the creditor, and the debtor's available exemptions can determine whether an action is legally viable.

For debtors who have experienced substantial wage garnishments immediately before filing, this remedy can be an important component of effective bankruptcy representation.

1. The Trustee's Avoidance Powers and the Debtor's Limited Independent Rights

Section 547(b) authorizes a bankruptcy trustee to avoid certain preferential transfers made before bankruptcy.

Ordinarily, recovered property becomes available for administration through the bankruptcy estate.

But Congress recognized that some avoidable transfers involve property the debtor could have exempted had the transfer not occurred.

Sections 522(g) and 522(h) provide a mechanism through which the debtor may preserve or recover qualifying exempt property.

The provisions must be read together.

Section 522(h) generally permits the debtor to avoid a transfer under specified avoidance provisions, including § 547, if the trustee does not attempt to avoid it and the debtor satisfies the conditions established by § 522(g)(1).

The debtor's authority is therefore derivative and conditional. It is not equivalent to a general assignment of the trustee's avoidance powers.

2. The Essential Requirements of § 522(h)

A debtor seeking to avoid a preferential transfer under § 522(h) generally must establish that:

- The transfer is avoidable under an applicable statutory provision, such as § 547.
- The trustee has not attempted to avoid the transfer.
- The transfer was not voluntary.
- The debtor did not conceal the property.
- The debtor could have exempted the property under § 522(g)(1) if the trustee had recovered it.

These requirements are cumulative.

A debtor who establishes the preference elements but cannot establish sufficient exemption rights may lack authority under § 522(h) to avoid the transfer to the extent requested.

Likewise, a debtor who voluntarily repaid a creditor ordinarily cannot rely on § 522(h) merely because the payment otherwise qualifies as preferential.

This distinction is especially important when comparing involuntary wage garnishments with voluntary payments to relatives.

3. Why Wage Garnishments Are Particularly Suitable for Recovery

A wage garnishment is generally an involuntary collection process.

The judgment creditor obtains legal process requiring the employer to withhold qualifying earnings and remit funds according to applicable law.

The employee ordinarily does not voluntarily direct payment to the judgment creditor.

Consequently, wage garnishments may satisfy the involuntary-transfer requirement of § 522(g)(1).

However, involuntariness alone is insufficient.

The debtor must also establish an avoidable transfer, the absence of concealment, available exemption protection, and the trustee's failure to pursue avoidance.

Example

A Maryland debtor has $4,800 withheld from wages pursuant to a judgment garnishment during the ninety days before filing Chapter 7.

The judgment creditor holds an ordinary unsecured claim.

The debtor was insolvent during the relevant period, and the creditor received more than it would have received in a hypothetical Chapter 7 liquidation without the transfer.

Assume the debtor could exempt the recovered funds, the trustee declines to pursue the transfer, and no preference defense applies.

Under those circumstances, debtor's counsel may have a basis to bring an avoidance action under §§ 522(h) and 547.

The precise transfer dates and applicable exemption provisions must still be established.

4. The Minimum Amount Required for Preference Recovery

Section 547(c)(8) provides a defense for certain relatively small transfers in cases involving individuals whose debts are primarily consumer debts.

The provision is particularly important when evaluating wage garnishments.

Section 547(c)(8) bars avoidance of qualifying consumer-case transfers with aggregate value less than $600. The $600 consumer threshold remains unchanged and is not adjusted under § 104. The April 1, 2025 adjustment applies to the separate nonconsumer threshold in § 547(c)(9), which became $8,575.

The statute applies to the aggregate value of qualifying transfers to a particular creditor.

Multiple garnishments are aggregated

Consider a creditor that garnishes the following wages within the ninety-day preference period:

Pay period	Amount garnished
First	$225
Second	$275
Third	$350
Total	$850

Although no individual withholding reaches $600, the aggregate amount is $850.

Assuming the other statutory requirements are satisfied, the small-transfer defense does not bar avoidance merely because each individual garnishment was less than $600.

Conversely, aggregate qualifying transfers of $575 to that creditor would ordinarily fall within the consumer-debt exception. An aggregate of $625 would not; equality with $600 also does not satisfy a defense requiring the aggregate to be less than $600.

The aggregation is creditor-specific. Garnishments by unrelated creditors are not ordinarily combined merely to satisfy the threshold.

The threshold is not a deductible

If qualifying transfers total $850, potential avoidance is not limited to the $250 exceeding the $600 threshold. Similarly, an otherwise avoidable $625 aggregate is not reduced by a $600 deductible.

Subject to the other statutory requirements and defenses, the entire $850 may be avoidable.

The amount ultimately recoverable and retained by the debtor under § 522(h) remains limited by the debtor's available exemption rights.

For debtors whose debts are not primarily consumer debts, § 547(c)(9) provides a separate, higher, periodically adjusted threshold.

5. Why the Ninety-Day Preference Period Matters

The ordinary preference period under § 547(b)(4)(A) is ninety days before the bankruptcy petition.

A judgment creditor may have obtained its judgment or served a garnishment writ months or years before bankruptcy.

That does not necessarily prevent recovery of wages earned during the ninety-day period.

The critical question is when the relevant transfer occurred for federal bankruptcy purposes.

A debtor should not assume that every dollar collected under an old garnishment is beyond recovery.

Nor should the debtor assume that every payment received by a creditor during the ninety days necessarily constitutes a transfer made during that period.

The relevant property rights and transfer dates must be established.

6. When Does a Wage Garnishment Transfer Occur?

Determining the transfer date can be one of the most important legal issues in a preference action.

A creditor may argue that its garnishment lien arose when the writ was served on the employer, even though the employee earned the wages later.

But § 547(e)(3) provides that a transfer is not made until the debtor has acquired rights in the transferred property.

An employee ordinarily does not acquire rights to future wages before earning them.

Accordingly, a garnishment writ served before the preference period does not necessarily establish that all later wage transfers occurred outside the period.

Courts have recognized this distinction in applying § 547(e)(3) to continuing garnishments.

The reasoning is reflected in decisions including *In re Morehead*, 249 F.3d 445 (6th Cir. 2001), and *Tower Credit, Inc. v. Schott (In re Jackson)*, 850 F.3d 816 (5th Cir. 2017).

Example: An old garnishment, but recently earned wages

A judgment creditor serves a wage garnishment in January.

The debtor files Chapter 7 in October.

The creditor argues that the garnishment began more than ninety days before bankruptcy.

That argument does not necessarily resolve the preference issue.

Wages earned during the ninety days before filing may constitute transfers within the preference period, notwithstanding the earlier service of the garnishment writ.

Counsel should distinguish the date of service, the dates wages were earned, the payroll withholding dates, and the dates money was paid to the creditor.

The governing Maryland and federal authorities must be applied to those facts.

7. Why Delaying Bankruptcy May Reduce the Recovery

Timing matters because the ninety-day preference period moves with the petition date.

Consider a debtor who has experienced substantial wage garnishment but has since changed employment, causing the garnishment to stop.

The debtor consults bankruptcy counsel several weeks later.

If bankruptcy is filed promptly, some of the garnished wages may still fall within the preference period.

If the debtor delays filing, additional transfers may fall outside the period.

Example

Assume $3,000 was garnished before bankruptcy.

Of that amount, $2,000 was attributable to wages earned more than ninety days before the petition, while $1,000 was attributable to wages earned within the preference period.

The older transfers generally fall outside the ordinary ninety-day preference window.

The more recent $1,000 may be avoidable, assuming the statutory requirements are satisfied.

If the debtor waits another month, some or all of that $1,000 may also fall outside the period.

This is particularly important when garnishment has ended. When garnishment continues, additional transfers may enter the rolling ninety-day period while older transfers leave it, requiring a fresh calculation.

The filing date can therefore determine not only when future garnishments stop but also how much previously garnished money may be recovered.

Timing cannot be evaluated in isolation

An immediate filing may preserve a preference recovery but create other problems.

For example, the debtor may need additional time to qualify under the means test, protect a tax refund, or resolve a nonexempt-property issue.

The anticipated preference recovery must be weighed against the entire bankruptcy case.

8. The Preference Elements Still Must Be Established

Section 522(h) does not eliminate the substantive requirements of § 547.

The debtor must establish a transfer of an interest in property, to or for the benefit of a creditor, on account of an antecedent debt, made while insolvent, within the applicable preference period, and satisfying the hypothetical Chapter 7 liquidation comparison.

Section 547(f) provides a presumption of insolvency during the ninety days immediately preceding bankruptcy.

The creditor may assert statutory defenses, including applicable ordinary-course, contemporaneous-exchange, new-value, and small-transfer defenses.

For ordinary wage garnishments on unsecured judgments, some defenses may be difficult to establish, but they should not be disregarded without examining the facts.

9. The Importance of *Stine* in Maryland

Maryland has particularly important authority concerning a debtor's recovery of preferentially garnished wages.

In *Bank of America, N.A. (USA) v. Stine*, 252 B.R. 902 (D. Md. 2000), the United States District Court for the District of Maryland addressed a Chapter 7 debtor's attempt to recover $1,064.05 in garnished wages under § 522(h).

The district court concluded that the debtor could avoid the garnishments but that the recovered amount remained subject to Maryland's applicable exemption limits.

The Fourth Circuit certified a question concerning the availability of Maryland exemption protection for the recovered wages.

In *Bank of America v. Stine*, 379 Md. 76, 839 A.2d 727 (2003), Maryland's highest court held that wages recovered after avoidance of a preferential garnishment could be claimed exempt, subject to Maryland's statutory limitations.

The Fourth Circuit subsequently affirmed in *In re Stine*, 360 F.3d 455 (4th Cir. 2004).

The significance of *Stine*

The decision establishes that a debtor's ability to recover garnished wages must be considered together with the available Maryland exemptions.

A debtor who recovers a preference does not necessarily retain the entire recovery.

The debtor must have sufficient exemption protection for the amount claimed.

The historical exemption limits discussed in *Stine* should not be confused with the amounts available under Maryland law at the time of a later bankruptcy filing.

10. The Trustee Must Not Have Attempted Avoidance

Section 522(h) expressly conditions debtor avoidance on the trustee's failure to attempt to avoid the transfer.

In practice, debtor's counsel should communicate with the Chapter 7 trustee before commencing litigation.

The trustee may determine that the potential recovery is too small to justify estate administration, particularly where the debtor could exempt the recovered funds.

A written statement from the trustee declining to pursue avoidance may help establish the debtor's authority to proceed.

However, § 522(h) does not expressly require a formal abandonment order or written refusal in every case.

Counsel should avoid filing a competing action while the trustee is actively pursuing the same transfer.

11. Exemption Analysis Before Litigation

Before demanding recovery, counsel should determine whether the debtor can exempt the funds.

This requires examining Schedule C, the value of other property claimed exempt, and the Maryland statutory provisions applicable on the filing date.

A debtor who has already exhausted an applicable general exemption may be unable to retain additional recovered funds under that same provision.

A successful avoidance action without sufficient exemption protection may produce little practical benefit.

Section 522(i) also addresses the debtor's rights concerning property recovered following avoidance under § 522(h).

The exemption calculation should be completed before substantial litigation expenses are incurred.

12. Commencing an Adversary Proceeding

A contested action seeking avoidance and recovery of preferentially garnished wages ordinarily proceeds through an adversary proceeding under Federal Rule of Bankruptcy Procedure 7001.

The debtor files a complaint in the bankruptcy court and obtains service of the summons and complaint under Rule 7004.

The complaint should identify the transfers, establish the statutory basis for avoidance, allege the debtor's authority under § 522(h), and request appropriate relief under §§ 522(i) and 550.

Counsel should also determine whether the bankruptcy case remains open and whether any procedural relief is necessary before commencing the action.

13. Pleading the Debtor's Recovery Claim

A properly drafted complaint should establish both the underlying preference and the debtor's independent right to prosecute it.

The factual allegations should identify the judgment creditor, underlying judgment, garnishment proceedings, petition date, and each allegedly preferential transfer.

The complaint should allege facts supporting insolvency, antecedent debt, the creditor's improved position under the hypothetical Chapter 7 liquidation test, and the absence of any apparent statutory bar.

Separate allegations should address involuntariness, nonconcealment, the trustee's failure to pursue avoidance, and the debtor's available exemption.

Illustrative pleading framework

A complaint may be organized around jurisdiction and venue, the parties, judgment and garnishment history, bankruptcy filing, identification and timing of transfers, preference elements, § 522(h) prerequisites, and requested relief.

A separate recovery count may invoke §§ 522(i) and 550.

The complaint should not merely allege that wages were garnished within ninety days. That allegation alone does not establish an avoidable preference.

14. Statute of Limitations

Preference actions are subject to the limitations provisions of 11 U.S.C. § 546(a).

The applicable deadline depends on the statutory circumstances, including the commencement of the bankruptcy case, appointment of a trustee, and case closing or dismissal.

A debtor exercising avoidance rights under § 522(h) should not assume that a new limitations period begins when the trustee declines to act.

The limitations issue should be evaluated before filing the adversary complaint.

Delay in obtaining the trustee's position can be particularly problematic when the bankruptcy case has been pending for an extended period.

15. Demand Letters and Settlement Before Litigation

Not every preference recovery requires contested litigation.

Where the law and facts are sufficiently clear, debtor's counsel may first send a demand identifying the garnishments, relevant bankruptcy provisions, available exemptions, and supporting authority.

The demand should explain the proposed recovery amount and provide the creditor an opportunity to resolve the matter voluntarily.

In Maryland, *Stine* supplies particularly relevant authority.

Settlement may avoid filing fees, service expenses, discovery, and litigation costs.

Nevertheless, counsel should avoid overstating the debtor's entitlement. The creditor may possess legitimate defenses, and the debtor must satisfy § 522(h)'s requirements.

16. Can Debtor's Counsel Recover Attorney's Fees?

A successful preference recovery does not automatically entitle debtor's counsel to an additional attorney's fee award against the creditor.

Under the American Rule, attorney's fees ordinarily are not shifted absent an applicable statute, contract, rule, or other recognized legal basis.

Sections 522(h), 522(i), and 547 do not establish a general fee-shifting remedy comparable to § 362(k)'s provision for certain willful automatic-stay violations.

Taxable litigation costs and attorney's fees must be distinguished.

Section 522(k) also addresses the treatment of certain expenses associated with recovering exempt property.

Counsel should evaluate the fee arrangement and anticipated recovery before litigation.

17. The Economics of a Preference Recovery

A preference claim may be legally sound but economically impractical.

For example, recovering $900 through contested litigation may require substantially more in attorney time and expenses than the amount at stake.

A larger garnishment recovery may justify litigation, particularly where the creditor has no substantial defense.

The practical analysis should consider the likely recovery, available exemptions, litigation expenses, settlement prospects, and the defendant's ability to satisfy a judgment.

A debtor should understand whether counsel's fees will be paid from the recovery, separately, or through another lawful arrangement.

18. Recoveries Beyond Wage Garnishment

Section 522(h) is not limited to garnished wages.

Other involuntary transfers may potentially qualify, including certain levies, executions, and transfers arising from judicial collection proceedings.

However, each type of transfer presents different questions concerning the debtor's property interest, timing, exemption rights, and applicable avoidance provision.

A voluntary payment to a relative generally presents a different problem because § 522(g)(1) requires the transfer to have been involuntary.

The debtor's independent avoidance authority should therefore be evaluated transaction by transaction.

19. Why Debtor's Counsel Should Investigate Prepetition Garnishments

A debtor may have lost substantial earnings to a judgment creditor before consulting a bankruptcy attorney.

Those payments should not automatically be treated as irretrievable.

During the initial consultation, counsel should determine when the garnishment began, whether wages were earned during the ninety days before filing, the aggregate amount transferred to each creditor, and whether sufficient exemptions remain available.

Counsel should obtain payroll records rather than relying solely on the debtor's estimate of the total garnishment.

The filing date should be considered carefully because a delay may cause recoverable transfers to fall outside the preference period.

The trustee's intentions should also be established.

This analysis can produce a meaningful benefit beyond stopping future garnishment.

In an appropriate case, bankruptcy may permit the debtor to recover money already taken.

Conclusion

Section 522(h) provides an important but limited remedy for individual bankruptcy debtors.

When the Chapter 7 trustee does not pursue an avoidable transfer, the debtor may have authority to recover property that could have been exempted had the trustee recovered it.

Wage garnishments are particularly significant because they ordinarily involve involuntary transfers, and Maryland appellate authority recognizes the availability of exemption protection for qualifying recovered wages.

The amount and timing of the garnishments are central to the analysis. Multiple transfers to the same creditor may need to be aggregated, and wages earned during the ninety-day preference period may qualify even when the garnishment writ was served earlier.

Recovery is not automatic. The debtor must establish the preference elements, satisfy §§ 522(g) and 522(h), and possess sufficient exemption rights.

Effective Chapter 7 representation should consider not only how to stop future collection, but also whether money already taken from the debtor can lawfully be recovered.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 522(g)–(k) — Debtor exemption, avoidance, recovery, and related protections.
- 11 U.S.C. § 547 — Preferential transfers, defenses, monetary thresholds, and transfer timing.
- 11 U.S.C. § 550 — Recovery of avoided transfers.
- 11 U.S.C. § 546 — Limitations on avoidance actions.
- Federal Rule of Bankruptcy Procedure 7001 — Adversary proceedings.
- Federal Rule of Bankruptcy Procedure 7004 — Service of summons and complaint.

Maryland statutes and rules

- Maryland Courts and Judicial Proceedings § 11-504 — Maryland exemptions.
- Maryland Commercial Law § 15-601.1 — Wage attachment exemptions.
- Maryland Rule 2-646 — Wage garnishment procedure.

Selected decisions

- Bank of America, N.A. (USA) v. Stine, 252 B.R. 902 (D. Md. 2000) — Recognizes the debtor's ability to avoid qualifying preferential wage garnishments under § 522(h), subject to exemption limits.
- Bank of America v. Stine, 379 Md. 76, 839 A.2d 727 (2003) — Holds that preferentially garnished wages recovered through bankruptcy avoidance may qualify for Maryland exemption protection.
- In re Stine, 360 F.3d 455 (4th Cir. 2004) — Affirms the district court following the Maryland court's resolution of the certified question.
- *In re Cox*, 10 B.R. 268 (Bankr. D. Md. 1981) — Early Maryland bankruptcy authority concerning wage garnishment and preference timing.
- *In re Morehead*, 249 F.3d 445 (6th Cir. 2001) — Addresses when wages subject to a continuing garnishment are transferred for preference purposes.
- *Tower Credit, Inc. v. Schott (In re Jackson)*, 850 F.3d 816 (5th Cir. 2017) — Holds that wages earned during the preference period may be preferentially transferred despite earlier service of the garnishment.
- *Barnhill v. Johnson*, 503 U.S. 393 (1992) — Addresses transfer timing for preference purposes in the context of payments by check.

When Chapter 7 Bankruptcy Is the Wrong Choice: Situations Where Filing Can Cause More Harm Than Good

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By Alan J. Belsky, Attorney at Law

Qualifying for Chapter 7 Does Not Necessarily Mean You Should File

Chapter 7 bankruptcy can provide extraordinary relief from overwhelming debt. In a relatively short period, a qualifying debtor may eliminate substantial unsecured obligations and obtain protection against further collection.

But Chapter 7 is not always the right choice.

A person may qualify under the means test, have substantial dischargeable debt, and desperately need financial relief—yet still face serious disadvantages from filing.

The most significant risks often involve property that cannot be exempted, debts that will survive discharge, transfers made before filing, and circumstances in which the debtor needs more than the temporary protection Chapter 7 provides.

In some cases, Chapter 13 offers a substantially better solution. In others, postponing bankruptcy or pursuing a nonbankruptcy alternative may be preferable.

The decision requires more than asking whether a debtor is eligible. It requires determining what bankruptcy will actually accomplish and what the debtor may lose in the process.

1. When the Debtor Owns Substantial Nonexempt Property

Chapter 7 is a liquidation proceeding.

Under 11 U.S.C. § 541, most of the debtor's legal and equitable interests in property become part of the bankruptcy estate when the petition is filed.

The Chapter 7 trustee may administer nonexempt property for the benefit of creditors.

Although most consumer Chapter 7 cases involve no liquidation, a debtor with substantial nonexempt assets may face significant risk.

Examples include valuable investment accounts, real estate equity exceeding available exemptions, expensive vehicles owned free and clear, business interests, and valuable claims or contract rights.

The debtor may be entitled to retain the value of valid exemptions, but the trustee may sell an asset when doing so produces a meaningful benefit to the estate.

A debtor should not assume that the trustee will overlook property merely because selling it would be inconvenient or emotionally difficult.

Example: A paid-off vehicle

A debtor owes $65,000 in unsecured credit card debt and owns a vehicle worth $32,000 free and clear.

The debtor qualifies financially for Chapter 7.

However, the available Maryland exemptions may not protect the vehicle's entire value.

The trustee may consider selling it and distributing the nonexempt proceeds to creditors.

Chapter 13 may permit the debtor to retain the vehicle while paying creditors through a plan that satisfies the applicable liquidation-value requirement.

The debtor's eligibility for Chapter 7 therefore does not establish that Chapter 7 is the better choice.

2. Home Equity Exceeding Maryland's New Exemption

Maryland's 2026 increase in its bankruptcy residential-property exemption to $125,000 substantially expands Chapter 7 protection for qualifying homeowners.

Nevertheless, the exemption does not protect unlimited home equity.

A homeowner with substantial equity exceeding the available exemption may face liquidation risk.

Example

A debtor owns a residence worth $525,000 with a mortgage balance of $325,000.

The estimated equity is $200,000 before considering sale expenses and other relevant adjustments.

Assuming the debtor qualifies for the $125,000 residential exemption and no additional protections apply, approximately $75,000 of equity exceeds that exemption.

The trustee may investigate whether selling the property would provide a meaningful distribution to creditors.

Chapter 13 may permit the debtor to retain the home while satisfying the statutory requirements applicable to nonexempt equity.

The analysis must account for the debtor's ownership interest, liens, exemptions, anticipated sale expenses, and the circumstances of the particular case.

3. When Tenancy by the Entirety Provides Protection—or Does Not

Maryland tenancy-by-the-entirety law may protect substantial property interests owned by married spouses against creditors holding claims against only one spouse.

Under 11 U.S.C. § 522(b)(3)(B), qualifying entireties interests may be exempt to the extent protected from creditor process under applicable nonbankruptcy law.

But joint creditors can change the result.

In *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985), the Fourth Circuit addressed the administration of entireties property when joint creditors exist.

A married debtor with substantial home equity and exclusively individual unsecured debts may present a very different Chapter 7 case from a debtor whose spouse is jointly liable for significant obligations.

The same problem arises following divorce, which generally terminates tenancy-by-the-entirety ownership.

The form of ownership and identity of creditors should be established before filing.

4. When the Debtor Is Behind on Mortgage Payments

Chapter 7 ordinarily provides temporary protection from foreclosure through the automatic stay.

But it does not generally provide a multiyear mechanism for curing mortgage arrears.

A lender may seek relief from the stay and resume foreclosure when legally permitted.

A debtor who wishes to retain the home but cannot immediately cure the default may need Chapter 13.

Under § 1322(b)(5), a qualifying Chapter 13 plan may permit the debtor to cure mortgage arrears over time while maintaining ongoing payments.

The debtor must have sufficient income to fund the plan and satisfy the other statutory requirements.

Example

A homeowner is $24,000 behind on mortgage payments but has resumed employment and can afford the regular mortgage payment.

Chapter 7 may temporarily stop foreclosure, but the arrears remain.

Chapter 13 may allow the homeowner to cure the default through a repayment plan.

In this situation, the longer Chapter 13 process may provide a benefit that Chapter 7 cannot.

5. When Most Debts Will Survive Chapter 7

Chapter 7 ordinarily discharges many credit card balances, medical bills, personal loans, and other unsecured obligations.

But some debts survive.

Examples include certain income taxes, domestic support obligations, qualifying student loans absent undue hardship, and debts arising from specified forms of fraud or intentional misconduct.

A debtor whose financial problems consist primarily of nondischargeable debts may receive little practical benefit from Chapter 7.

For example, a debtor owing $80,000 in recent nondischargeable income taxes and only $5,000 in ordinary credit card debt may not obtain meaningful relief from Chapter 7 alone.

Chapter 13 may provide a structured means of addressing certain priority obligations.

Other tax collection arrangements or nonbankruptcy alternatives may also warrant consideration.

6. When a Pending Personal Injury Claim Is Valuable

A personal injury claim generally becomes property of the bankruptcy estate when the debtor files Chapter 7, even if no lawsuit has yet been filed.

The trustee may acquire authority to prosecute or settle the claim, subject to applicable exemptions and other legal limitations.

Maryland provides substantial exemption protection for qualifying personal injury compensation under Courts and Judicial Proceedings Article § 11-504(b)(2).

But not every component of every lawsuit recovery necessarily receives the same protection.

A claim may include compensation for bodily injury, property damage, contract losses, punitive damages, or other categories requiring separate analysis.

A debtor who files without disclosing a potentially valuable claim may also face serious consequences.

The appropriate bankruptcy strategy should be determined after examining the claim's nature, ownership, likely value, and available exemptions.

7. When the Debtor Expects an Inheritance or Other Property

Chapter 7 can be particularly risky when a debtor expects to receive valuable property.

Under 11 U.S.C. § 541(a)(5), certain interests acquired or becoming available within 180 days after filing become property of the bankruptcy estate.

These include specified interests arising through inheritance, divorce-related property settlements, and life insurance or death benefit arrangements.

Example

A debtor files Chapter 7 while a parent is seriously ill.

The parent dies sixty days after the petition, leaving the debtor a substantial inheritance.

Even though the inheritance was received after filing, the debtor's interest may become property of the bankruptcy estate.

The trustee may administer the nonexempt portion for creditors.

The debtor's rights depend on the nature and timing of the interest, applicable exemptions, and other circumstances.

A debtor should not assume that all property received after filing is beyond the trustee's reach.

8. When the Debtor Recently Repaid Family Members

Repaying a family loan shortly before bankruptcy may create an avoidable preference.

Under § 547, the trustee may recover certain payments made on antecedent debts within ninety days before filing.

The period generally extends to one year for qualifying insider creditors.

For example, a debtor who repays $15,000 to a parent eight months before bankruptcy may expose the parent to a preference recovery action.

The payment need not have been fraudulent.

A debtor who is considering bankruptcy should disclose substantial payments to relatives and evaluate the consequences before filing.

9. When the Debtor Recently Transferred Property

Transfers of property before bankruptcy can create more serious problems.

Under § 548, a trustee may avoid certain transfers made with actual intent to hinder, delay, or defraud creditors, or transfers made for less than reasonably equivalent value under specified financial circumstances.

Section 544 may permit reliance on applicable state-law avoidance remedies.

For example, transferring a valuable vehicle to an adult child without consideration shortly before filing may expose the property to recovery.

The transaction may also create discharge problems if it involved the intent prohibited by § 727(a)(2).

A debtor should not assume that transferring property out of the debtor's name protects it.

10. When Bankruptcy Could Result in Denial of Discharge

Chapter 7 relief depends on compliance with the Bankruptcy Code's disclosure and conduct requirements.

Section 727 permits denial of discharge under specified circumstances, including certain fraudulent transfers, concealment of assets, false oaths, destruction of financial records, and refusal to obey lawful court orders.

Denial of discharge is particularly serious because it can leave the debtor liable for numerous debts that otherwise would have been discharged.

A debtor who has engaged in questionable transactions should obtain legal advice before filing.

The appropriate response is not to conceal the transactions or provide misleading information.

11. When the Debtor Has Substantial Recent Credit Card Charges

Credit card debt is ordinarily dischargeable, but recent transactions may create exceptions.

Section 523(a)(2) addresses debts obtained through specified forms of fraud.

The statute also creates rebuttable presumptions concerning certain luxury purchases and cash advances made shortly before bankruptcy, subject to periodically adjusted monetary thresholds.

A debtor who recently incurred substantial credit card debt may face dischargeability litigation.

However, recent use alone does not automatically establish fraud.

The nature of the purchases, timing, representations, and debtor's circumstances must be examined.

12. When the Debtor Has a Business or Valuable Business Interests

A self-employed debtor may own equipment, inventory, accounts receivable, intellectual property, or an interest in a corporation or limited liability company.

Those interests may become property of the bankruptcy estate.

A Chapter 7 trustee may investigate their value and determine whether they can be administered.

The debtor should not assume that business property is protected merely because it is needed to earn a living.

The legal form of the business matters, but ownership through an LLC or corporation does not automatically eliminate the debtor's personal ownership interest in that entity.

Chapter 13 or another form of bankruptcy relief may provide a better alternative for some debtors with ongoing business operations.

13. When the Debtor Has Significant Income but Passes the Means Test

Passing the means test does not guarantee that Chapter 7 relief is appropriate.

Under § 707(b)(3), a court may consider bad faith or the totality of the debtor's financial circumstances in determining whether a case involving primarily consumer debts constitutes abuse.

A debtor may pass the mechanical calculation yet possess substantial current repayment capacity.

The means test also uses historical income, which may differ from present circumstances.

For example, a debtor who was unemployed during much of the six-month measurement period but has recently obtained a highly compensated position may warrant additional analysis.

The debtor's current and anticipated financial condition should be evaluated, not merely the numerical means-test result.

14. When Chapter 13 Can Protect Property That Chapter 7 Would Expose

Chapter 13 ordinarily allows a debtor to retain property while making payments under a court-approved plan.

Under § 1325(a)(4), unsecured creditors generally must receive at least as much through the plan as they would receive in a hypothetical Chapter 7 liquidation.

This is commonly called the *best-interests-of-creditors test* or *liquidation test*.

Example

A debtor owns $25,000 in nonexempt property.

In Chapter 7, the trustee might liquidate the property for the benefit of creditors.

In Chapter 13, the debtor may be able to retain the property by proposing a feasible plan that satisfies the applicable liquidation-value requirement and other confirmation standards.

The debtor does not necessarily have to surrender the property.

However, Chapter 13 requires sufficient income to fund the plan, and the debtor must satisfy the statutory eligibility and confirmation requirements.

15. When the Debtor Cannot Afford Chapter 13 Either

Chapter 13 is not always a workable alternative.

A debtor may need to cure mortgage arrears, protect nonexempt property, and pay priority debts, but lack sufficient income to fund a feasible repayment plan.

In that situation, neither Chapter 7 nor Chapter 13 may accomplish every desired objective.

The debtor may need to consider selling property voluntarily, negotiating with secured creditors, modifying housing expenses, or pursuing other lawful arrangements.

A bankruptcy filing should not be undertaken on the assumption that a court will approve an unaffordable plan.

16. When a Creditor Is Willing to Settle

Some debtors may be able to resolve financial problems through negotiated settlements without bankruptcy.

For example, an individual with one substantial judgment and otherwise manageable obligations may benefit from negotiating a compromise.

But settlement carries its own risks.

A creditor may refuse to negotiate, other creditors may continue collection, and cancellation of indebtedness can create tax consequences under applicable law.

Payments to selected creditors may also affect a later bankruptcy.

The debtor should evaluate whether settlement will actually resolve the financial problem rather than merely postpone it.

17. When the Debtor Is Judgment-Proof

A person with little income, no nonexempt property, and no realistic ability to pay creditors may be described informally as *judgment-proof*.

That term does not mean creditors cannot sue or obtain judgments.

It means that available collection remedies may produce little or no recovery because the debtor's income and property are protected or otherwise unavailable.

For some individuals, immediate bankruptcy may provide limited additional benefit.

However, judgments, collection pressure, changes in employment, and future acquisitions can affect the analysis.

A debtor who is currently judgment-proof may not remain so indefinitely.

18. When the Debtor Expects a Significant Change in Financial Circumstances

A bankruptcy filing can be affected by anticipated changes in income, property, and household composition.

Examples include retirement, job loss, a substantial bonus, divorce, sale of real estate, or receipt of a significant settlement.

Because bankruptcy rights and obligations often depend on the petition date, timing may materially change the outcome.

A debtor who expects a reduction in income may obtain a different means-test result by filing later.

Conversely, a debtor who expects to acquire valuable nonexempt property may need to consider the consequences of filing before or after that event.

The appropriate timing must be determined from the entire financial picture.

19. When Filing Too Early Could Prevent Discharge of Taxes

Certain older income tax debts may be dischargeable in Chapter 7.

However, dischargeability depends on the statutory timing rules, including the three-year, two-year, and 240-day provisions, as well as other requirements and exceptions.

A debtor who files shortly before the relevant period expires may remain liable for taxes that could have been discharged through a later filing.

For example, filing one month too early may leave a substantial income tax obligation intact.

But waiting also permits creditors and taxing authorities to continue lawful collection.

The decision should be based on verified return, assessment, and tolling dates.

20. When Filing Could Jeopardize a Potential Preference Recovery

Timing can also affect the debtor's ability to recover wages garnished before bankruptcy.

Under §§ 522(h) and 547, a debtor may, in specified circumstances, avoid qualifying preferential transfers that the trustee does not pursue.

The ordinary preference period is ninety days.

If the debtor delays filing, some garnished wages may fall outside the preference period.

The monetary thresholds, available exemptions, and timing of the transfers must be considered.

Thus, delaying bankruptcy may improve the treatment of one obligation while reducing the debtor's ability to recover money previously garnished.

This is another reason bankruptcy timing should not be determined by a single consideration.

21. When the Debtor Has Recently Filed Bankruptcy

The Bankruptcy Code restricts successive discharges.

A prior discharge can bar another Chapter 7 discharge under § 727(a)(8) or (9). The ordinary periods are eight years after commencement of the earlier Chapter 7 or Chapter 11 case, or six years after commencement of the earlier Chapter 12 or Chapter 13 case. The latter rule has exceptions for payment of all allowed unsecured claims, or at least 70% under a good-faith plan representing the debtor's best effort. The measurement is generally filing to filing, rather than discharge to filing.

Repeat filings may also affect the automatic stay under § 362(c)(3) and (4).

A debtor who files a new case without considering these restrictions may discover that the filing provides limited protection or no available discharge.

Prior bankruptcy history should be examined before another petition is filed.

22. When the Debtor Cannot or Will Not Provide Complete Financial Information

Bankruptcy requires full disclosure of assets, debts, income, expenses, transfers, and other financial matters.

A debtor who cannot identify significant assets, explain large transfers, or produce required records may face substantial difficulties.

The trustee may request additional documentation or conduct further examinations.

In serious circumstances, inadequate records or false statements may create grounds for denial of discharge.

A debtor should not file on the assumption that missing information can always be reconstructed later.

Where possible, the necessary financial investigation should occur before filing.

23. When the Costs and Consequences Outweigh the Benefits

Bankruptcy can be extraordinarily beneficial, but it is not cost-free.

The debtor must consider filing expenses, attorney's fees, credit consequences, possible loss of nonexempt property, and obligations that may survive discharge.

The debtor should also consider whether the bankruptcy will solve the underlying financial problem.

For example, eliminating unsecured debt may provide limited relief when ongoing housing and transportation expenses remain unaffordable.

The objective should be a sustainable financial outcome, not merely obtaining a discharge order.

24. The Importance of Comparing Alternatives

Before filing, the debtor should receive a realistic comparison of available options.

Chapter 7 may provide the fastest and most comprehensive discharge of ordinary unsecured debts.

Chapter 13 may provide greater protection for property, mortgage arrears, and certain obligations requiring structured repayment.

Nonbankruptcy alternatives may be appropriate when debts are limited, settlement is feasible, or collection remedies are ineffective.

In some cases, waiting may improve the legal result.

In others, delay may expose the debtor to foreclosure, garnishment, repossession, or loss of valuable recovery rights.

There is no universally correct answer.

Conclusion

Chapter 7 bankruptcy can provide substantial relief, but eligibility alone does not establish that filing is advisable.

A debtor may qualify financially yet face liquidation of valuable property, nondischargeable obligations, trustee avoidance actions, or other consequences that outweigh the benefits.

Maryland's increased residential exemption has made Chapter 7 more attractive for many homeowners, but careful planning remains essential. The 2026 legislation took effect June 1, 2026, and expanded the exemption for qualifying owner-occupied residential property.

The proper question is not simply, “Can I file Chapter 7?” It is, “Will Chapter 7 leave me in a better financial and legal position than the alternatives?”

That determination should be made before the petition is filed.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 522 — Exemptions.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 547 — Preferential transfers.
- 11 U.S.C. § 548 — Fraudulent transfers.
- 11 U.S.C. § 707 — Chapter 7 dismissal and abuse.
- 11 U.S.C. § 727 — Chapter 7 discharge and denial of discharge.
- 11 U.S.C. § 1322 — Chapter 13 plan provisions.
- 11 U.S.C. § 1325 — Chapter 13 plan confirmation and liquidation-value requirements.

Maryland law

- Maryland Courts and Judicial Proceedings § 11-504 — Maryland property exemptions.
- Maryland Senate Bill 939, Chapter 400 (2026) — Expansion of the residential-property exemption.

Selected decisions

- *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985) — Addresses tenancy-by-the-entirety property and joint creditors.
- *Schwab v. Reilly*, 560 U.S. 770 (2010) — Addresses the scope and valuation of claimed exemptions.
- *Law v. Siegel*, 571 U.S. 415 (2014) — Limits bankruptcy courts' equitable authority to override statutory exemptions.
- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Addresses known or virtually certain changes in income or expenses in Chapter 13 projected disposable-income calculations.
- *In re Bane*, 720 F.3d 465 (4th Cir. 2013) — Addresses transfers made with intent to hinder, delay, or defraud creditors and denial of discharge.
- *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365 (2007) — Addresses bad faith and conversion between bankruptcy chapters.
- *Grogan v. Garner*, 498 U.S. 279 (1991) — Addresses the evidentiary standard for exceptions to discharge.

Chapter 7 Versus Chapter 13 Bankruptcy in Maryland: Choosing the Right Chapter and Understanding the Consequences

Belsky Bankruptcy Legal Library | Bankruptcy Planning and Strategy

By Alan J. Belsky, Attorney at Law

Two Bankruptcy Chapters, Two Different Approaches to Debt Relief

Individuals considering bankruptcy frequently assume that Chapter 7 is intended for people with little income, while Chapter 13 is reserved for those who earn more. Although income can influence eligibility, that distinction oversimplifies the law.

Chapter 7 and Chapter 13 provide fundamentally different forms of bankruptcy relief.

Chapter 7 ordinarily permits an eligible debtor to discharge qualifying debts without making payments through a multiyear repayment plan. In exchange, the debtor's nonexempt property may be liquidated by a bankruptcy trustee.

Chapter 13 generally permits an eligible individual with regular income to retain property while making payments under a court-approved plan lasting three to five years.

Neither chapter is inherently better.

The appropriate choice depends on the debtor's assets, income, debts, financial objectives, and the consequences of filing under each chapter.

For Maryland homeowners, the decision has become particularly important following the substantial increase in the state's residential bankruptcy exemption in 2026. Many individuals who previously considered Chapter 13 necessary to protect home equity may now qualify for Chapter 7 without exposing their residences to liquidation.

1. The Fundamental Difference Between Chapter 7 and Chapter 13

Chapter 7 is primarily a liquidation and discharge proceeding.

A trustee examines the debtor's financial affairs and determines whether nonexempt property can be administered for creditors. In many consumer cases, all meaningful assets are exempt or otherwise unavailable for distribution.

The debtor ordinarily receives a discharge within several months, assuming the statutory requirements are satisfied and no successful objection prevents discharge.

Chapter 13 is a repayment proceeding.

The debtor proposes a plan providing for payments to creditors according to the Bankruptcy Code's requirements.

The debtor generally retains property while making payments through the Chapter 13 trustee.

A Chapter 13 discharge ordinarily occurs after successful completion of the plan and satisfaction of the other statutory requirements.

2. Who Is Eligible for Chapter 7?

Individuals may qualify for Chapter 7 regardless of whether they are employed, unemployed, retired, or receiving disability benefits.

For debtors whose obligations are primarily consumer debts, the means test under 11 U.S.C. § 707(b) may affect whether Chapter 7 relief is appropriate.

The test generally begins with income received during the six complete calendar months preceding the filing month.

That historical income is compared with the applicable median-income threshold.

Above-median debtors may still qualify after allowable deductions and other statutory considerations.

A debtor's income alone does not determine eligibility.

Moreover, individuals whose debts are primarily nonconsumer debts generally are not subject to the ordinary § 707(b) means-test presumption.

3. Who Is Eligible for Chapter 13?

Chapter 13 is available to qualifying individuals with regular income whose debts fall within the statutory eligibility limits.

Under 11 U.S.C. § 109(e), Chapter 13 eligibility depends on the amount of qualifying noncontingent, liquidated debt.

The applicable debt limits are periodically adjusted under § 104.

An individual operating an unincorporated business may qualify, subject to the statutory requirements.

A debtor must also have sufficient income to propose a feasible repayment plan.

Regular income does not necessarily mean traditional wages. Depending on the circumstances, it may include retirement income, business income, rental income, or other sufficiently reliable sources.

A debtor who lacks the ability to fund a feasible plan may be unable to obtain Chapter 13 confirmation even when the debt limits are satisfied.

4. How Long Does Each Chapter Take?

A relatively straightforward Chapter 7 case commonly results in discharge approximately three to four months after filing.

An asset case may remain open longer while the trustee administers property.

Chapter 13 generally involves a repayment plan lasting three to five years.

The applicable commitment period depends on statutory provisions, including income and household-size considerations.

A debtor may obtain valuable protection during Chapter 13, but the discharge ordinarily requires completion of the plan.

This difference matters to individuals who want prompt debt relief and those who need a longer period to resolve secured or priority obligations.

5. What Happens to Property in Chapter 7?

When a Chapter 7 petition is filed, most of the debtor's legal and equitable interests in property become part of the bankruptcy estate under § 541.

The debtor may claim applicable exemptions.

A Chapter 7 trustee may sell nonexempt property when doing so provides a meaningful benefit to creditors.

For example, a debtor who owns valuable investment property or substantial nonexempt vehicle equity may face liquidation risk.

A debtor whose property is fully exempt may have a no-asset case.

The availability of exemptions is therefore central to the Chapter 7 analysis.

6. What Happens to Property in Chapter 13?

Chapter 13 generally permits a debtor to retain property while making payments under a confirmed plan.

However, the debtor cannot necessarily retain valuable nonexempt property without providing corresponding value to unsecured creditors.

Under § 1325(a)(4), unsecured creditors generally must receive at least as much through the plan as they would receive in a hypothetical Chapter 7 liquidation.

This is the liquidation-value requirement.

Example

A debtor owns $30,000 in nonexempt property.

In Chapter 7, the trustee might liquidate the property.

In Chapter 13, the debtor may be able to retain it by funding a plan that satisfies the applicable liquidation-value requirement and other confirmation standards.

The debtor must have sufficient income to make the required payments.

Chapter 13 therefore can protect property that might otherwise be sold in Chapter 7.

7. Maryland's New Homestead Exemption Changes the Comparison

Effective June 1, 2026, Maryland increased its bankruptcy residential-property exemption to $125,000 for qualifying owner-occupied residential property.

The increase substantially expanded Chapter 7 protection for homeowners.

Previously, a homeowner with $90,000 in equity might have faced significant liquidation concerns.

Under the new exemption, the same equity may be fully protected, assuming the statutory requirements are satisfied.

This change can eliminate one of the principal reasons a debtor previously would have selected Chapter 13.

However, homeowners with equity exceeding the exemption may still face liquidation risk.

Joint ownership, tenancy by the entirety, liens, and other circumstances can materially affect the calculation.

8. Tenancy by the Entirety and Married Homeowners

Maryland tenancy-by-the-entirety law may provide significant protection for qualifying property owned by married spouses.

Under § 522(b)(3)(B), entireties interests may be exempt to the extent protected from creditor process under applicable nonbankruptcy law.

The protection generally applies against creditors holding claims against only one spouse.

Joint creditors may present a different situation.

In *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985), the Fourth Circuit addressed administration of Maryland entireties property for the benefit of joint creditors.

Divorce also can terminate entireties ownership.

These issues may influence whether Chapter 7 or Chapter 13 provides better protection.

9. Mortgage Arrears: One of Chapter 13's Greatest Advantages

Chapter 7 generally provides temporary foreclosure protection through the automatic stay but does not furnish a multiyear repayment mechanism for curing mortgage arrears.

Chapter 13 may permit a qualifying debtor to cure arrears over the life of the plan while maintaining ongoing mortgage payments.

Example

A homeowner is $30,000 behind on mortgage payments but has resumed stable employment.

The homeowner can afford the regular mortgage payment but cannot immediately pay the arrears.

Chapter 7 may delay foreclosure without resolving the default.

Chapter 13 may permit the homeowner to cure the arrears over time.

For this debtor, Chapter 13 may offer a meaningful advantage even if Chapter 7 is otherwise available.

10. Vehicle Loans and Repossession

Chapter 7 generally permits a debtor to surrender collateral, redeem qualifying personal property, or enter into a valid reaffirmation agreement.

Reaffirmation may preserve personal liability for a debt that otherwise would be discharged.

Chapter 13 can provide additional options for addressing secured vehicle loans through a repayment plan.

In some circumstances, a Chapter 13 plan may modify the treatment of a secured claim based on the collateral's value.

However, § 1325(a)'s special provisions concerning certain recently acquired vehicles and other collateral may restrict this treatment.

The debtor should not assume that every vehicle loan can be reduced to the vehicle's current market value.

11. Credit Cards and Medical Bills

Ordinary unsecured credit card and medical debts generally are dischargeable in Chapter 7.

A qualifying Chapter 7 debtor may eliminate these obligations without making payments through a repayment plan.

In Chapter 13, unsecured creditors may receive partial or full payment depending on disposable income, liquidation value, and other statutory requirements.

At completion of a qualifying plan, remaining dischargeable unsecured balances generally are discharged.

For a debtor with substantial unsecured debt, little nonexempt property, and no need to cure arrears, Chapter 7 may offer a simpler and faster solution.

12. Income Taxes

Some older income taxes may be dischargeable in Chapter 7 when the statutory requirements are satisfied.

Other taxes survive discharge.

Chapter 13 may permit a debtor to pay qualifying priority tax obligations through a repayment plan.

This can be particularly valuable when the debtor owes substantial nondischargeable taxes but cannot pay the entire balance immediately.

However, tax liens and other enforcement rights require separate analysis.

The appropriate chapter depends on the tax years, filing dates, assessments, liens, and the debtor's financial circumstances.

13. Student Loans

Qualifying student loans generally are excepted from discharge in both chapters unless the debtor establishes undue hardship under § 523(a)(8).

Chapter 7 does not automatically eliminate student loans.

Chapter 13 may temporarily prevent certain collection activity while the debtor performs the plan, but the underlying student loan obligation may remain afterward.

Interest and repayment-program issues may also affect the debtor's long-term financial position.

The availability of an undue-hardship adversary proceeding should be considered separately from the choice of chapter.

14. Domestic Support Obligations

Child support, alimony, and other qualifying domestic support obligations generally survive bankruptcy.

Chapter 13 imposes specific requirements concerning domestic support obligations, including payment of qualifying priority claims and compliance with certain ongoing support obligations.

A debtor who is substantially behind on support may face challenges obtaining confirmation or discharge.

Neither chapter should be viewed as a mechanism for eliminating ordinary domestic support obligations.

15. Divorce-Related Property Settlement Debts

Chapter 7 generally does not discharge debts falling within § 523(a)(15), including certain obligations owed to a former spouse arising from divorce or separation.

Chapter 13's discharge provisions may treat some of these non-support obligations differently.

This distinction can make Chapter 13 attractive to a debtor with substantial property settlement obligations.

However, the legal character of the debt must be examined.

A true domestic support obligation generally remains nondischargeable.

16. Lawsuits and Personal Injury Claims

A debtor's pending or potential lawsuit may become property of the bankruptcy estate.

In Chapter 7, the trustee may acquire authority to administer the claim, subject to exemptions and other applicable law.

In Chapter 13, the debtor generally retains a more active role in managing property and claims, although disclosure, court approval, and estate-related requirements may still apply.

Maryland provides important exemption protection for qualifying personal injury compensation.

The debtor should not assume that filing either chapter permits an undisclosed lawsuit to proceed without bankruptcy consequences.

17. Preferential Payments and Fraudulent Transfers

Both chapters require disclosure of specified prepetition transfers.

Chapter 7 trustees may pursue preferential payments and fraudulent transfers under the Bankruptcy Code.

Chapter 13 also presents avoidance and estate-administration issues, although the allocation of avoidance authority and practical consequences can differ.

A debtor who recently repaid a relative, transferred real estate, or disposed of valuable property should not assume that choosing Chapter 13 eliminates every risk.

The transaction must be evaluated under the applicable statutory provisions.

18. The Automatic Stay

Both Chapter 7 and Chapter 13 ordinarily trigger the automatic stay under § 362.

The stay generally prevents many collection actions, including wage garnishments, lawsuits, repossessions, and foreclosure proceedings.

However, exceptions and limitations apply.

Repeat filings may receive reduced protection.

Chapter 13 also provides a codebtor stay under § 1301 for certain consumer obligations, subject to statutory exceptions and relief provisions.

This protection may benefit a nonfiling cosigner in circumstances where Chapter 7 provides no comparable codebtor stay.

19. The Effect on Credit

Both chapters ordinarily appear on consumer credit reports and may affect future borrowing.

Under federal credit reporting law, bankruptcy information may generally be reported for up to ten years, subject to applicable rules.

Credit reporting practices may differ between Chapter 7 and Chapter 13.

But the practical effect on a particular debtor's credit score depends on the debtor's previous credit history, payment record, outstanding obligations, and subsequent financial conduct.

A debtor should not assume that Chapter 13 necessarily produces a better credit outcome merely because creditors receive payments.

20. Attorney's Fees and Overall Cost

Chapter 7 attorney's fees ordinarily must be addressed in a manner consistent with the Bankruptcy Code's treatment of prepetition obligations and professional compensation.

Chapter 13 attorney's fees may, subject to applicable rules and court approval, be paid in part through the repayment plan.

Chapter 13 generally involves greater ongoing administrative obligations and trustee payments.

But comparing only attorney's fees can be misleading.

A debtor who pays more in legal fees through Chapter 13 may nevertheless preserve a home or vehicle that would be lost in Chapter 7.

The appropriate comparison is the overall financial result.

21. What Happens If the Debtor Cannot Complete Chapter 13?

Chapter 13 requires sustained plan performance.

A debtor who loses employment, experiences unexpected expenses, or otherwise cannot maintain payments may face dismissal or conversion.

Depending on the circumstances, modification of the plan may be available.

In limited situations, a hardship discharge may be possible under § 1328(b).

But completion is not guaranteed.

A debtor should not enter Chapter 13 based on an unrealistic budget.

22. Can a Chapter 13 Case Be Converted to Chapter 7?

Under § 1307(a), a debtor generally has a right to convert a Chapter 13 case to Chapter 7, subject to the statutory requirements.

Conversion can have significant consequences for estate property, exemptions, secured debts, and prior transactions.

The debtor must also be eligible for Chapter 7 relief.

A conversion should not be treated as a routine administrative change without financial consequences.

23. Can a Chapter 7 Case Be Converted to Chapter 13?

Section 706 permits conversion from Chapter 7 to Chapter 13 under specified circumstances.

However, conversion is not always available as a matter of absolute right.

In *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365 (2007), the Supreme Court addressed the consequences of bad-faith conduct in connection with conversion.

A debtor who files Chapter 7 without adequate planning should not assume that conversion will always cure the problem.

24. Comparing Chapter 7 and Chapter 13

Issue	Chapter 7	Chapter 13

Issue	Chapter 7	Chapter 13
Typical duration	Several months to discharge	Generally 3–5 years
Repayment plan	Ordinarily none	Required
Nonexempt property	May be liquidated	Generally retained subject to plan requirements
Mortgage arrears	No ordinary long-term cure mechanism	May be cured through plan
Unsecured debts	Generally discharged without plan payments	Paid according to plan, with qualifying balance discharged
Secured vehicle loans	Reaffirmation, redemption, surrender, or other lawful arrangements	Plan treatment may be available
Priority taxes	Generally survive if nondischargeable	Generally must receive required plan treatment
Domestic support	Generally nondischargeable	Generally nondischargeable, with additional plan requirements
Codebtor protection	Generally no Chapter 7 codebtor stay	Limited consumer codebtor stay
Discharge timing	Ordinarily early in case	Generally after plan completion
Risk of plan failure	Not applicable	Significant consideration

25. Why the Best Choice Depends on the Debtor's Objectives

Consider three debtors.

The first has $75,000 in credit card debt, modest income, and fully exempt property. Chapter 7 may provide relatively prompt relief without a repayment plan.

The second has similar unsecured debt but is $35,000 behind on mortgage payments and has stable income. Chapter 13 may provide the better mechanism for preserving the home.

The third owns substantial nonexempt property but lacks enough income to fund a feasible Chapter 13 plan. Neither chapter may accomplish every desired objective, and alternatives may need to be considered.

The amount of unsecured debt alone does not determine the appropriate chapter.

The analysis must consider property, income, secured obligations, dischargeability, and the debtor's realistic ability to comply with the chosen procedure.

Conclusion

Chapter 7 and Chapter 13 offer different paths to bankruptcy relief.

Chapter 7 ordinarily provides a faster discharge and avoids a multiyear repayment plan, but nonexempt property may be liquidated.

Chapter 13 generally permits debtors to retain property, cure certain arrears, and manage qualifying obligations through a repayment plan, but requires sustained financial performance.

Maryland's increased residential exemption has made Chapter 7 a more attractive option for many homeowners who previously faced substantial equity-related risks.

Nevertheless, Chapter 13 remains particularly valuable for debtors seeking to prevent foreclosure, retain nonexempt property, or address obligations requiring structured repayment.

The appropriate chapter is the one that best protects the debtor's property, resolves the debts that can be addressed, and provides a realistic path to financial stability.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 109 — Eligibility for bankruptcy relief.
- 11 U.S.C. § 362 — Automatic stay.
- 11 U.S.C. § 522 — Exemptions.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 706 — Conversion from Chapter 7.

Federal statutes (continued)

- 11 U.S.C. § 707 — Chapter 7 dismissal and abuse provisions.
- 11 U.S.C. § 727 — Chapter 7 discharge.
- 11 U.S.C. § 1301 — Chapter 13 codebtor stay.
- 11 U.S.C. § 1307 — Conversion or dismissal of Chapter 13 cases.
- 11 U.S.C. § 1322 — Contents of Chapter 13 repayment plans.
- 11 U.S.C. § 1325 — Chapter 13 plan confirmation requirements.
- 11 U.S.C. § 1328 — Chapter 13 discharge.

Maryland law

- Maryland Code, Courts and Judicial Proceedings § 11-504 — Maryland property exemptions, including the expanded residential-property exemption.
- Maryland Senate Bill 939, Chapter 400 (2026) — Legislation increasing the qualifying residential-property exemption to $125,000.

Selected decisions

- *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985) — Addresses tenancy-by-the-entirety property and joint creditors.

- *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365 (2007) — Addresses bad faith and conversion from Chapter 7 to Chapter 13.
- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Addresses projected disposable income and known or virtually certain financial changes in Chapter 13.
- *Ransom v. FIA Card Services, N.A.*, 562 U.S. 61 (2011) — Addresses vehicle ownership expense deductions under the means-test framework.
- *Harris v. Viegelahn*, 575 U.S. 510 (2015) — Addresses undistributed postpetition wages after conversion from Chapter 13 to Chapter 7.
- *Schwab v. Reilly*, 560 U.S. 770 (2010) — Explains the scope of exemption claims.
- *Law v. Siegel*, 571 U.S. 415 (2014) — Limits equitable interference with statutory exemption protections.
- *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010) — Addresses student loan treatment and procedural requirements in Chapter 13 confirmation.

The Chapter 7 Bankruptcy Timeline: From the Initial Consultation Through Discharge and Case Closing

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By Alan J. Belsky, Attorney at Law

What Happens After You Decide to File Chapter 7 Bankruptcy?

Most routine Chapter 7 bankruptcy cases proceed from filing to discharge in approximately three to four months. But the process begins well before the petition is filed, and receiving a discharge does not necessarily mean the bankruptcy case is closed.

The period before filing may be the most important part of the entire proceeding.

During that time, the debtor's attorney must evaluate eligibility, identify assets that could be liquidated, determine which debts can be discharged, investigate recent financial transactions, and ensure that the petition accurately describes the debtor's financial circumstances.

Once the case is filed, federal law establishes deadlines for the meeting of creditors, required financial education, objections to discharge, and other proceedings.

Although the timetable is relatively predictable in an uncomplicated case, a missing document, undisclosed asset, disputed exemption, or creditor objection can substantially delay the process.

Understanding the sequence helps debtors know what to expect and why careful preparation matters.

1. The Initial Bankruptcy Consultation

The process ordinarily begins with a review of the debtor's financial circumstances.

The attorney should identify the debtor's income, household composition, assets, secured and unsecured debts, judgments, pending collection proceedings, and prior bankruptcy filings.

The analysis should also consider whether Chapter 7 is preferable to Chapter 13 or another available alternative.

A debtor may qualify financially for Chapter 7 but own nonexempt property that a trustee could sell.

Conversely, a debtor with substantial earnings may nevertheless qualify for Chapter 7 because of allowable deductions, household circumstances, or the nature of the debts.

The initial consultation should identify potential problems before the debtor incurs the consequences of filing.

2. Determining Whether Chapter 7 Is Appropriate

Chapter 7 eligibility involves more than the means test.

For debtors whose obligations are primarily consumer debts, the means test under 11 U.S.C. § 707(b) may determine whether a presumption of abuse arises.

But the attorney must also evaluate property exemptions, dischargeability, recent transfers, and the debtor's objectives.

For Maryland homeowners, the increased $125,000 residential-property exemption effective June 1, 2026, can materially change the analysis.

A homeowner previously advised that Chapter 7 was too risky because of home equity may now have substantially greater protection.

The correct decision should be based on the debtor's complete circumstances rather than income alone.

3. Gathering Financial Documents

Preparing a bankruptcy petition requires detailed financial information.

Documents commonly needed include tax returns, pay statements, bank statements, mortgage information, vehicle loan records, retirement account statements, insurance information, and documentation of significant assets.

Additional records may be necessary when the debtor operates a business, owns real estate, has pending litigation, or has made substantial transfers.

The attorney should also obtain information concerning lawsuits, judgments, wage garnishments, and collection activity.

The debtor must disclose assets and obligations even when they are disputed, jointly owned, or believed to be exempt.

4. Credit Counseling Before Filing

Under 11 U.S.C. § 109(h), most individual debtors must receive approved credit counseling during the 180 days preceding the bankruptcy filing.

The counseling must be provided by an agency approved for the relevant judicial district.

Limited statutory exceptions and accommodations may apply.

The counseling requirement is separate from the postpetition financial management course.

A debtor should not assume that completing one course satisfies both requirements.

Failure to satisfy the prepetition counseling requirement can create eligibility problems and may result in dismissal.

5. Preparing the Petition, Schedules, and Statements

A Chapter 7 filing ordinarily includes the voluntary petition, schedules of assets and liabilities, income and expenses, statement of financial affairs, statement of intention concerning certain secured debts, and other required documents.

The means-test forms must also be completed when applicable.

The debtor signs the filings under penalty of perjury.

The schedules must identify all required property interests, not merely property the debtor believes the trustee might sell.

Potential personal injury claims, tax refunds, business interests, inheritances, and other rights may require disclosure.

The accuracy of the documents is essential because the trustee will examine them and question the debtor under oath.

6. Choosing the Filing Date

The date of filing can materially affect the outcome.

The means test ordinarily uses income received during the six complete calendar months preceding the filing month.

Exemptions and property interests generally are determined by reference to the petition date, subject to applicable law.

The filing date also determines the ordinary ninety-day preference period.

Certain income taxes may become dischargeable only after statutory waiting periods expire.

A filing that occurs too early or too late may therefore produce substantially different results.

The timing should be selected after evaluating all relevant considerations.

7. Filing the Bankruptcy Petition

The bankruptcy case begins when the petition is filed with the appropriate United States Bankruptcy Court.

Maryland bankruptcy cases are filed in the United States Bankruptcy Court for the District of Maryland, subject to federal venue requirements.

The court assigns a case number, and a Chapter 7 trustee ordinarily is appointed through the applicable administrative process.

The filing creates the bankruptcy estate under § 541.

It also ordinarily triggers the automatic stay under § 362, subject to statutory exceptions and limitations.

The debtor does not need to wait for the meeting of creditors or discharge before the stay takes effect.

8. The Automatic Stay Begins

The automatic stay generally prohibits many collection activities concerning prepetition debts.

These include most collection lawsuits, wage garnishments, judgment enforcement, repossessions, and foreclosure proceedings.

However, the stay is not absolute.

Certain domestic relations, criminal, tax, and governmental regulatory activities may continue.

Creditors may seek relief from the stay.

Repeat bankruptcy filings may also receive limited or no automatic-stay protection.

A debtor facing imminent collection should ensure that the appropriate creditor, attorney, employer, or other participant receives prompt notice.

9. What Happens to Wage Garnishments?

A bankruptcy filing ordinarily stops further wage garnishment to collect an ordinary prepetition unsecured judgment while the stay applies.

However, the employer and garnishing creditor may need prompt notice to ensure that withholding ceases.

Money already garnished presents a separate issue.

Under §§ 522(h) and 547, a debtor may, in specified circumstances, recover qualifying preferential transfers when the trustee does not pursue them.

The amount and timing of the garnishments matter.

A debtor should preserve pay statements and garnishment records so counsel can evaluate whether a recovery action is available.

10. The Trustee's Appointment and Initial Review

The Chapter 7 trustee examines the debtor's schedules, financial affairs, assets, and recent transactions.

The trustee may request tax returns, bank statements, pay records, deeds, vehicle titles, or other documents.

The trustee's principal duties appear in § 704.

The trustee is not the debtor's attorney and does not represent the debtor personally.

The trustee's responsibility is to administer the bankruptcy estate according to law.

In many consumer cases, the trustee determines that there is no nonexempt property available for meaningful distribution.

These are commonly called no-asset cases.

11. The Meeting of Creditors

Under 11 U.S.C. § 341, the debtor ordinarily must attend a meeting of creditors.

Federal Rule of Bankruptcy Procedure 2003 generally requires the meeting in a Chapter 7 case to be scheduled between 21 and 40 days after the order for relief, subject to specified exceptions.

The trustee conducts the examination under oath. The bankruptcy judge does not attend.

Creditors may participate, but in many routine consumer cases, none appear.

The trustee typically verifies the debtor's identity and asks questions concerning the petition, schedules, assets, debts, income, expenses, and recent transactions.

A straightforward meeting may take only a few minutes, but the debtor should not regard it as a formality.

12. What Happens If the Trustee Continues the Meeting?

The trustee may continue the meeting when additional information or documents are needed.

For example, the trustee may request further bank statements, clarification concerning a property transfer, or evidence supporting an exemption.

A continued meeting does not necessarily mean the debtor has done anything wrong.

However, failure to cooperate may lead to additional investigation, a motion to compel, dismissal, or other appropriate relief.

The debtor should provide requested information promptly and remain available for further examination.

13. The Statement of Intention and Secured Property

An individual Chapter 7 debtor whose schedules include debts secured by property of the estate ordinarily must comply with the statement-of-intention requirements of § 521(a)(2). Separate provisions impose additional consequences for specified personal-property collateral.

The debtor generally identifies whether the collateral will be surrendered, redeemed, reaffirmed, or otherwise treated as permitted by law.

The statement generally must be filed within thirty days after the petition or by the first date set for the meeting of creditors, whichever occurs earlier, unless extended.

Section 521(a)(2)(B) ordinarily requires performance within 30 days after the first date set for the meeting of creditors, unless timely extended for cause. Section 521(a)(6) separately addresses specified allowed purchase-price claims secured by personal property and generally uses 45 days after the first meeting; the provisions should not be conflated.

Failure to comply may affect the automatic stay and the debtor's ability to retain collateral.

These deadlines are particularly important for financed automobiles.

14. Reaffirmation Agreements

A debtor who wishes to retain secured property may consider reaffirmation.

Under § 524(c), a valid reaffirmation agreement can preserve personal liability for a debt that otherwise would be discharged.

The agreement generally must be made before discharge and satisfy statutory disclosure, filing, and approval requirements.

Reaffirmation should not be treated as a routine administrative document.

A debtor who reaffirms an automobile loan may remain liable for a deficiency if the vehicle is later repossessed and sold.

The debtor should consider the vehicle's value, loan balance, payment affordability, and available alternatives before signing.

15. The Postpetition Financial Management Course

Most individual Chapter 7 debtors must complete an approved course in personal financial management before receiving a discharge.

This requirement is separate from the credit counseling completed before filing.

Under Rule 1007(b)(7) and (c)(4), the debtor generally must file the provider's certificate of completion within 60 days after the first date set for the meeting of creditors, unless the approved provider has notified the court of completion, the requirement does not apply, or the court extends the time. Confirm that the court has received the required certificate or provider notification.

Failure to complete the requirement can prevent discharge and may result in the case being closed without one.

16. Deadlines for Objections to Discharge

Under Federal Rule of Bankruptcy Procedure 4004(a), a complaint objecting to a Chapter 7 discharge generally must be filed within sixty days after the first date set for the meeting of creditors.

The deadline is measured from the first scheduled meeting date, not necessarily the date on which a continued meeting is concluded.

A trustee, creditor, or other authorized party may object when statutory grounds exist.

Such grounds may include fraudulent concealment, false oaths, inadequate financial records, or other conduct described in § 727.

An objection to the debtor's entire discharge is different from an objection concerning one particular debt.

17. Deadlines for Challenging Particular Debts

Under Rule 4007(c), complaints seeking determinations of nondischargeability under § 523(c)—principally specified fraud, fiduciary misconduct, and willful and malicious injury—generally must be filed within 60 days after the first date set for the meeting of creditors.

Other categories of nondischargeable debts are not necessarily governed by that deadline.

For example, qualifying student loan obligations, domestic support obligations, and certain taxes may survive discharge without a creditor filing a complaint within the ordinary sixty-day period.

The absence of a creditor objection therefore does not guarantee that every debt will be discharged.

18. When Is the Discharge Entered?

In an uncomplicated Chapter 7 case, the bankruptcy court ordinarily enters the discharge after the applicable objection periods expire, provided the debtor has satisfied the requirements for discharge and no legal impediment remains.

This commonly occurs approximately three to four months after filing.

The discharge eliminates personal liability for qualifying debts and creates the protections of the discharge injunction under § 524.

The discharge order does not necessarily identify every debt that survives.

Nor does it automatically eliminate valid liens.

A mortgage or automobile lender may retain enforceable rights against collateral even though the debtor's personal liability has been discharged.

19. Discharge Is Not the Same as Case Closing

This distinction is frequently overlooked.

A debtor may receive a discharge while the Chapter 7 trustee continues administering property.

For example, the trustee may be awaiting a tax refund, selling real estate, prosecuting an avoidance action, or resolving claims against the estate.

The debtor's discharge does not automatically terminate the trustee's authority over estate property.

A case generally closes when administration is complete and the court enters the appropriate closing order.

In a routine no-asset case, closing may follow discharge relatively promptly.

In an asset case, administration can continue for months or even years.

20. What Happens in an Asset Case?

If the trustee identifies nonexempt property, the case may become an asset case.

The trustee may collect and liquidate property, investigate claims, resolve disputes, and distribute proceeds to creditors.

Creditors may be required to file proofs of claim within the applicable deadline.

The trustee's administration may involve sales, settlements, objections, and other proceedings.

The debtor may receive a discharge before those matters conclude.

The existence of an asset case does not necessarily mean the debtor has engaged in misconduct.

It means that property is available for administration under the Bankruptcy Code.

21. What Can Delay the Discharge?

Several circumstances can delay entry of the discharge.

Missing financial management certification, unresolved objections, pending motions concerning abuse, certain reaffirmation issues, or other statutory impediments may prevent entry.

A debtor who fails to cooperate with the trustee or comply with court orders may face additional consequences.

Some delays are administrative. Others involve substantive legal disputes.

The appropriate response depends on the reason for the delay.

22. What Can Cause the Case to Be Dismissed?

A Chapter 7 case may be dismissed for cause under § 707(a), subject to the statutory requirements.

Examples can include unreasonable delay prejudicial to creditors, nonpayment of required fees, or other legally sufficient grounds.

Cases involving primarily consumer debts may also be subject to dismissal or conversion for abuse under § 707(b).

Failure to satisfy applicable credit counseling requirements may create separate eligibility problems.

Dismissal generally differs from discharge.

When a case is dismissed without discharge, the debtor ordinarily remains personally liable for debts that would otherwise have been discharged.

The automatic stay also generally terminates upon dismissal, subject to applicable provisions.

23. What Happens If the Debtor Receives an Inheritance After Filing?

Under § 541(a)(5), certain interests acquired or becoming available within 180 days after the petition may become property of the bankruptcy estate.

These include specified interests arising through inheritance, divorce-related property settlements, and life insurance or death benefit arrangements.

A debtor who becomes entitled to such property should promptly notify bankruptcy counsel.

The fact that the debtor has already attended the meeting of creditors or received a discharge does not necessarily eliminate the estate's rights.

24. What If the Debtor Discovers an Error After Filing?

Errors and omissions should be addressed promptly.

The debtor may need to amend schedules, provide additional documents, or explain the circumstances to the trustee.

A genuine mistake does not automatically constitute fraud.

However, intentional concealment, false statements, or failure to correct material inaccuracies can create serious problems.

The debtor should not wait for the trustee to discover an omission.

Complete and accurate disclosure remains important throughout the case.

25. Can a Closed Bankruptcy Case Be Reopened?

Under § 350(b), a bankruptcy court may reopen a case to administer assets, provide relief to the debtor, or for other cause.

Reopening does not automatically reinstate the automatic stay or change the discharge.

A case may be reopened to administer previously undisclosed property, address certain lien issues, or resolve other matters.

Property that was not properly scheduled may remain property of the estate despite the closing of the case.

The debtor should not assume that case closing eliminates every possible bankruptcy consequence.

26. A Typical Chapter 7 Timeline

The following is an illustrative schedule for a routine individual Chapter 7 case. Actual dates are determined by the court, applicable rules, and circumstances of the case.

Stage	Approximate timing
Initial consultation and document collection	Before filing
Required credit counseling	Within 180 days before filing
Petition and schedules filed	Day 0
Automatic stay ordinarily begins	Upon filing
Trustee document review	First several weeks
Meeting of creditors	Generally days 21–40
Statement of intention	Generally by day 30 or first meeting date, whichever is earlier
Financial management certification	Generally within 60 days after first meeting date
Ordinary discharge-objection deadline	60 days after first meeting date
Discharge in routine case	Often months 3–4
Case closing	After estate administration is complete

The discharge and objection deadlines are generally tied to the first date set for the meeting of creditors, not the date a continued meeting eventually concludes.

27. Why the Work Before Filing Matters Most

The formal Chapter 7 process may last only a few months, but the legal consequences of filing can extend far beyond that period.

A filing date may determine whether a tax debt is dischargeable, whether garnished wages can be recovered, whether home equity is exempt, or whether a recent payment to a relative can be avoided.

Once the petition is filed, the debtor generally cannot undo the creation of the bankruptcy estate simply by deciding that filing was a mistake.

A debtor should therefore complete the necessary investigation before filing whenever circumstances permit.

Emergency filings may sometimes be necessary, but urgency does not eliminate the importance of identifying substantial risks.

Conclusion

A routine Chapter 7 bankruptcy case follows a relatively predictable sequence, beginning with financial preparation and continuing through filing, trustee examination, discharge, and closing.

The automatic stay ordinarily provides immediate protection against many collection activities. The meeting of creditors allows the trustee to investigate the debtor's financial affairs. The discharge generally eliminates personal liability for qualifying debts.

But the process is not complete merely because the meeting has concluded or the discharge has been entered.

The trustee may continue administering estate property, and certain debts and liens may survive.

The most effective Chapter 7 cases are prepared carefully before filing, documented accurately, and managed through every required deadline until administration is complete.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 109 — Bankruptcy eligibility and credit counseling.
- 11 U.S.C. § 341 — Meeting of creditors.
- 11 U.S.C. § 343 — Debtor examination.
- 11 U.S.C. § 362 — Automatic stay.
- 11 U.S.C. § 521 — Debtor duties and required documents.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 704 — Chapter 7 trustee duties.
- 11 U.S.C. § 707 — Dismissal and abuse.
- 11 U.S.C. § 727 — Chapter 7 discharge.
- 11 U.S.C. § 350 — Closing and reopening bankruptcy cases.

Federal Rules of Bankruptcy Procedure

- Rule 1007 — Required schedules, statements, and documents.
- Rule 2003 — Meeting of creditors.
- Rule 4004 — Granting or denying discharge.
- Rule 4007 — Determining dischargeability.
- Rule 4008 — Reaffirmation agreements.

Selected decisions

- *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992) — Explains the importance of timely exemption objections.
- *Schwab v. Reilly*, 560 U.S. 770 (2010) — Addresses the scope of claimed exemptions.
- *Law v. Siegel*, 571 U.S. 415 (2014) — Limits bankruptcy courts' authority to override statutory exemptions.
- *City of Chicago v. Fulton*, 592 U.S. 154 (2021) — Addresses retention of property seized before bankruptcy.
- *Taggart v. Lorenzen*, 587 U.S. 554 (2019) — Establishes the contempt standard for violating the discharge injunction.
- *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365 (2007) — Addresses bad faith and conversion between bankruptcy chapters.

Bankruptcy Discharge Versus Case Closing: Why Your Bankruptcy May Continue After Your Debts Are Eliminated

Belsky Bankruptcy Legal Library | Chapter 7 Procedure and Discharge

By Alan J. Belsky, Attorney at Law

Your Debts May Be Discharged While Your Bankruptcy Case Remains Open

One of the most misunderstood aspects of Chapter 7 bankruptcy is the distinction between receiving a discharge and having the bankruptcy case closed.

These events are not the same.

A discharge ordinarily eliminates the debtor's personal liability for qualifying debts. Case closing is an administrative and judicial event reflecting the completion of bankruptcy estate administration.

In a routine no-asset Chapter 7 case, the two events may occur relatively close together.

But when the trustee is administering property, investigating claims, or pursuing litigation, the case may remain open for months or even years after the debtor receives a discharge.

The distinction matters because the trustee may retain authority over estate property even after the debtor is no longer personally liable for most prepetition debts.

A debtor who receives a discharge should not assume that every financial matter connected with the bankruptcy has ended.

1. What Is a Chapter 7 Discharge?

Under 11 U.S.C. § 727, an eligible Chapter 7 debtor ordinarily receives a discharge of qualifying prepetition debts.

The discharge is implemented through a court order.

Under § 524(a), the discharge generally operates as an injunction against attempts to collect discharged debts as personal liabilities.

A creditor whose debt has been discharged ordinarily cannot continue collection calls, file a lawsuit to recover the discharged personal obligation, garnish wages, or pursue other prohibited collection remedies.

The discharge does not necessarily eliminate valid liens or debts excepted from discharge.

For example, a mortgage lender may retain foreclosure rights even though the debtor's personal liability on the mortgage note has been discharged.

2. What Does It Mean for a Bankruptcy Case to Be Closed?

Under § 350(a), the bankruptcy court closes a case after the estate has been fully administered and the trustee has been discharged.

Closing the case ordinarily reflects completion of the estate administration process.

The trustee may have investigated assets, resolved claims, distributed proceeds, or determined that no property was available for administration.

The closing order does not itself create the discharge.

Nor does it necessarily determine whether every debt was dischargeable.

A debtor may have a closed case without having received a discharge.

3. Can a Debtor Receive a Discharge Before the Case Closes?

Yes.

This is common in Chapter 7 asset cases.

The debtor may satisfy the requirements for discharge while the trustee continues administering estate property.

For example, the trustee may be selling real estate, collecting a tax refund, resolving a lawsuit, or pursuing a preference recovery action.

The debtor's discharge may be entered before those matters conclude.

The trustee's continuing administration ordinarily concerns property of the estate and creditors' rights, rather than the debtor's discharged personal liability.

4. What Is a No-Asset Case?

A no-asset case is one in which the trustee determines that no property is available for meaningful distribution to unsecured creditors.

The debtor may own substantial property, but it may be exempt, fully encumbered, excluded from the estate, or otherwise not economically worthwhile to administer.

In a routine no-asset case, the trustee ordinarily files a report indicating that there are no assets to distribute.

The discharge may then be followed relatively promptly by case closing, assuming no other matters remain.

But a no-asset designation is not necessarily permanent.

If additional property is discovered, the case may require further administration.

5. What Is an Asset Case?

An asset case involves property that the trustee can administer for the benefit of creditors.

The trustee may collect, liquidate, settle, or otherwise realize value from estate property.

Examples include nonexempt real estate equity, valuable vehicles, tax refunds, business interests, and legal claims.

The trustee may also recover preferential payments or fraudulent transfers.

Administration can require notice to creditors, litigation, claim review, and distribution of proceeds.

These activities may continue long after the debtor's discharge.

6. Does the Trustee Still Control Property After Discharge?

Potentially, yes.

Under § 541, property interests belonging to the debtor at the commencement of the case generally become property of the bankruptcy estate.

The discharge does not automatically return all estate property to the debtor.

The trustee may retain authority over property that remains in the estate until it is administered, exempted, abandoned, or otherwise removed from estate administration.

For example, a pending personal injury claim may remain under the trustee's control even after the debtor receives a discharge.

The debtor should not assume that discharge restores unrestricted authority to sell, settle, or transfer estate property.

7. What Happens to a Tax Refund After Discharge?

A tax refund attributable to prepetition earnings or payments may constitute property of the bankruptcy estate.

The trustee may request the debtor's tax return after filing and determine whether any portion of the refund is available for creditors.

For example, a debtor who files in October may later receive a refund relating partly to income earned before the petition.

The fact that the refund arrives after discharge does not necessarily remove it from the estate.

The debtor should consult counsel before spending a refund that may be subject to administration.

8. What Happens to a Pending Personal Injury Claim?

A personal injury claim existing when the bankruptcy petition is filed generally becomes property of the estate, subject to exemptions and other applicable law.

The trustee may acquire authority to prosecute, settle, or abandon the claim.

Maryland provides significant exemption protection for qualifying personal injury compensation.

However, the availability and extent of protection depend on the nature of the recovery and applicable statutory provisions.

A debtor who receives a discharge while the claim remains pending should not assume that the debtor alone controls settlement.

The trustee's rights must be resolved.

9. What If the Debtor Receives an Inheritance After Filing?

Under § 541(a)(5), certain property interests acquired or becoming available within 180 days after filing may enter the bankruptcy estate.

These include specified interests arising through inheritance, divorce-related property settlements, and life insurance or death benefit arrangements.

The debtor should promptly disclose such developments.

The fact that the discharge has already been entered does not necessarily eliminate the trustee's rights.

The relevant inquiry concerns the statutory timing and nature of the property interest.

10. What Happens to Property the Trustee Abandons?

Under § 554, a trustee may abandon property that is burdensome to the estate or of inconsequential value and benefit.

Abandonment generally removes the property from estate administration.

For example, a trustee may abandon a vehicle when liens, exemptions, and sale expenses leave no meaningful value for creditors.

The debtor may then retain the property subject to any surviving liens and other applicable rights.

Abandonment is not the same as exemption.

Exemption protects qualifying property interests under applicable law, while abandonment reflects the estate's decision or statutory consequence that property will not be administered.

11. Scheduled Property May Be Abandoned When the Case Closes

Section 554(c) generally provides that scheduled property not otherwise administered at the time of closing is abandoned to the debtor, unless the court orders otherwise.

This is sometimes called technical abandonment.

The statutory requirements matter.

Property must have been properly scheduled, and the court may order a different result.

A debtor should not assume that merely mentioning an asset informally to the trustee necessarily satisfies the scheduling requirement.

Accurate disclosure in the bankruptcy schedules is important.

12. Undisclosed Property May Remain in the Estate

Section 554(d) generally provides that property not abandoned or administered remains property of the estate.

This can create serious consequences when a debtor fails to disclose an asset.

For example, a debtor may omit a pending lawsuit from the schedules, receive a discharge, and have the case closed.

The debtor may later attempt to pursue or settle the lawsuit.

Because the claim was not properly scheduled and abandoned, it may remain property of the bankruptcy estate.

The trustee may retain authority over the claim even though the case has been closed.

13. Can a Closed Case Be Reopened?

Yes.

Under § 350(b), a bankruptcy court may reopen a case to administer assets, provide relief to the debtor, or for other cause.

Reopening is not the same as filing a new bankruptcy case.

It permits further proceedings in the existing case.

A case may be reopened when previously undisclosed property is discovered, additional administration is necessary, or other legally sufficient grounds exist.

Reopening does not automatically reinstate the automatic stay.

Nor does it automatically change the discharge.

14. What Happens When an Undisclosed Lawsuit Is Discovered?

An undisclosed lawsuit can create problems extending beyond the bankruptcy proceeding.

The trustee may seek to reopen the case and administer the claim.

The debtor's standing to pursue the lawsuit may be questioned.

The defendant may also raise judicial estoppel arguments based on the debtor's failure to disclose the claim.

The consequences depend on the circumstances, including the debtor's knowledge, conduct, the status of the bankruptcy case, and applicable law.

A debtor should disclose potential legal claims even when their value is uncertain.

15. Does Reopening Automatically Restore the Debtor's Rights?

No.

Reopening permits the bankruptcy court to address matters requiring further administration or relief.

It does not automatically determine ownership, exemptions, dischargeability, or the merits of an underlying claim.

For example, reopening a case to administer an undisclosed asset does not necessarily establish that the debtor may retain the asset.

The trustee and other parties may have rights requiring judicial determination.

16. Can the Trustee Pursue Preference Actions After Discharge?

Yes, subject to applicable limitations and procedural requirements.

A trustee may pursue qualifying preferential transfers under § 547 even after the debtor receives a discharge.

The relevant limitation periods appear in § 546(a).

The trustee's avoidance powers concern recovery of estate value for creditors.

They are separate from the debtor's discharge of personal liability.

A debtor should therefore understand that the trustee may continue investigating and litigating prepetition transactions after discharge.

17. Can the Trustee Pursue Fraudulent Transfers After Discharge?

Yes.

A trustee may pursue qualifying fraudulent-transfer claims under §§ 544 and 548, subject to statutory requirements and limitations.

The trustee may seek recovery under § 550.

These actions may involve transfers made to relatives, business associates, or other recipients before bankruptcy.

The debtor's discharge does not automatically terminate the trustee's avoidance powers.

18. Does Discharge Protect the Debtor From Every Creditor?

No.

Certain debts are excepted from discharge under § 523.

Examples include qualifying domestic support obligations, certain taxes, specified student loans absent undue hardship, and debts arising from particular forms of misconduct.

Valid liens may also survive.

The discharge injunction protects against collection of discharged personal liabilities, not every possible creditor action.

A debtor should distinguish between a creditor enforcing a surviving lien and attempting to collect a discharged debt personally.

19. What Happens When a Creditor Violates the Discharge Injunction?

Section 524(a) generally prohibits attempts to collect discharged debts as personal liabilities.

A creditor that violates the discharge injunction may face enforcement proceedings.

In *Taggart v. Lorenzen*, 587 U.S. 554 (2019), the Supreme Court held that civil contempt may be appropriate when there is no fair ground of doubt as to whether the discharge order prohibited the creditor's conduct.

A debtor should preserve collection letters, account statements, and other evidence of prohibited collection activity.

The debtor may need to seek relief from the bankruptcy court.

20. Can a Debtor Obtain Relief After the Case Closes?

In appropriate circumstances, yes.

A debtor may seek to reopen a case to pursue relief that requires bankruptcy court action.

Examples may include certain lien-avoidance proceedings, discharge-enforcement matters, or other legally appropriate requests.

However, reopening is not automatic, and the debtor must establish a sufficient basis.

The availability of relief may also depend on statutory deadlines, prejudice, and other considerations.

21. What If the Debtor Never Received a Discharge?

A bankruptcy case can close without discharge.

For example, a debtor may fail to complete the required financial management course or satisfy another discharge requirement.

The case may then close without the debtor receiving the principal benefit of Chapter 7.

In some circumstances, the debtor may seek to reopen the case and address the missing requirement.

But reopening does not guarantee that discharge will be granted.

The debtor should confirm that an actual discharge order was entered rather than assuming that case closing means the debts were eliminated.

22. How Can a Debtor Confirm the Status of the Case?

The bankruptcy court's docket identifies whether a discharge order has been entered and whether the case has been closed.

The debtor may also receive copies of the discharge and closing notices.

These documents serve different purposes.

A discharge order establishes the relief granted under § 727 and § 524.

A final decree or closing entry reflects completion of administration.

A debtor should retain both records.

23. Why the Distinction Matters in Practice

Consider three situations.

A debtor receives a discharge while the trustee continues pursuing a preference recovery. The debtor's ordinary unsecured debts may be discharged, but the estate remains open.

Another debtor receives a discharge and later learns that an undisclosed personal injury claim remains property of the estate. The case may be reopened for administration.

A third debtor completes a no-asset case, receives a discharge, and has the case closed shortly afterward. For that debtor, the two events occur close together but remain legally distinct.

These examples demonstrate why discharge and closing should not be treated as interchangeable.

Conclusion

A Chapter 7 discharge ordinarily eliminates personal liability for qualifying debts.

Case closing reflects completion of bankruptcy estate administration.

The debtor may receive a discharge while the trustee continues collecting property, prosecuting claims, or distributing proceeds.

Undisclosed property may remain in the estate even after closing, and the bankruptcy court may reopen a case when appropriate.

Receiving a discharge means that qualifying debts have been eliminated. It does not necessarily mean that every property issue, trustee investigation, or bankruptcy-related proceeding has ended.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 350 — Closing and reopening bankruptcy cases.
- 11 U.S.C. § 524 — Effect of discharge.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 554 — Abandonment of estate property.
- 11 U.S.C. § 547 — Preferential transfers.
- 11 U.S.C. § 548 — Fraudulent transfers.
- 11 U.S.C. § 727 — Chapter 7 discharge.
- Federal Rule of Bankruptcy Procedure 5010 — Reopening cases.

Selected decisions

- *Taggart v. Lorenzen*, 587 U.S. 554 (2019) — Addresses contempt for violating the discharge injunction.
- *Schwab v. Reilly*, 560 U.S. 770 (2010) — Addresses exemption claims and property interests.
- *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992) — Addresses exemption objections.
- *Parker v. Wendy's International, Inc.*, 365 F.3d 1268 (11th Cir. 2004) — Discusses undisclosed claims and bankruptcy estate ownership.

- In re Hamlett, 304 B.R. 737 (Bankr. M.D.N.C. 2003) — Addresses reopening and an undisclosed personal-injury claim remaining estate property under § 554(d). Its older equitable exemption-denial discussion must be read subject to Law v. Siegel, 571 U.S. 415 (2014).
- *In re Kestell*, 99 F.3d 146 (4th Cir. 1996) — Discusses bankruptcy abuse and debtor conduct.

Bankruptcy and Personal Injury Claims in Maryland: Who Controls the Lawsuit, Who Receives the Settlement, and What Must Be Disclosed?

Belsky Bankruptcy Legal Library | Bankruptcy, Litigation, and Property Exemptions

By Alan J. Belsky, Attorney at Law

A Personal Injury Claim Can Become Part of the Bankruptcy Estate

A person injured in an automobile accident, medical malpractice incident, workplace occurrence, or other event may have a valuable claim for damages. If that person files bankruptcy, the claim may become property of the bankruptcy estate—even if no lawsuit has been filed, no settlement offer has been made, and the debtor does not yet know how much the claim is worth.

This can create serious complications.

A Chapter 7 trustee may acquire authority to prosecute or settle the claim. The debtor's personal injury attorney may need bankruptcy court approval to continue representing the estate. Settlement proceeds may be subject to exemptions, liens, attorney's fees, and other claims.

Failure to disclose the personal injury claim can create problems in both proceedings.

Maryland law provides significant exemption protection for qualifying personal injury compensation, but the protection does not eliminate the debtor's duty to disclose the claim or automatically resolve every question concerning ownership and control.

The proper coordination of bankruptcy and personal injury representation is therefore essential.

1. When Does a Personal Injury Claim Become Property of the Bankruptcy Estate?

Under 11 U.S.C. § 541(a)(1), the bankruptcy estate generally includes the debtor's legal and equitable interests in property as of the commencement of the case.

A cause of action is a property interest.

Consequently, a personal injury claim arising before the bankruptcy petition ordinarily becomes property of the estate, even if the debtor has not filed suit.

The relevant inquiry generally concerns when the claim arose under applicable law, not merely when a lawsuit was filed or a settlement was reached.

For example, a debtor injured in an automobile collision six months before filing Chapter 7 may possess an estate asset even though the claim remains under investigation.

The debtor must disclose the claim in the bankruptcy schedules.

2. What If the Injury Occurred Before Bankruptcy but Was Discovered Later?

The timing of an injury claim can be more complicated when the debtor does not discover the injury or its cause until after bankruptcy.

Maryland law governs important questions concerning when a cause of action accrues.

However, accrual for limitations purposes and the existence of a property interest under § 541 are not necessarily identical questions.

A claim based on prepetition conduct may belong to the bankruptcy estate even when the debtor did not appreciate its existence at filing.

The analysis may require examining the underlying tort law, the timing of the injury, and the debtor's rights when the petition was filed.

A debtor who discovers a potentially valuable claim after filing should promptly consult bankruptcy counsel.

3. What If the Accident Happens After Bankruptcy Is Filed?

In an ordinary Chapter 7 case, a personal injury claim arising entirely after the petition generally does not become estate property merely because the bankruptcy case remains open.

However, the characterization of the claim depends on when the relevant property interest arose and whether it derives from estate property.

Chapter 13 presents different issues because § 1306 expands the estate to include certain property acquired after filing and before the case is closed, dismissed, or converted.

A debtor should not assume that the treatment of a postpetition injury claim is identical under Chapters 7 and 13.

4. Who Controls the Personal Injury Lawsuit in Chapter 7?

When a prepetition claim becomes property of the Chapter 7 estate, the trustee generally becomes the representative of the estate under § 323.

The trustee ordinarily has authority to determine whether the claim should be pursued, settled, sold, or abandoned.

The debtor may remain an important witness and may have an exemption interest in the recovery.

But the debtor does not necessarily retain exclusive authority to direct litigation or approve settlement.

The trustee's control must be considered before counsel files suit, negotiates settlement, or distributes proceeds.

5. What Happens to the Personal Injury Attorney?

An attorney retained before bankruptcy may not automatically continue representing the bankruptcy estate.

Under § 327, a trustee may employ attorneys and other professionals with court approval, subject to statutory requirements.

Compensation may be governed by §§ 328 and 330 and the applicable Bankruptcy Rules.

The attorney's prepetition contingent-fee agreement does not necessarily establish the terms on which the attorney may represent the estate after filing.

The trustee may seek to employ existing counsel, retain different counsel, or pursue another appropriate arrangement.

The personal injury attorney should coordinate with bankruptcy counsel promptly upon learning of the filing.

6. Does the Trustee Have to Pursue the Claim?

No.

The trustee must evaluate whether pursuing the claim is likely to benefit the estate.

Relevant considerations include liability, causation, damages, insurance coverage, litigation expenses, attorney's fees, liens, exemptions, and the likely net recovery.

A claim may have substantial gross settlement value but produce little or no nonexempt value for creditors.

The trustee may determine that administration is not economically worthwhile.

In appropriate circumstances, the trustee may abandon the claim under § 554.

Abandonment and exemption are distinct concepts, however, and the debtor should not assume that the trustee's lack of immediate action constitutes abandonment.

7. Maryland's Personal Injury Exemption

Maryland Courts and Judicial Proceedings Article § 11-504(b)(2) provides important protection for certain money payable in the event of sickness, accident, injury, or death.

The statute includes qualifying compensation for loss of future earnings and contains limitations concerning certain categories of recovery.

Unlike some Maryland exemptions, this provision is not expressed as a simple fixed-dollar maximum.

The Fourth Circuit addressed the exemption in *In re Butcher*, 125 F.3d 238 (4th Cir. 1997).

The court upheld the application of Maryland's exemption for personal injury compensation against the constitutional challenge presented.

The absence of a fixed dollar ceiling does not mean that every payment associated with a lawsuit is automatically exempt.

The nature of the damages matters.

Section 11-504(i) makes 25% of the debtor’s net recovery on a personal injury claim or qualifying workers’ compensation indemnity claim subject to execution on a judgment for child support arrearages. Net recovery is calculated after attorney’s fees, expenses, medical bills, and the specified liens or subrogation claims. Exemption from ordinary judgment execution also does not itself extinguish valid medical, governmental, or contractual reimbursement interests.

8. Are Pain and Suffering Damages Exempt?

Compensation for bodily injury, including qualifying noneconomic damages, may fall within Maryland's personal injury exemption.

The legal characterization of the recovery is important.

A settlement may compensate the claimant for physical injury, pain and suffering, lost earnings, medical expenses, or other losses.

Some categories may receive different exemption treatment.

The debtor should not assume that a settlement's total amount determines the exemption without considering what the payment represents.

9. What About Lost Wages and Future Earnings?

Maryland's statutory language expressly addresses certain compensation for loss of future earnings.

The treatment of past lost earnings, wage replacement, and other economic damages may require separate analysis.

A personal injury recovery should not automatically be classified as entirely exempt merely because some portion compensates for bodily injury.

The underlying claim, settlement documents, and applicable case law may be relevant.

The debtor's attorney should consider these distinctions when negotiating and documenting a settlement.

10. Property Damage Claims Are Different

A personal injury lawsuit may include claims for damage to an automobile or other property.

Maryland's personal injury exemption does not necessarily protect property damage compensation in the same manner as bodily injury damages.

For example, an automobile accident settlement may include compensation for physical injuries and reimbursement for damage to the vehicle.

Those components may require separate exemption analysis.

The debtor may have other available exemptions for the property damage portion, but the personal injury exemption should not automatically be applied to every category.

11. Punitive Damages and Other Noncompensatory Recoveries

Punitive damages serve a different purpose from compensatory damages.

They are intended to punish and deter certain misconduct rather than compensate the injured person for a particular loss.

Whether punitive damages qualify for an exemption requires separate statutory analysis.

A settlement or judgment that includes punitive damages may therefore present additional bankruptcy issues.

The same caution applies to contractual damages, statutory penalties, and other noncompensatory awards included in litigation arising from an injury.

12. Can the Trustee Settle the Claim Without the Debtor's Consent?

When the claim belongs to the estate, the trustee generally possesses authority to propose settlement.

Compromises involving estate claims ordinarily require compliance with Federal Rule of Bankruptcy Procedure 9019 and applicable notice and approval procedures.

The debtor may have an interest in the settlement, particularly where exempt proceeds or other personal rights are involved.

But the debtor does not necessarily possess an absolute veto over the trustee's administration of an estate claim.

The bankruptcy court may need to determine whether a proposed settlement is appropriate under the applicable standards.

13. Who Receives the Settlement Proceeds?

Settlement proceeds may be subject to several competing interests.

These can include attorney's fees, litigation expenses, valid liens, medical reimbursement claims, exemption rights, and the bankruptcy estate's interest.

The allocation depends on the nature of the recovery and applicable law.

The trustee may be required to distribute nonexempt proceeds according to the Bankruptcy Code.

The debtor ordinarily is entitled to property or proceeds properly exempted.

The personal injury attorney should not disburse settlement proceeds without resolving the bankruptcy estate's rights.

14. What About Medical Liens and Reimbursement Claims?

Personal injury recoveries may be subject to claims asserted by healthcare providers, insurers, government programs, or other entities.

Examples can include Medicare, Medicaid, ERISA plan reimbursement claims, workers' compensation liens, and other legally recognized interests.

The validity, priority, and enforceability of those claims require separate analysis.

The bankruptcy discharge does not necessarily eliminate every lien or reimbursement right associated with a personal injury recovery.

The trustee and personal injury attorney may need to coordinate resolution of these obligations.

15. What If the Claim Is Fully Exempt?

A debtor may possess a personal injury claim whose proceeds are fully protected under Maryland law.

Nevertheless, the claim generally must be disclosed.

The debtor must properly claim the exemption, and interested parties may have objection rights.

The trustee may need sufficient information to determine whether the exemption applies to the entire claim.

If the claim is fully exempted or properly abandoned, the debtor may regain control of the claim, subject to applicable law.

The precise effect depends on the exemption claimed, the scope of any objection, and the relevant court orders.

16. What If the Claim Is Only Partially Exempt?

A claim may contain both exempt and nonexempt components.

For example, a settlement may include qualifying personal injury compensation and separate property damage or other nonexempt recovery.

The trustee may seek to administer the nonexempt portion.

Disputes can arise concerning allocation of damages, valuation, and the extent of the exemption.

The settlement documents may be relevant evidence, but labels selected by the parties do not necessarily control the bankruptcy characterization.

17. What Happens If the Claim Was Not Disclosed?

Failure to disclose a personal injury claim can create serious problems.

The claim may remain property of the bankruptcy estate even after discharge and case closing.

The trustee may seek to reopen the case and administer the asset.

The debtor may face questions concerning standing to pursue the lawsuit.

The defendant may also assert judicial estoppel based on inconsistent positions taken in bankruptcy and subsequent litigation.

The consequences depend on the facts and governing law.

An omission should be corrected promptly rather than concealed.

18. Judicial Estoppel and Undisclosed Claims

Judicial estoppel is an equitable doctrine intended to protect the integrity of judicial proceedings.

In the bankruptcy context, defendants sometimes argue that a plaintiff who failed to disclose a claim in bankruptcy should be prevented from pursuing it afterward.

The doctrine is not necessarily applied automatically whenever a claim was omitted.

Courts consider the relevant circumstances, including the debtor's knowledge, conduct, and whether the positions were genuinely inconsistent.

The trustee's rights may also differ from those of the debtor.

In *Parker v. Wendy's International, Inc.*, 365 F.3d 1268 (11th Cir. 2004), the court distinguished the bankruptcy trustee's ability to pursue an undisclosed claim from the debtor's conduct.

Maryland and Fourth Circuit authority must be considered when evaluating judicial estoppel in a particular case.

19. Can the Bankruptcy Case Be Reopened?

Under § 350(b), a bankruptcy court may reopen a case to administer assets, provide relief to the debtor, or for other cause.

A previously undisclosed personal injury claim may provide grounds for reopening.

Reopening does not automatically establish that the debtor owns the claim or may retain the proceeds.

The trustee may need to determine whether the claim should be administered or abandoned.

The debtor may also need to amend the schedules and claim applicable exemptions.

20. What If the Personal Injury Case Settles Before Bankruptcy?

A settlement reached before filing may create several different property interests.

The debtor may possess settlement proceeds, an enforceable right to receive payment, or funds held in an attorney's trust account.

The bankruptcy treatment depends on the circumstances and applicable law.

A debtor should not assume that settlement funds become exempt merely because they originated from a personal injury claim.

The nature of the compensation, ownership of the funds, applicable exemptions, and any valid liens must be examined.

21. What If the Debtor Spends the Settlement Before Filing?

Spending settlement proceeds before bankruptcy may affect the assets remaining on the petition date.

But the debtor must disclose specified prepetition transfers and financial transactions.

Payments to creditors may raise preference issues.

Transfers to relatives or transactions for inadequate consideration may raise fraudulent-transfer concerns.

The debtor should not attempt to dispose of settlement proceeds merely to prevent the trustee from administering them.

Legitimate ordinary living expenses and other transactions require separate analysis.

22. What If the Debtor Files Chapter 13?

Chapter 13 differs from Chapter 7.

Under § 1306, the Chapter 13 estate generally includes certain property acquired after filing and before the case is closed, dismissed, or converted.

A personal injury claim arising during Chapter 13 may therefore become estate property.

The debtor may retain possession of estate property under § 1306(b), but disclosure and court approval requirements may apply.

Settlement proceeds may affect the repayment plan, projected disposable income, or other plan obligations.

A Chapter 13 debtor should not assume that a postpetition injury claim is entirely outside bankruptcy.

23. What If the Injured Person Is a Minor?

A minor's personal injury recovery may involve additional protections under Maryland law.

Maryland Courts and Judicial Proceedings Article § 13-402 and related provisions govern certain payments and property held for minors.

The minor's claim ordinarily belongs to the minor, not automatically to a parent who files bankruptcy.

However, parents may possess separate claims or interests arising from an injury, depending on applicable law.

The ownership of each claim must be identified.

A parent's bankruptcy should not automatically be assumed to place the child's independent recovery into the parent's bankruptcy estate.

24. What If the Debtor Dies While the Claim Is Pending?

Death may affect the underlying personal injury claim, the parties authorized to prosecute it, and the bankruptcy estate's interests.

Maryland law distinguishes survival actions from wrongful death claims.

A survival claim generally concerns rights belonging to the injured person or estate.

A wrongful death claim belongs to the statutory beneficiaries under applicable Maryland law.

The bankruptcy treatment depends on the ownership of the particular claim and the timing of the relevant events.

The trustee's rights in a prepetition survival claim may differ from the rights of wrongful death beneficiaries.

25. Why Bankruptcy Counsel and Personal Injury Counsel Must Communicate

Bankruptcy and personal injury proceedings should not be handled independently when the debtor has a pending or potential claim.

The bankruptcy attorney must understand the claim's nature, estimated value, and exemption issues.

The personal injury attorney must understand whether the trustee controls the claim, whether court approval is required, and how settlement proceeds may be distributed.

Failure to coordinate can result in unauthorized settlements, improper disbursements, standing disputes, or loss of valuable rights.

The safest approach is to identify the claim before filing and establish the appropriate litigation and exemption strategy.

Conclusion

A personal injury claim can be a valuable asset in bankruptcy.

When the claim arose before a Chapter 7 filing, it generally becomes property of the bankruptcy estate, even if no lawsuit has been filed or settlement reached.

Maryland law provides significant exemption protection for qualifying personal injury compensation, but the exemption does not eliminate the duty to disclose the claim.

The trustee may possess authority to prosecute or settle estate claims, and undisclosed claims may remain estate property after discharge and closing.

A debtor with a pending or potential personal injury claim should coordinate bankruptcy planning with personal injury representation before filing, whenever possible.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 323 — Trustee as representative of the estate.
- 11 U.S.C. § 327 — Employment of professional persons.
- 11 U.S.C. § 328 — Terms and conditions of professional employment.
- 11 U.S.C. § 330 — Compensation of officers and professionals.
- 11 U.S.C. § 350 — Closing and reopening cases.
- 11 U.S.C. § 522 — Exemptions.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 554 — Abandonment.
- 11 U.S.C. § 1306 — Chapter 13 estate property.
- Federal Rule of Bankruptcy Procedure 9019 — Compromises and settlements.

Maryland law

- Maryland Courts and Judicial Proceedings § 11-504(b)(2) — Exemption for qualifying personal injury compensation.
- Maryland Courts and Judicial Proceedings § 13-402 — Certain payments and property held for minors.

Selected decisions

- *In re Butcher*, 125 F.3d 238 (4th Cir. 1997) — Addresses Maryland's personal injury compensation exemption.
- *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992) — Addresses the consequences of failing to object timely to claimed exemptions.
- *Schwab v. Reilly*, 560 U.S. 770 (2010) — Explains the distinction between exempting a specified value and an entire property interest.
- *Parker v. Wendy's International, Inc.*, 365 F.3d 1268 (11th Cir. 2004) — Distinguishes the bankruptcy trustee's authority to pursue an undisclosed employment claim from the debtor's conduct for judicial estoppel purposes.
- *Cannon-Stokes v. Potter*, 453 F.3d 446 (7th Cir. 2006) — Addresses judicial estoppel when a debtor fails to disclose a legal claim in bankruptcy and later attempts to pursue it.
- *Jethroe v. Omnova Solutions, Inc.*, 412 F.3d 598 (5th Cir. 2005) — Examines judicial estoppel arising from nondisclosure of a claim in bankruptcy.
- *In re Coastal Plains, Inc.*, 179 F.3d 197 (5th Cir. 1999) — Discusses the duty to disclose contingent and unliquidated claims and the application of judicial estoppel.
- *In re Butcher*, 189 B.R. 357 (Bankr. D. Md. 1995), aff'd, 125 F.3d 238 (4th Cir. 1997) — Addresses Maryland's exemption for qualifying personal injury compensation.

How Long Does Bankruptcy Affect You? Credit Reports, Mortgage Eligibility, Financing, Employment, and Other Long-Term Consequences

BELSKY BANKRUPTCY LEGAL LIBRARY | LIFE AFTER BANKRUPTCY

By Alan J. Belsky, Attorney at Law

Bankruptcy Does Not Create a Ten-Year Financial Disability

One of the most common reasons people hesitate to file bankruptcy is the belief that doing so will prevent them from obtaining credit, buying a home, financing an automobile, or otherwise functioning financially for the next ten years.

That belief confuses two very different concepts: how long a bankruptcy may appear on a credit report and how long it actually affects a person's financial opportunities.

Federal law generally permits a bankruptcy filing to remain on a consumer credit report for up to ten years. But there is no general federal law prohibiting someone from obtaining credit, purchasing real estate, or financing a vehicle throughout that period.

Indeed, some individuals become better credit risks after bankruptcy because substantial unsecured obligations have been eliminated.

Bankruptcy can have lasting consequences. Those consequences, however, vary considerably depending on the debtor's financial circumstances, the chapter filed, the type of credit sought, and the lender's underwriting requirements.

The appropriate question is not simply how long bankruptcy remains visible. It is how the bankruptcy affects particular financial decisions and what can be done to improve the debtor's position afterward.

1. How Long Does Bankruptcy Remain on a Credit Report?

The Fair Credit Reporting Act, 15 U.S.C. § 1681c(a)(1), generally permits consumer reporting agencies to report bankruptcy cases for up to ten years from the date of entry of the order for relief or adjudication.

For an ordinary voluntary bankruptcy case, the filing date generally serves as the relevant starting point.

A Chapter 7 bankruptcy may therefore appear for up to ten years.

Although federal law permits the same maximum period for Chapter 13, major consumer reporting agencies have traditionally removed completed Chapter 13 bankruptcies after approximately seven years under their reporting practices.

That shorter period is generally a reporting-agency policy rather than a separate statutory maximum for Chapter 13.

The distinction is important: a bankruptcy's continued appearance on a credit report does not mean the debtor remains in bankruptcy or is prohibited from borrowing.

2. Does Bankruptcy Ruin Your Credit for Ten Years?

No. A bankruptcy may negatively affect credit scores, but the impact is not necessarily constant throughout the reporting period.

Credit scoring models consider numerous factors, including payment history, outstanding balances, utilization, length of credit history, and recent credit activity.

The effect of bankruptcy also depends on the debtor's credit history before filing.

A person with an excellent payment record may experience a substantial immediate decline.

A debtor whose credit report already reflects numerous delinquent accounts, collection proceedings, judgments, and charged-off debts may experience a different result.

Over time, the effect of the bankruptcy may diminish as the debtor establishes a record of responsible financial conduct.

There is no universal timetable for credit-score recovery.

3. Why Credit May Improve After Bankruptcy

Bankruptcy can eliminate substantial unsecured debt.

For example, a debtor who owes $85,000 on credit cards may be using nearly all available revolving credit and making payments that barely cover interest.

After Chapter 7, the debtor may no longer owe those discharged balances personally.

This can improve the debtor's debt-to-income position and ability to meet current obligations.

However, discharged accounts do not necessarily disappear from the credit report. They may continue to be reported with an appropriate indication that they were included in bankruptcy and with accurate balances and historical information.

A discharge does not erase the debtor's prior credit history.

It changes the legal enforceability of the discharged obligations.

4. Can You Obtain a Credit Card After Chapter 7?

Yes.

There is no general statutory waiting period prohibiting a person from obtaining a credit card after Chapter 7 discharge.

Whether a lender approves an application depends on its underwriting criteria.

Some lenders offer secured credit cards or other products designed for consumers rebuilding credit.

Others may decline applications because of the bankruptcy or require a period of satisfactory postbankruptcy credit history.

A debtor should be cautious about high fees, excessive interest rates, and products marketed as guaranteed credit repair.

Obtaining new credit is not necessarily beneficial if it recreates the financial problems that led to bankruptcy.

5. Can You Finance an Automobile After Bankruptcy?

Yes.

Automobile financing may be available relatively soon after Chapter 7 discharge, and sometimes while a bankruptcy case is pending, depending on the lender and circumstances.

There is no general ten-year prohibition.

However, lenders may charge higher interest rates, require larger down payments, or impose other underwriting conditions.

The debtor should compare the total cost of financing rather than focusing solely on the monthly payment.

A loan with a long repayment period and high interest rate may make an automobile substantially more expensive than its purchase price suggests.

For some debtors, retaining a reliable existing vehicle through an appropriate bankruptcy arrangement may be preferable to financing a replacement.

6. Can You Buy a Home After Bankruptcy?

Yes.

Bankruptcy does not permanently disqualify a person from obtaining a mortgage.

However, mortgage eligibility depends heavily on the loan program, the type of bankruptcy, the date of discharge or dismissal, the borrower's credit history, and any applicable exceptions.

Government-backed mortgage programs and conventional lenders may apply different waiting periods.

The waiting period is ordinarily measured from a specified bankruptcy event, such as discharge or dismissal, rather than from the date the bankruptcy disappears from the credit report.

A borrower may therefore qualify for a mortgage while the bankruptcy remains visible.

7. Mortgage Waiting Periods: FHA, Conventional, and Other Loans

Mortgage programs have different eligibility requirements. The following are important examples, not guarantees of loan approval.

Mortgage program	General bankruptcy waiting period
FHA, after Chapter 7	Generally 2 years after discharge
FHA, during Chapter 13	Potentially after 12 months of satisfactory plan

Mortgage program	General bankruptcy waiting period
	payments, with required approvals
Fannie Mae conventional, after Chapter 7	Generally 4 years after discharge or dismissal
Fannie Mae conventional, after Chapter 13 discharge	Generally 2 years
Fannie Mae conventional, after Chapter 13 dismissal	Generally 4 years

FHA guidelines recognize exceptions for certain documented extenuating circumstances. Fannie Mae also permits shorter periods in specified circumstances.

Under HUD Handbook 4000.1, II.A.5.a.iii(H), the ordinary Chapter 7 period is measured to FHA case-number assignment: at least two years after discharge, with good credit reestablished or no new credit obligations during the most recent two years. A documented exception may permit at least 12 months where circumstances beyond the borrower's control caused the bankruptcy and responsible financial management has been demonstrated. For an ongoing Chapter 13, at least 12 months of the payout period must have elapsed at case-number assignment; all required payments during the most recent 12 months must have been made on time, and the borrower must have written bankruptcy-court permission for the mortgage transaction.

These are program requirements, not universal federal restrictions on obtaining a mortgage. Individual lenders may impose additional conditions.

Fannie Mae separately generally requires five years from the most recent discharge or dismissal when there was more than one bankruptcy filing within the previous seven years. Its documented-extenuating-circumstances exception may reduce that period to three years when the most recent filing resulted from those circumstances. This separate rule can override an assumption based solely on the table's single-case examples.

A borrower also must satisfy ordinary underwriting standards concerning income, employment, debt-to-income ratio, credit history, down payment, and property eligibility.

8. Bankruptcy and Foreclosure May Create Separate Waiting Periods

A debtor who loses a home through foreclosure may face different mortgage eligibility rules from a debtor who files bankruptcy but retains the residence.

For conventional financing, foreclosure may trigger a longer waiting period than bankruptcy alone.

When a mortgage debt was discharged in bankruptcy and foreclosure occurred later, the applicable Fannie Mae rules may permit use of the bankruptcy waiting period if the required documentation establishes the relevant facts.

Otherwise, the longer applicable period may govern.

This distinction can be particularly important when foreclosure proceedings continue after a Chapter 7 discharge.

The debtor should preserve the bankruptcy discharge order, mortgage documents, and foreclosure records.

9. Can Bankruptcy Affect Renting an Apartment?

Yes.

Landlords and property management companies may review consumer reports when evaluating rental applications, subject to applicable law.

A bankruptcy may influence their assessment of payment risk.

However, there is no general federal law prohibiting a person from renting housing merely because bankruptcy appears on a credit report.

Some landlords may focus on income, rental history, and whether previous housing obligations were satisfied.

Others may impose stricter credit requirements.

A debtor who has maintained a satisfactory rental history and stable postbankruptcy income may be in a stronger position than the bankruptcy filing alone suggests.

10. Can Bankruptcy Affect Employment?

Bankruptcy law provides important employment protections.

Under 11 U.S.C. § 525(a), governmental units generally may not deny employment, terminate employment, or discriminate with respect to employment solely because of specified bankruptcy-related circumstances.

Section 525(b) prohibits private employers from terminating employment or discriminating with respect to employment against an individual solely on the grounds specified in that provision.

However, the statutory language governing private employers differs from that governing governmental employers.

In *Rea v. Federated Investors*, 627 F.3d 937 (3d Cir. 2010), the court held that § 525(b) did not prohibit a private employer from refusing to hire an applicant solely because of a prior bankruptcy. The distinction has generated litigation and should not be overlooked.

Employment-related credit checks may also be subject to the Fair Credit Reporting Act and applicable state law.

A bankruptcy filing therefore does not automatically prevent employment, but the scope of legal protection depends on the employer and the challenged action.

11. Professional Licenses and Government Benefits

Section 525(a) also protects debtors against certain discriminatory governmental licensing actions.

A governmental unit generally may not deny, revoke, suspend, or refuse to renew a license, permit, charter, franchise, or similar grant solely because of the bankruptcy-related circumstances specified in the statute.

The provision does not eliminate legitimate licensing requirements unrelated to bankruptcy.

For example, professional regulators may retain authority to investigate misconduct, dishonesty, or violations of professional obligations.

A bankruptcy discharge does not automatically erase the underlying conduct that produced a disciplinary concern.

The debtor's profession and the governing licensing rules must be examined.

12. Security Clearances and Financial Background Investigations

A bankruptcy filing may be considered in a financial background investigation, but it does not automatically disqualify a person from holding a security clearance.

Financial difficulties can raise concerns about judgment, reliability, or vulnerability to improper influence.

However, obtaining legal relief through bankruptcy may also demonstrate an effort to resolve financial problems.

The relevant analysis considers the surrounding circumstances, causes of indebtedness, disclosure, subsequent conduct, and applicable clearance standards.

A debtor should provide accurate information rather than attempting to conceal the bankruptcy.

13. Does Bankruptcy Affect Insurance?

Bankruptcy may affect certain insurance underwriting decisions, particularly where insurers are legally permitted to consider credit-based insurance information.

The treatment varies by insurance product and applicable state law.

Maryland regulates the use of credit history and other factors in insurance underwriting and rating.

A bankruptcy should not be assumed to produce an automatic premium increase or loss of coverage.

The debtor should distinguish between the legal effect of bankruptcy and the insurer's otherwise lawful underwriting criteria.

14. Can Bankruptcy Affect a Business Owner?

A business owner who files personal bankruptcy may experience consequences involving financing, personal guarantees, business ownership interests, and commercial relationships.

A Chapter 7 trustee may administer the debtor's nonexempt ownership interest in a corporation or limited liability company.

A bankruptcy filing may also affect access to commercial credit.

However, personal bankruptcy does not automatically dissolve every business owned by the debtor.

The legal structure of the business, ownership agreements, financing arrangements, and nature of the debtor's interests must be examined.

15. Does Bankruptcy Prevent You From Opening a Bank Account?

There is no general federal prohibition against opening a checking or savings account after bankruptcy.

However, financial institutions may apply account-screening policies concerning prior account closures, unpaid overdrafts, suspected fraud, or other banking history.

A debtor who owed money to a particular bank before filing may encounter additional issues concerning account relationships or setoff rights.

The debtor should not assume that bankruptcy prevents ordinary banking activity.

16. Does Bankruptcy Affect Student Loan Eligibility?

Section 525(c) provides specific protections concerning certain government-operated or government-guaranteed student loan programs.

A qualifying educational lender or governmental unit generally may not deny covered student loan assistance solely because of the bankruptcy-related circumstances identified in the statute.

The protection does not eliminate all other eligibility requirements.

Nor does it require every private lender to extend credit.

A debtor seeking educational financing should distinguish covered federal or state student loan programs from ordinary private credit products.

17. Can Bankruptcy Affect a Cosigner?

A Chapter 7 discharge generally eliminates the debtor's qualifying personal liability but does not automatically discharge a nonfiling cosigner's separate obligation.

A lender may continue pursuing the cosigner under applicable law.

For example, a parent who cosigned an automobile loan may remain liable after the child's Chapter 7 discharge.

Chapter 13 provides a limited codebtor stay under § 1301 for certain consumer obligations, subject to exceptions and relief provisions.

The debtor should consider these consequences before filing, particularly when family members have guaranteed substantial debts.

18. How Long Do Discharged Debts Remain on Credit Reports?

A discharged account may remain on a consumer credit report for the applicable reporting period even though the debtor no longer owes the debt personally.

The account should be reported accurately.

A discharged debt should not be reported in a manner that falsely suggests an enforceable outstanding personal balance.

The underlying account's reporting period may differ from the bankruptcy public-record entry's reporting period.

The debtor should review all three major credit reports after discharge and dispute material inaccuracies.

The Fair Credit Reporting Act provides procedures for disputing inaccurate or incomplete information.

19. What If a Creditor Continues Reporting a Balance?

Credit reporting disputes require careful distinction between inaccurate reporting and an actionable violation of the bankruptcy discharge injunction.

The discharge generally eliminates personal liability for qualifying debts.

However, the legal consequences of a particular credit reporting entry depend on its accuracy, context, and the creditor's conduct.

A debtor may dispute inaccurate information with the consumer reporting agency and the furnisher.

In appropriate circumstances, the Fair Credit Reporting Act may provide remedies.

A discharge-injunction claim requires separate analysis under § 524 and governing case law.

Not every credit reporting error automatically constitutes contempt of the discharge order.

20. Can You Rebuild Credit Without Taking on Significant Debt?

Yes.

A debtor does not need to incur substantial new debt merely to establish responsible financial conduct.

Possible steps include maintaining accurate credit reports, paying ongoing obligations on time, keeping bank accounts in good standing, and using modest credit responsibly when appropriate.

A secured credit card may be useful for some debtors, but it is not necessary for everyone.

The debtor should avoid excessive fees and unnecessary borrowing.

The objective should be financial stability rather than achieving a particular credit score as quickly as possible.

21. Why the First Two Years After Discharge Can Matter

The period immediately following discharge can be important because lenders may evaluate whether the debtor has established stable income, maintained current obligations, and avoided new delinquencies.

For some mortgage programs, two years after discharge is a significant eligibility milestone.

But the same period has no universal legal significance for every type of credit.

A debtor may qualify for automobile financing much earlier, while certain conventional mortgage programs require longer waiting periods.

The relevant timetable depends on the specific financial objective.

22. Bankruptcy Does Not Eliminate Every Debt or Lien

A debtor's long-term financial position depends partly on which obligations survive.

Certain taxes, domestic support obligations, student loans, and debts arising from specified misconduct may remain enforceable.

Valid mortgages and other liens may also survive discharge.

A debtor who emerges from bankruptcy with substantial nondischargeable obligations may continue experiencing financial pressure.

The long-term consequences of bankruptcy therefore depend on the actual discharge obtained, not simply the fact that a case was filed.

23. The Difference Between Legal Restrictions and Lender Policies

This distinction should guide any discussion of life after bankruptcy.

A legal restriction is imposed by statute, regulation, or binding legal requirement.

A lender policy is an underwriting condition imposed by a particular creditor or mortgage program.

For example, the Fair Credit Reporting Act permits bankruptcy reporting for a specified period.

It does not require every lender to deny credit throughout that period.

Similarly, mortgage program waiting periods are underwriting requirements rather than general prohibitions against owning a home.

Understanding the source of a restriction helps the debtor determine whether an exception or alternative may be available.

24. When Does Bankruptcy Stop Being a Practical Impediment?

There is no single answer.

For some debtors, bankruptcy may cease to be a significant obstacle within a relatively short period after discharge.

For others, it may affect mortgage eligibility, interest rates, or other financial opportunities for several years.

The consequences depend on the debtor's prebankruptcy history, the chapter filed, the type of financing sought, subsequent payment history, income, assets, and the creditor's requirements.

A bankruptcy filing may remain visible long after its practical significance has diminished.

Conclusion

Bankruptcy can affect credit reports and financial opportunities for years, but it does not impose a universal ten-year prohibition against borrowing, purchasing a home, obtaining employment, or conducting ordinary financial affairs.

Federal law generally permits bankruptcy information to remain on consumer credit reports for up to ten years.

Mortgage programs impose separate waiting periods, many of which are substantially shorter.

Employment and licensing protections also limit certain forms of bankruptcy discrimination.

For many debtors, the elimination of overwhelming unsecured debt can create a foundation for improved financial stability.

The long-term objective of bankruptcy is not merely to eliminate existing debt. It is to place the debtor in a position to rebuild financial security without repeating the circumstances that made bankruptcy necessary.

Related Bankruptcy Cases and Authorities

Federal statutes

- 15 U.S.C. § 1681c — Credit reporting periods and exclusions.
- 15 U.S.C. § 1681i — Disputes concerning inaccurate consumer report information.
- 11 U.S.C. § 525 — Protections against specified discriminatory treatment.
- 11 U.S.C. § 524 — Discharge injunction.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 1301 — Chapter 13 codebtor stay.

Mortgage and consumer guidance

- Fannie Mae Selling Guide — Significant Derogatory Credit Events — Conventional mortgage waiting periods following bankruptcy.
- HUD Single Family Housing Policy Handbook 4000.1 — FHA underwriting standards, including bankruptcy-related eligibility requirements.
- Consumer Financial Protection Bureau — Bankruptcy and Credit Reports — Federal consumer guidance on reporting periods.

Selected decisions

- *Rea v. Federated Investors*, 627 F.3d 937 (3d Cir. 2010) — Addresses the distinction between private-employer hiring decisions and employment discrimination prohibited by § 525(b).
- *Myers v. TooJay's Management Corp.*, 640 F.3d 1278 (11th Cir. 2011) — Addresses § 525(b) and refusal to hire based on bankruptcy.
- *FCC v. NextWave Personal Communications Inc.*, 537 U.S. 293 (2003) — Addresses governmental license cancellation and the protections of § 525(a).
- *Taggart v. Lorenzen*, 587 U.S. 554 (2019) — Establishes the contempt standard for violations of the discharge injunction.

How Soon Can You File Bankruptcy Again? Waiting Periods, Repeat Discharges, and Limitations on the Automatic Stay

Belsky Bankruptcy Legal Library | Bankruptcy Eligibility and Repeat Filings

By Alan J. Belsky, Attorney at Law

Filing Bankruptcy Again Is Not the Same as Qualifying for Another Discharge

A person who previously filed bankruptcy may need relief again because of unemployment, illness, divorce, business failure, or other financial difficulties.

Federal bankruptcy law does not impose a universal prohibition against filing another bankruptcy case.

However, the Bankruptcy Code restricts how frequently an individual may receive a discharge. It also limits automatic-stay protection in certain repeat-filing situations.

These are separate questions.

A debtor may be permitted to file another bankruptcy petition but be ineligible to receive a discharge in the new case.

Similarly, a debtor may be eligible for a new discharge but receive limited protection from foreclosure, repossession, or other collection activity because of recently dismissed cases.

Understanding the differences is essential before filing again.

1. Three Questions Must Be Answered

When evaluating a repeat bankruptcy filing, counsel should determine whether the debtor is eligible to commence the new case, whether the debtor is eligible to receive a discharge, and whether the automatic stay will arise and remain effective.

These questions are governed by different provisions of the Bankruptcy Code.

Eligibility to file is addressed principally through § 109 and other applicable provisions.

Eligibility for a Chapter 7 discharge is governed in part by § 727(a)(8) and (9).

Eligibility for a Chapter 13 discharge is governed in part by § 1328(f).

Repeat-filing restrictions on the automatic stay appear principally in § 362(c)(3) and (4).

A debtor should not assume that satisfying one set of requirements satisfies the others.

2. The Waiting Periods for Another Bankruptcy Discharge

The following table summarizes the ordinary waiting periods between successive discharges.

Previous discharge	New case	Ordinary waiting period

Previous discharge	New case	Ordinary waiting period
Chapter 7	Chapter 7	8 years
Chapter 7	Chapter 13	4 years
Chapter 13	Chapter 7	6 years, subject to statutory exceptions
Chapter 13	Chapter 13	2 years

These periods generally are measured from the filing date of the earlier case to the filing date of the new case—not from the date the earlier discharge was entered.

That distinction can materially affect eligibility.

3. Chapter 7 Followed by Another Chapter 7: Eight Years

Under § 727(a)(8), a debtor generally cannot receive a Chapter 7 discharge if the debtor received a discharge in a Chapter 7 or Chapter 11 case commenced within eight years before the filing of the new Chapter 7 petition.

Example

A debtor files Chapter 7 on March 15, 2020, and receives a discharge several months later.

The ordinary eight-year period is measured from March 15, 2020.

The debtor generally would not be eligible for another Chapter 7 discharge in a case filed before March 15, 2028.

The date of the earlier discharge is not the starting point.

The debtor must still satisfy the other eligibility requirements.

4. Chapter 7 Followed by Chapter 13: Four Years

Under § 1328(f)(1), a debtor generally cannot receive a Chapter 13 discharge if the debtor received a discharge in a Chapter 7, Chapter 11, or Chapter 12 case filed during the four years preceding the new Chapter 13 filing.

A debtor may nevertheless be able to file Chapter 13 before four years have passed.

The absence of discharge eligibility does not necessarily prevent confirmation of a plan in every circumstance.

For example, a debtor who recently completed Chapter 7 may need Chapter 13 to cure mortgage arrears or address other obligations through a repayment plan.

This sequence is sometimes described as a *Chapter 20* strategy.

It is not a separate chapter of the Bankruptcy Code.

The debtor's eligibility, good faith, plan feasibility, and available relief must be examined carefully.

5. Chapter 13 Followed by Chapter 7: Six Years

Under § 727(a)(9), a debtor generally cannot receive a Chapter 7 discharge if the debtor received a discharge in a Chapter 12 or Chapter 13 case commenced within six years before the new Chapter 7 filing.

However, the statute provides important exceptions.

The six-year restriction does not apply when the payments under the earlier plan totaled at least 100% of allowed unsecured claims.

An exception also applies when payments totaled at least 70% of allowed unsecured claims and the plan was proposed in good faith and represented the debtor's best effort.

These exceptions can materially affect the calculation.

Counsel should review the prior confirmed plan, payment history, trustee records, and discharge order rather than assuming that every prior Chapter 13 discharge creates a six-year bar.

6. Chapter 13 Followed by Another Chapter 13: Two Years

Under § 1328(f)(2), a debtor generally cannot receive a Chapter 13 discharge if the debtor received a discharge in a Chapter 13 case filed during the two years preceding the new filing.

Because Chapter 13 plans commonly last three to five years, the two-year restriction may already have expired by the time the debtor completes the earlier case.

Nevertheless, unusual circumstances can make the provision relevant.

The period is measured between petition dates.

7. What If the Earlier Case Was Dismissed Without Discharge?

A dismissal is different from a discharge.

The ordinary two-, four-, six-, and eight-year discharge waiting periods generally depend on a discharge having been received in the earlier case.

A case dismissed without discharge ordinarily does not trigger those particular restrictions.

However, dismissal can create other barriers.

Section 109(g) may impose a 180-day restriction in specified circumstances.

Repeat dismissals can also limit or prevent the automatic stay in a new case.

A debtor should therefore not assume that dismissal means another case can be filed immediately with full protection.

8. The 180-Day Filing Restriction Under § 109(g)

Section 109(g) generally makes an individual ineligible to be a debtor for 180 days after certain dismissals.

The restriction may apply when the prior case was dismissed because of the debtor's willful failure to obey court orders or appear before the court in proper prosecution of the case.

It may also apply when the debtor voluntarily dismissed the case following the filing of a request for relief from the automatic stay.

The statutory language and relevant case law must be examined.

Not every dismissal for failure to file documents automatically establishes the willfulness required under § 109(g)(1).

The reason for dismissal matters.

9. One Dismissed Case Within the Previous Year: The Thirty-Day Rule

Section 362(c)(3) addresses certain debtors who had one bankruptcy case pending and dismissed during the preceding year.

When the provision applies, the automatic stay generally terminates on the thirtieth day after the new filing with respect to the debtor, unless the court extends it.

The statute contains exceptions and qualifications.

Courts have disagreed about whether the termination extends to property of the bankruptcy estate.

That distinction can be critical in foreclosure cases.

A debtor who files again should not assume that the stay will protect every relevant interest for the full duration of the case.

10. Extending the Stay Beyond Thirty Days

Section 362(c)(3)(B) permits a party in interest to request an extension of the automatic stay.

The motion must be filed and heard within the statutory period.

The court must find that the later case was filed in good faith as to the creditors to be stayed.

The statute establishes presumptions of bad faith in specified circumstances.

A debtor seeking an extension should be prepared to explain why the earlier case failed and why the new case is likely to succeed.

For example, a debtor whose earlier Chapter 13 case was dismissed after job loss may have stronger evidence of good faith if the debtor has since obtained stable employment and can fund a feasible plan.

The hearing must be completed before expiration of the thirty-day period.

A motion filed shortly before the deadline may therefore be too late to obtain effective relief.

11. Two or More Dismissed Cases Within the Previous Year: No Automatic Stay

Under § 362(c)(4), when two or more qualifying cases were pending and dismissed during the preceding year, the automatic stay generally does not take effect upon filing the new petition.

This is more severe than the thirty-day limitation.

The debtor may file a new case without receiving the ordinary immediate protection against foreclosure, repossession, or collection.

A party in interest may request an order imposing the stay.

The motion must satisfy the statutory timing and good-faith requirements.

For § 362(c)(4), the request to impose the stay must be made within 30 days after the new case is filed; an order generally becomes effective when entered. That motion deadline differs from § 362(c)(3), which requires completion of the extension hearing before the original 30-day stay expires.

The court may impose the stay after notice and hearing when the required showing is made.

12. Why Repeat Filings Can Be Dangerous Before Foreclosure

A debtor facing an imminent foreclosure may believe that filing another bankruptcy petition will automatically stop the sale.

That assumption can be wrong.

If § 362(c)(4) applies, no automatic stay may arise.

If § 362(c)(3) applies, the stay may terminate after thirty days unless extended.

The effect of the filing also depends on the timing and status of the foreclosure proceeding.

A debtor should not rely on repeated petitions as a substitute for a feasible plan to resolve mortgage arrears.

13. What If the Previous Bankruptcy Was Voluntarily Dismissed?

A voluntary dismissal can have different consequences depending on the circumstances.

Under § 109(g)(2), a debtor who voluntarily dismisses a case following a creditor's request for relief from the automatic stay may face a 180-day eligibility restriction.

The statutory language has generated litigation concerning the required relationship between the stay-relief request and dismissal.

A debtor should not assume that voluntarily dismissing a case eliminates all consequences for future filings.

The procedural history must be reviewed.

14. Does Conversion Count as Another Bankruptcy Filing?

Conversion from one chapter to another generally does not commence a new bankruptcy case.

Under § 348(a), conversion ordinarily does not change the date of the filing of the petition, commencement of the case, or order for relief, except as otherwise provided.

This distinction matters when calculating discharge waiting periods.

For example, a case originally filed under Chapter 13 and later converted to Chapter 7 generally retains the original petition date for the relevant calculation.

The chapter under which the debtor ultimately received a discharge also matters.

The docket and discharge order should be reviewed.

15. What If the Prior Discharge Was Denied?

A debtor whose discharge was denied may face additional restrictions.

Section 523(a)(10) addresses certain debts that were or could have been listed in a prior case in which discharge was waived or denied under specified provisions.

A later bankruptcy does not necessarily eliminate debts that survived because of misconduct in the earlier case.

The consequences depend on the statutory basis for the prior denial.

A debtor should not assume that waiting eight years automatically cures every prior discharge problem.

16. Can a Debtor File Chapter 13 Without Being Eligible for a Discharge?

Potentially, yes.

A debtor who recently received a Chapter 7 discharge may seek Chapter 13 relief to address mortgage arrears, secured obligations, or other debts.

But the debtor must satisfy Chapter 13 eligibility, good faith, feasibility, and confirmation requirements.

The absence of discharge eligibility can affect the benefits available at completion.

A debtor should understand that plan completion may not eliminate remaining personal liability for obligations that otherwise would have been discharged.

17. Repeat Filings and Good Faith

Bankruptcy courts may examine whether a repeat filing represents a legitimate effort to obtain relief or an abusive attempt to delay creditors.

Relevant factors can include the debtor's financial circumstances, reasons for prior dismissals, changes in income, accuracy of disclosures, and feasibility of the proposed plan.

Repeat filing alone does not necessarily establish bad faith.

But a history of unsuccessful cases filed shortly before foreclosure may warrant heightened scrutiny.

The debtor should be prepared to explain what has changed and why the new case is likely to succeed.

18. Why the Prior Bankruptcy Docket Matters

The debtor's recollection of an earlier case may be incomplete.

A person may remember filing Chapter 13 but not recall whether the case was dismissed, converted, or discharged.

The relevant dates may also differ from the debtor's assumptions.

Before filing again, counsel should obtain the prior bankruptcy docket and determine the original petition date, chapter, conversion history, dismissal or discharge date, and reasons for dismissal.

Any prior stay-relief motions should also be reviewed.

The docket may reveal restrictions that materially affect the new case.

19. Can a New Bankruptcy Discharge Old Debts That Survived the Previous Case?

Sometimes, depending on why the debts survived and the applicable statutory provisions.

For example, a debt may have survived because the earlier case was dismissed without discharge.

A later qualifying bankruptcy may discharge that debt.

But debts excepted from discharge under § 523 may remain nondischargeable.

Debts associated with certain prior denials of discharge may also be excepted under § 523(a)(10).

The nature of the debt and the outcome of the earlier case must be examined.

20. Why Filing Eligibility and Discharge Eligibility Must Be Kept Separate

A debtor may be eligible to file Chapter 13 but ineligible for another discharge.

A debtor may be eligible for discharge but subject to a shortened automatic stay.

A debtor may also be temporarily ineligible to file because of § 109(g).

These are different legal consequences.

A careful repeat-filing analysis should identify each restriction separately.

The debtor should not rely on a simplified statement that bankruptcy can be filed only once every seven or eight years.

That statement is incorrect.

Conclusion

Federal bankruptcy law permits repeat filings in appropriate circumstances, but it imposes important restrictions on successive discharges and automatic-stay protection.

The ordinary discharge waiting periods are two, four, six, or eight years, depending on the chapters involved and applicable exceptions.

Those periods generally run from the filing date of the earlier case to the filing date of the new case.

Dismissed cases may create separate restrictions, including a possible 180-day filing bar and limitations on the automatic stay.

Before filing bankruptcy again, the prior case's docket, discharge history, dismissal history, and stay-relief proceedings should be examined.

A repeat filing should be undertaken only after determining what protection and relief the new case can actually provide.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 109(g) — Certain 180-day eligibility restrictions.
- 11 U.S.C. § 348 — Effect of conversion.
- 11 U.S.C. § 362(c)(3)–(4) — Automatic-stay limitations for repeat filings.
- 11 U.S.C. § 523(a)(10) — Certain debts affected by prior denial or waiver of discharge.
- 11 U.S.C. § 727(a)(8)–(9) — Restrictions on successive Chapter 7 discharges.
- 11 U.S.C. § 1328(f) — Restrictions on successive Chapter 13 discharges.

Selected decisions

- *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365 (2007) — Addresses bad faith and conversion between bankruptcy chapters.
- *In re Tomlin*, 105 F.3d 933 (4th Cir. 1997) — Addresses dismissal with prejudice and the effect of prior bankruptcy dismissal orders.
- *In re Dilley*, 125 B.R. 189 (Bankr. N.D. Ohio 1991) — Discusses repeat filings and eligibility restrictions.
- *In re Casse*, 198 F.3d 327 (2d Cir. 1999) — Addresses abusive repeat filings and bankruptcy court authority to impose filing restrictions.
- *In re Jumpp*, 356 B.R. 789 (1st Cir. BAP 2006) — Discusses the scope of stay termination under § 362(c)(3).
- *In re Reswick*, 446 B.R. 362 (9th Cir. BAP 2011) — Addresses the scope of § 362(c)(3)(A) stay termination.

Avoiding Judgment Liens in Bankruptcy: How 11 U.S.C. § 522(f) Can Protect Your Home and Other Exempt Property

Belsky Bankruptcy Legal Library | Bankruptcy Exemptions and Lien Avoidance

By Alan J. Belsky, Attorney at Law

Discharging a Judgment Does Not Necessarily Remove Its Lien

A debtor who files Chapter 7 bankruptcy may receive a discharge eliminating personal liability for a judgment debt, yet discover years later that the judgment still encumbers real estate.

This can create a serious problem when the debtor attempts to sell or refinance the property.

The distinction arises because bankruptcy generally eliminates qualifying personal liabilities without automatically extinguishing valid liens against property.

Fortunately, 11 U.S.C. § 522(f) permits debtors to avoid certain judicial liens that impair exemptions to which they are entitled.

The procedure can be especially valuable for Maryland homeowners following the state's 2026 increase in the bankruptcy residential-property exemption to $125,000.

But lien avoidance is not automatic. The debtor ordinarily must file an appropriate motion, establish the statutory requirements, and obtain an order determining the lien's avoidable extent.

Understanding the difference between discharging a debt and avoiding its lien can prevent significant postbankruptcy difficulties.

1. What Is a Judgment Lien?

A judgment lien is a legal interest in property arising from a court judgment and applicable lien-creation procedures.

In Maryland, a properly recorded or indexed judgment may create a lien against qualifying real property under Maryland Courts and Judicial Proceedings Article § 11-402 and the applicable Maryland Rules.

The precise requirements depend on the court in which the judgment was entered and the location of the property.

Section 11-402 expressly recognizes the medical-debt exception in Real Property § 14-203.1. A judgment therefore should not be assumed to create a lien against a primary residence when that statutory medical-debt protection applies.

A judgment lien can affect the debtor's ability to sell or refinance real estate because a purchaser or lender may require resolution of the lien before closing.

The lien is distinct from the debtor's personal obligation to pay the judgment.

2. What Happens to a Judgment When Chapter 7 Is Filed?

An ordinary unsecured judgment debt generally may be discharged in Chapter 7.

However, discharge of the personal obligation does not necessarily eliminate a valid prepetition judgment lien.

The creditor may retain an in rem interest in property to which the lien properly attached.

For example, a debtor may discharge a $40,000 credit card judgment but remain subject to a judgment lien affecting the debtor's residence.

Unless the lien is avoided, released, satisfied, or otherwise rendered unenforceable, it may create problems when the property is sold or refinanced.

This is why judgment liens should be identified before filing.

3. What Does § 522(f) Permit?

Section 522(f)(1)(A) generally permits a debtor to avoid the fixing of a judicial lien on an interest of the debtor in property to the extent the lien impairs an exemption to which the debtor would have been entitled.

The statute contains exceptions, including specified domestic support obligations.

The debtor must establish that the lien is of a type subject to avoidance, that it fixed on a qualifying property interest, and that it impairs an available exemption.

The statute does not authorize avoidance of every lien.

Its purpose is to protect exemption rights from qualifying judicial liens.

4. Judicial Liens Versus Consensual Liens

The distinction between judicial and consensual liens is fundamental.

A judicial lien generally arises through judgment or other legal process.

A consensual lien ordinarily arises through an agreement granting a security interest, such as a mortgage or automobile loan.

Section 522(f)(1)(A) generally addresses judicial liens, not ordinary consensual mortgages.

A debtor cannot use the judicial-lien avoidance provision merely to eliminate a valid mortgage because the mortgage impairs home equity.

Other Bankruptcy Code provisions may affect secured claims in different circumstances, but they operate under separate requirements.

5. Maryland's New Homestead Exemption Makes Lien Avoidance More Important

Maryland increased its bankruptcy residential-property exemption to $125,000 effective June 1, 2026.

The increased exemption may permit debtors to avoid larger portions of qualifying judicial liens than would have been possible under the former exemption.

The exemption applies to qualifying owner-occupied residential property, subject to statutory requirements.

A debtor who previously had substantial nonexempt equity may now be able to claim greater protection.

However, the applicable exemption amount generally must be determined under the law governing the particular bankruptcy filing.

The increase should not be assumed to apply retroactively to every previously filed case.

6. The Statutory Impairment Formula

Section 522(f)(2)(A) provides a formula for determining whether a lien impairs an exemption.

The calculation generally adds:

- The judicial lien being tested.
- All other liens on the property.
- The exemption the debtor could claim if there were no liens.

The resulting sum is compared with the value of the debtor's interest in the property absent liens.

The amount by which the sum exceeds that value determines the extent of impairment, subject to the statute's limitations.

The formula can produce results that differ from a simple calculation of equity.

7. Example: Complete Avoidance of a Judgment Lien

Assume a qualifying Maryland homeowner has the following circumstances:

Item	Amount
Home value	$400,000
Mortgage balance	$300,000
Judgment lien	$35,000
Available residential exemption	$125,000

The calculation is:

$300,000 mortgage + $35,000 judgment lien + $125,000 exemption = $460,000.

The total exceeds the home's $400,000 value by $60,000.

Because the impairment exceeds the $35,000 judgment lien, the lien may be avoided in full, assuming all other statutory requirements are satisfied.

The result is not simply that the debtor has $100,000 in equity.

The statutory formula determines the extent to which the judicial lien impairs the exemption.

8. Example: Partial Lien Avoidance

Assume the following circumstances:

Item	Amount
Home value	$500,000
Mortgage balance	$300,000
Judgment lien	$100,000
Available exemption	$125,000

The calculation is:

$300,000 + $100,000 + $125,000 = $525,000.

The total exceeds the property's value by $25,000.

Accordingly, the judgment lien may be avoidable to the extent of $25,000.

The remaining $75,000 may continue encumbering the property, subject to the applicable law and court order.

This illustrates why lien avoidance is not necessarily an all-or-nothing remedy.

9. Multiple Judgment Liens

When property is subject to multiple judicial liens, § 522(f)(2)(B) contains special rules concerning the calculation.

The statute prevents double-counting liens already avoided in the calculation.

The order in which liens are analyzed can affect the result.

Counsel should identify every lien, its priority, the underlying judgment, and the relevant recording information.

A debtor should not assume that all judgment liens can be avoided merely because the total amount of judgments exceeds the available equity.

Each lien must be analyzed under the statutory formula.

10. What Property Value Is Used?

The relevant valuation generally concerns the debtor's property interest at the legally applicable time, ordinarily the bankruptcy petition date.

A later increase in real estate value does not necessarily change the historical impairment calculation.

For example, a residence worth $350,000 when bankruptcy was filed may be worth $475,000 several years later.

If lien avoidance is sought after the case closes, the debtor may still need to establish the value applicable at the original bankruptcy filing.

Historical appraisals, tax assessments, real estate records, and other valuation evidence may be relevant.

The debtor should preserve documentation supporting the petition-date value.

11. What If the Property Is Jointly Owned?

Joint ownership can complicate lien avoidance.

Section 522(f) focuses on the debtor's interest in the property.

A debtor who owns an undivided one-half interest as a tenant in common may not be entitled to calculate impairment as though the debtor owned the entire property.

The nature of the ownership interest, the judgment lien's attachment, and the applicable exemption must be examined.

The Fourth Circuit's decision in *In re Opperman*, 943 F.2d 441 (4th Cir. 1991), addressed lien avoidance and property interests under the statutory framework then applicable.

Because § 522(f) was amended after that decision, counsel must distinguish the historical holding from the current statutory formula.

12. Tenancy by the Entirety

Maryland tenancy-by-the-entirety property ordinarily is protected against creditors holding claims against only one spouse.

A judgment against one spouse generally does not attach to qualifying entireties property in the same manner as a judgment against both spouses.

The threshold question may therefore be whether a valid judicial lien attached at all.

If the property was formerly held by the entirety but the spouses later divorced, the ownership structure may have changed.

Divorce ordinarily terminates tenancy-by-the-entirety ownership, potentially creating separate interests as tenants in common.

The timing of the judgment, divorce, bankruptcy filing, and lien attachment must be examined.

13. What If the Judgment Was Entered After Bankruptcy?

A creditor ordinarily cannot create or enforce a judicial lien to collect a discharged personal debt in violation of the discharge injunction.

However, a judgment entered after bankruptcy may concern a nondischargeable obligation or another matter not prohibited by the discharge.

The legal effect depends on the underlying debt, timing, and applicable court orders.

A debtor should not assume that every postbankruptcy judgment is invalid.

Nor should a creditor assume that a prepetition debt remains enforceable merely because a judgment was later entered.

14. Domestic Support Judgment Liens

Section 522(f)(1)(A) excludes certain judicial liens securing debts described in § 523(a)(5).

These are qualifying domestic support obligations.

A debtor generally cannot avoid such a lien under the ordinary judicial-lien provision merely because it impairs an exemption.

The classification of the obligation matters.

A debt arising from a divorce decree is not necessarily a domestic support obligation simply because it is owed to a former spouse.

Property settlement obligations and true support obligations may receive different treatment.

15. Judicial Liens on Personal Property

Section 522(f) is not limited to real estate.

Qualifying judicial liens impairing exemptions in personal property may also be avoidable.

The debtor must identify the property interest, lien, available exemption, and statutory impairment.

Examples may involve vehicles or other personal property subject to judicial liens.

However, not every security interest in personal property is a judicial lien.

The source and nature of the lien must be established.

16. Certain Nonpossessory, Nonpurchase-Money Security Interests

Section 522(f)(1)(B) provides a separate avoidance mechanism for specified nonpossessory, nonpurchase-money security interests in qualifying personal property.

The provision applies only to designated categories, including certain household furnishings, household goods, appliances, clothing, jewelry, tools of the trade, and professionally prescribed health aids.

The statute contains definitions and limitations.

It does not permit avoidance of every consensual lien on personal property.

A purchase-money security interest securing the acquisition of an item ordinarily presents different issues.

17. How Is a Judgment Lien Avoided?

Lien avoidance ordinarily requires a motion filed in the bankruptcy court.

Federal Rule of Bankruptcy Procedure 4003(d) governs proceedings under § 522(f).

The debtor must provide appropriate notice and comply with applicable service requirements.

The motion should identify the judgment creditor, judgment, lien, property, exemption, valuation, and impairment calculation.

Supporting documentation may include the deed, judgment records, mortgage balances, valuation evidence, and Schedule C.

The court may enter an order avoiding the lien to the extent established.

18. Does the Lien Disappear Automatically When the Motion Is Filed?

No.

Filing a motion does not itself establish that the lien has been avoided.

The creditor may object, challenge valuation, dispute exemption eligibility, or raise other legal issues.

The bankruptcy court must determine the requested relief.

A debtor should obtain and preserve the signed order.

Where appropriate, the order should be recorded or otherwise placed in the relevant land records so that title examiners and future lenders can identify its effect.

19. Can a Judgment Lien Be Avoided After Discharge?

Potentially, yes.

A debtor may discover a surviving judgment lien when attempting to sell or refinance property years after receiving a discharge.

The Bankruptcy Code does not establish a universal deadline requiring every § 522(f) motion to be filed before discharge.

However, delay can create procedural and equitable issues.

The debtor may need to reopen the bankruptcy case under § 350(b).

The creditor may raise questions concerning prejudice, valuation, or other circumstances.

The availability of relief depends on applicable law and the particular case.

20. Reopening a Closed Case to Avoid a Lien

Federal Rule of Bankruptcy Procedure 5010 governs reopening bankruptcy cases.

A debtor seeking lien avoidance after closing may file a motion to reopen, followed by or accompanied by the appropriate lien-avoidance request as permitted by local practice.

Reopening does not automatically avoid the lien.

The debtor must still establish the substantive requirements of § 522(f).

A court may consider whether reopening is appropriate and whether the requested relief remains available.

The debtor should not assume that case closing permanently eliminates the opportunity for lien avoidance, but prompt action is generally preferable.

21. Why Lien Avoidance Should Be Addressed During the Bankruptcy

Although post-discharge lien avoidance may be possible, addressing judgment liens during the original bankruptcy case is ordinarily preferable.

The debtor and counsel are more likely to have ready access to the relevant schedules, property valuations, mortgage statements, and judgment records.

The creditor can receive notice while the case is active.

A timely order also reduces the risk of discovering an unresolved lien during a future sale or refinancing.

The debtor should not wait until a real estate closing is imminent to determine whether a judgment lien survived bankruptcy.

22. What If the Judgment Creditor Refuses to Release the Lien?

If the bankruptcy court has entered an effective order avoiding the lien, the debtor may need to take appropriate steps to establish the order's effect in the land records or obtain further relief.

The creditor's obligations depend on the order and applicable law.

A creditor's refusal to comply with a valid court order may require enforcement proceedings.

However, the debtor should distinguish a lien that has actually been avoided from a judgment debt that was merely discharged.

The latter does not necessarily establish that the lien itself is unenforceable.

23. Can a Debtor Avoid a Lien on Property Acquired After Bankruptcy?

Section 522(f) generally concerns liens that fixed on qualifying interests of the debtor in property and impaired exemptions.

A lien affecting property acquired after bankruptcy may present different issues.

The debtor must establish that the statutory requirements apply to the relevant property interest and lien.

A prepetition judgment may also have consequences under state law concerning after-acquired property.

The timing of ownership, attachment, and bankruptcy filing must be analyzed.

Where the underlying personal judgment debt was discharged, § 524(a) must also be applied: a creditor cannot simply use state-law after-acquired-property rules to enforce that discharged personal liability against property newly acquired by the debtor. This differs from enforcement of a valid lien that attached to property before bankruptcy and survived the case.

24. The Importance of Reviewing Maryland Land Records

Before filing bankruptcy, counsel should determine whether judgments have attached to the debtor's real estate.

This may require examination of court judgment records, land records, and title information.

A debtor may be unaware that a judgment has become a lien.

The existence of a judgment in a court docket does not always establish that it has attached to every parcel of real estate.

The applicable Maryland procedures and property location matter.

A complete lien review can identify problems that otherwise might remain undiscovered until a future transaction.

Conclusion

Chapter 7 bankruptcy may discharge the debtor's personal liability for a judgment without automatically eliminating the judgment lien.

Section 522(f) provides an important mechanism for avoiding qualifying judicial liens that impair exemptions.

Maryland's expanded residential-property exemption makes this remedy particularly valuable for homeowners whose equity now falls within the increased protection.

But lien avoidance requires a statutory calculation, appropriate procedure, and an effective court order.

Joint ownership, multiple liens, property valuation, and the timing of the bankruptcy can materially affect the result.

A debtor should not assume that a discharged judgment can no longer interfere with ownership, sale, or refinancing of property. Judgment liens should be identified and addressed as part of comprehensive bankruptcy planning.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 522(f) — Avoidance of qualifying judicial liens and specified security interests.
- 11 U.S.C. § 524 — Effect of discharge.
- 11 U.S.C. § 350 — Reopening bankruptcy cases.
- Federal Rule of Bankruptcy Procedure 4003(d) — Lien avoidance proceedings.
- Federal Rule of Bankruptcy Procedure 5010 — Reopening cases.

Maryland statutes and rules

- Maryland Courts and Judicial Proceedings § 11-402 — Judgment liens on real property.
- Maryland Courts and Judicial Proceedings § 11-504 — Maryland exemptions.
- Maryland Rules 2-621 and 3-621 — Judgment lien procedures, as applicable.

Selected decisions

- *Farrey v. Sanderfoot*, 500 U.S. 291 (1991) — Addresses the requirement that a judicial lien fix on a preexisting interest of the debtor.
- *Owen v. Owen*, 500 U.S. 305 (1991) — Addresses lien avoidance and exemptions under § 522(f).
- *In re Opperman*, 943 F.2d 441 (4th Cir. 1991) — Addresses lien avoidance and exemption impairment under the statutory framework then applicable.

- *In re Brantz*, 106 B.R. 62 (Bankr. E.D. Pa. 1989) — Discusses the calculation of impairment under the pre-1994 statutory framework.
- *In re Chiu*, 304 F.3d 905 (9th Cir. 2002) — Addresses post-sale lien avoidance and the debtor's property interest.
- *In re Wilding*, 475 F.3d 428 (1st Cir. 2007) — Addresses lien avoidance after discharge and case closing.

Denial and Revocation of a Chapter 7 Discharge: When Bankruptcy Relief Can Be Lost

Belsky Bankruptcy Legal Library | Bankruptcy Discharge and Debtor Obligations

By Alan J. Belsky, Attorney at Law

Bankruptcy Relief Is Powerful, but It Is Not Unconditional

The principal benefit of Chapter 7 bankruptcy is the discharge of qualifying debts. A debtor who receives a discharge generally is relieved of personal liability for most ordinary unsecured obligations.

But the Bankruptcy Code imposes duties of honesty, disclosure, record preservation, and cooperation.

A debtor who conceals assets, makes fraudulent statements, destroys financial records, or engages in other specified misconduct may lose the right to a discharge altogether.

The consequences can be severe.

Instead of eliminating substantial unsecured debts, the debtor may emerge from bankruptcy still personally liable for obligations that otherwise would have been discharged.

In some circumstances, a discharge already granted can be revoked.

These remedies are distinct from an objection concerning the dischargeability of one particular debt. Understanding the difference is essential.

1. Denial of Discharge Versus Nondischargeability of a Particular Debt

The Bankruptcy Code distinguishes between denial of the debtor's general discharge under 11 U.S.C. § 727 and exceptions to discharge for particular debts under § 523.

Section 523 generally concerns whether an individual obligation survives bankruptcy.

For example, a creditor may contend that a debt arising from fraud or willful and malicious injury is nondischargeable.

Section 727 addresses whether the debtor should receive a Chapter 7 discharge at all.

A successful § 727 objection can prevent discharge of numerous otherwise dischargeable debts.

This distinction makes § 727 litigation particularly consequential.

2. Who Can Object to Discharge?

Under § 727(c), the trustee, a creditor, or the United States Trustee may object to the debtor's discharge.

The objection ordinarily must be pursued through an adversary proceeding.

Federal Rule of Bankruptcy Procedure 4004 governs the relevant deadline.

In a routine Chapter 7 case, a complaint objecting to discharge generally must be filed within sixty days after the first date set for the meeting of creditors, subject to the rule's exceptions and extension provisions.

The deadline is not necessarily extended merely because the meeting is continued.

3. Fraudulent Transfers and Concealment of Property

Section 727(a)(2) addresses specified transfers, removals, destruction, mutilation, or concealment of property undertaken with intent to hinder, delay, or defraud creditors or an officer of the estate.

For prepetition conduct involving the debtor's property, the statute generally focuses on the one-year period before filing.

It also addresses qualifying postpetition conduct involving property of the bankruptcy estate.

Example

A debtor owns a valuable automobile free and clear.

Shortly before filing Chapter 7, the debtor transfers title to an adult child without payment but continues using the vehicle.

If the transfer was intended to hinder, delay, or defraud creditors, it may support denial of discharge.

The trustee may also pursue avoidance of the transfer under separate statutory provisions.

The same transaction can therefore create both property-recovery and discharge consequences.

4. Continuing Concealment

A transfer made more than one year before bankruptcy does not necessarily eliminate every § 727(a)(2) concern.

Courts have recognized a continuing-concealment doctrine in appropriate circumstances.

For example, a debtor may transfer legal title to property but retain a concealed beneficial interest and continue treating the property as personally owned.

If concealment continues into the statutory period with the requisite intent, the conduct may support a discharge objection.

The doctrine is fact-specific.

A debtor should not assume that the passage of one year automatically cures an earlier fraudulent arrangement.

5. False Oaths and False Accounts

Section 727(a)(4)(A) permits denial of discharge when the debtor knowingly and fraudulently makes a false oath or account in or in connection with the bankruptcy case.

The schedules and statement of financial affairs are signed under penalty of perjury.

The debtor also testifies under oath at the meeting of creditors.

Material omissions or false statements may therefore create discharge problems.

Examples include knowingly failing to disclose bank accounts, real estate interests, valuable claims, or significant financial transactions.

A genuine mistake does not automatically establish fraudulent intent.

However, repeated omissions, inconsistent explanations, and failure to correct known inaccuracies may provide evidence of the requisite state of mind.

6. Materiality of a False Statement

Not every inaccurate statement warrants denial of discharge.

A false oath must satisfy the applicable legal requirements, including materiality.

A statement may be material when it concerns the debtor's financial affairs, assets, business dealings, or the discovery and administration of estate property.

The fact that an omitted asset has little monetary value does not necessarily make the omission immaterial.

The trustee and creditors are entitled to accurate information concerning the debtor's financial affairs.

The debtor cannot decide unilaterally that an asset need not be disclosed because it appears insignificant.

7. Failure to Preserve Financial Records

Section 727(a)(3) permits denial of discharge when the debtor has concealed, destroyed, mutilated, falsified, or failed to keep or preserve recorded information from which financial condition or business transactions might be ascertained, unless the conduct is justified under the circumstances.

The provision does not impose identical recordkeeping expectations on every debtor.

A consumer with simple finances may reasonably maintain fewer records than an individual operating a substantial business.

But a debtor must provide sufficient information to permit meaningful examination of financial affairs.

Missing bank statements, unexplained cash transactions, inadequate business records, and destroyed accounting documents can create problems.

The debtor's sophistication, business activities, and circumstances may be relevant.

8. Unexplained Loss of Assets

Under § 727(a)(5), discharge may be denied when the debtor fails to explain satisfactorily a loss of assets or deficiency of assets to meet liabilities.

For example, a debtor may have received $150,000 from a property sale shortly before bankruptcy but have little money remaining when the petition is filed.

The trustee may ask what happened to the proceeds.

The debtor should be prepared to provide a credible explanation supported by available records.

The statute does not necessarily require proof of fraudulent intent.

The issue is whether the debtor satisfactorily explains the disappearance or depletion of assets.

9. Refusal to Obey Court Orders

Section 727(a)(6) addresses certain refusals to obey lawful orders of the bankruptcy court or to respond as required in specified circumstances.

A debtor who refuses to comply with a court order directing production of documents or other required conduct may face serious consequences.

The statute distinguishes refusal from circumstances in which compliance is genuinely impossible.

The debtor should promptly seek appropriate relief when unable to comply rather than simply ignoring an order.

10. Failure to Cooperate With the Trustee

Section 521 imposes duties to cooperate with the trustee and surrender qualifying property and records.

A debtor who fails to provide requested documents, attend examinations, or disclose required information may face motions to compel, dismissal, or other relief.

Not every failure to cooperate automatically establishes grounds for denial of discharge under § 727.

The particular statutory requirements must be satisfied.

Nevertheless, persistent noncompliance can materially jeopardize the case.

11. Fraudulent Claims and Other Misconduct

Section 727(a)(4) also addresses specified misconduct involving false claims, bribery, and withholding recorded information.

For example, a debtor who knowingly presents a false claim in connection with the bankruptcy may face discharge consequences.

The statute contains separate provisions with distinct elements.

A discharge objection should identify the particular subsection and factual basis rather than relying on generalized allegations of dishonesty.

12. Prior Bankruptcy Misconduct

Section 727(a)(7) extends certain discharge-denial provisions to specified misconduct involving another bankruptcy case concerning an insider.

The statute applies under particular circumstances and within defined periods.

For example, misconduct involving a related business bankruptcy may affect an individual's Chapter 7 discharge when the statutory requirements are satisfied.

The relationship between the debtor and the other bankruptcy case must be established.

13. What Is the Burden of Proof?

A party objecting to discharge ordinarily bears the burden of proving the statutory grounds.

Federal Rule of Bankruptcy Procedure 4005 assigns the burden of proof to the plaintiff in an objection-to-discharge proceeding.

Courts generally apply a preponderance-of-the-evidence standard.

The elements differ among the subsections of § 727.

For example, a false-oath claim requires proof of the applicable knowledge and fraudulent-intent elements, while a recordkeeping objection under § 727(a)(3) involves a different inquiry.

The court should not treat every inaccurate schedule entry as equivalent to intentional fraud.

14. Can the Debtor Correct an Omission?

Bankruptcy schedules may be amended under applicable rules.

A debtor who discovers an error should promptly disclose it to counsel and take appropriate steps to correct the filing.

An amendment can be important evidence of cooperation and good faith.

However, correcting an omission does not automatically eliminate the consequences of an earlier knowingly fraudulent statement.

The timing, circumstances, and debtor's intent remain relevant.

A debtor should not wait until the trustee discovers an omission before considering correction.

15. Can a Discharge Be Revoked After It Has Been Granted?

Yes.

Under § 727(d), the bankruptcy court may revoke a Chapter 7 discharge under specified circumstances.

Revocation is not available merely because a creditor regrets failing to object before discharge.

The statute establishes particular grounds.

These include obtaining the discharge through fraud under circumstances described in § 727(d)(1), certain conduct involving property of the estate under § 727(d)(2), and specified failures to comply with court orders or respond to material questions under § 727(d)(3).

Additional provisions address certain failures involving audit-related documents or explanations.

16. Fraudulently Obtaining a Discharge

Under § 727(d)(1), discharge may be revoked when it was obtained through the debtor's fraud and the requesting party did not know of the fraud until after discharge.

This provision requires more than proof that the debtor made an inaccurate statement.

The fraud must satisfy the statutory requirements, including its relationship to obtaining the discharge.

The requesting party's knowledge is also important.

A creditor who knew the relevant facts before discharge may face difficulty relying on this provision afterward.

17. Failure to Turn Over Estate Property

Section 727(d)(2) addresses circumstances in which the debtor acquired property of the estate or became entitled to acquire property that would be estate property and knowingly and fraudulently failed to report or deliver it to the trustee.

For example, a debtor may become entitled to a substantial inheritance within the statutory postpetition period.

If the interest belongs to the estate, the debtor may have duties to disclose and surrender it.

Knowingly and fraudulently withholding estate property may support revocation.

The precise statutory elements must be established.

18. Deadlines for Revocation

Section 727(e) establishes limitations periods for revocation actions.

For revocation under § 727(d)(1), the request generally must be made within one year after discharge.

For revocation under § 727(d)(2) or (3), § 727(e)(2) requires the request before the later of one year after discharge and the date the case is closed. Section 727(e) does not expressly list (d)(4), the audit-related ground; counsel should address the applicable authority rather than assume that every revocation ground has the same limitations period.

These deadlines are important and should not be confused with the ordinary sixty-day objection deadline under Rule 4004.

A party seeking revocation must establish both the substantive grounds and timeliness.

19. Does Denial of Discharge Mean the Case Is Dismissed?

No.

Denial of discharge and dismissal are separate events.

A bankruptcy case may continue even when the debtor is denied a discharge.

The trustee may still administer estate property for the benefit of creditors.

The debtor, however, may remain personally liable for debts that would otherwise have been discharged.

The distinction matters because the debtor may lose the principal personal benefit of bankruptcy while remaining subject to the estate administration process.

20. Can the Debtor File Bankruptcy Again After Denial of Discharge?

A later bankruptcy filing does not necessarily eliminate debts that survived because discharge was denied in an earlier case.

Section 523(a)(10) excepts certain debts from discharge when they were or could have been listed in a prior case in which discharge was waived or denied under specified provisions of § 727.

The statutory details matter.

A debtor should not assume that waiting several years automatically restores the ability to discharge all debts from the earlier case.

The grounds for denial and the nature of the obligations must be examined.

21. Can a Creditor Settle an Objection to Discharge?

Disputes concerning denial of discharge may sometimes be resolved through appropriate procedures.

However, an objection to the debtor's general discharge implicates interests beyond those of a single creditor.

Federal Rule of Bankruptcy Procedure 7041 imposes special requirements concerning dismissal of complaints objecting to discharge.

The court may require notice and examine the circumstances of a proposed dismissal.

A creditor should not assume that a § 727 complaint can be treated as an ordinary private collection lawsuit.

22. Why Discharge Objections Are Different From Ordinary Collection Litigation

A creditor pursuing an ordinary debt seeks payment.

A creditor objecting to discharge seeks to prevent the debtor from receiving relief from potentially all dischargeable debts.

The consequences extend beyond the particular creditor.

This makes discharge litigation especially serious.

The debtor may face substantial litigation expenses and risk losing the central benefit of Chapter 7.

The court must apply the statutory requirements carefully.

23. Practical Steps to Avoid Discharge Problems

The most effective protection against discharge litigation is complete and accurate disclosure.

Before filing, the debtor should identify all assets, debts, financial accounts, business interests, potential legal claims, and significant transfers.

The debtor should preserve relevant financial records and provide accurate explanations for unusual transactions.

After filing, the debtor should cooperate with the trustee, attend required examinations, comply with court orders, and promptly report material developments.

The debtor should not assume that an asset is too small, too uncertain, or too personal to disclose.

Conclusion

Chapter 7 bankruptcy provides substantial relief, but that relief depends on compliance with statutory duties.

A debtor who conceals property, makes fraudulent statements, destroys records, or engages in other specified misconduct may be denied a discharge.

In certain circumstances, a discharge already granted may be revoked.

The consequences can be severe because the debtor may remain liable for obligations that otherwise would have been eliminated.

The safest bankruptcy filing is one based on complete disclosure, accurate financial records, and cooperation with the trustee—not one that depends on an asset or transaction escaping scrutiny.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 727 — Denial and revocation of Chapter 7 discharge.
- 11 U.S.C. § 523 — Exceptions to discharge, including § 523(a)(10).
- 11 U.S.C. § 521 — Debtor duties.
- Federal Rule of Bankruptcy Procedure 4004 — Objections to discharge.
- Federal Rule of Bankruptcy Procedure 4005 — Burden of proof.
- Federal Rule of Bankruptcy Procedure 7001 — Adversary proceedings.
- Federal Rule of Bankruptcy Procedure 7041 — Dismissal of discharge-objection complaints.

Selected decisions

- *Grogan v. Garner*, 498 U.S. 279 (1991) — Establishes the preponderance-of-the-evidence standard in dischargeability litigation.
- *In re Bane*, 720 F.3d 465 (4th Cir. 2013) — Addresses denial of discharge for transfers made with intent to hinder, delay, or defraud creditors.
- *In re French*, 499 F.3d 345 (4th Cir. 2007) — Addresses false oaths and fraudulent intent under § 727(a)(4).
- *In re Kestell*, 99 F.3d 146 (4th Cir. 1996) — Discusses abuse of bankruptcy relief and debtor conduct.
- *In re Chalik*, 748 F.2d 616 (11th Cir. 1984) — Addresses materiality of false oaths and omissions.
- *In re Tully*, 818 F.2d 106 (1st Cir. 1987) — Discusses the debtor's duty of full disclosure and fraudulent false oaths.

Bankruptcy and Inheritances: What Happens When Someone Dies Before or After You File Chapter 7?

Belsky Bankruptcy Legal Library | Bankruptcy Estate, Inheritances, and Property Rights

By Alan J. Belsky, Attorney at Law

An Inheritance Can Become Property of the Bankruptcy Estate Even After Filing

A person considering bankruptcy may expect to receive an inheritance from a parent, spouse, relative, or other individual.

The inheritance may consist of money, real estate, investments, personal property, or an interest in a trust.

Whether the inheritance becomes property of the bankruptcy estate depends on several factors, including when the deceased person died, the debtor's legal rights, the terms of any will or trust, and the timing of the bankruptcy petition.

One of the most important provisions is 11 U.S.C. § 541(a)(5), which brings certain property interests acquired or becoming available within 180 days after filing into the bankruptcy estate.

But the familiar 180-day rule is only part of the analysis.

An inheritance may belong to the bankruptcy estate even when probate has not been completed. A trust interest may present different questions from a direct inheritance. And a debtor who attempts to disclaim an inheritance may discover that the disclaimer does not prevent the bankruptcy trustee from asserting rights.

Understanding these distinctions is essential before filing Chapter 7.

1. Property of the Bankruptcy Estate

Under § 541(a)(1), the bankruptcy estate generally includes the debtor's legal and equitable interests in property as of the commencement of the case.

These interests may include rights that are contingent, disputed, unliquidated, or not yet reduced to possession.

For example, a debtor may have an inheritance interest even though the estate administration process remains incomplete.

The fact that the debtor has not received a check or deed does not necessarily mean the inheritance is excluded from bankruptcy.

The relevant inquiry concerns the debtor's legal interest under applicable law.

2. What If the Person Died Before Bankruptcy Was Filed?

When the person from whom the debtor inherits died before the bankruptcy petition, the debtor may already possess an inheritance interest.

The interest generally becomes property of the bankruptcy estate under § 541(a)(1), even if probate remains pending.

Example

A debtor's mother dies in January, leaving the debtor $80,000 under her will.

The debtor files Chapter 7 in March.

The probate estate has not yet distributed the inheritance.

Nevertheless, the debtor's interest may be property of the bankruptcy estate because the mother died before the bankruptcy filing.

The debtor must disclose the inheritance.

The trustee may administer the nonexempt interest, subject to applicable law.

3. The 180-Day Rule

Section 541(a)(5)(A) generally includes property interests the debtor acquires or becomes entitled to acquire within 180 days after filing by bequest, devise, or inheritance.

The provision extends the bankruptcy estate to certain postpetition inheritances.

Example

A debtor files Chapter 7 on October 1.

The debtor's father dies on December 15, leaving the debtor $100,000.

Because the death occurs within 180 days after filing, the debtor's inheritance interest may become property of the bankruptcy estate.

The fact that the probate estate does not distribute the money until the following year does not necessarily change the result.

The legally significant event may be the debtor's acquisition of the inheritance right, not the eventual payment date.

4. What If the Person Dies After 180 Days?

An inheritance arising from a death occurring more than 180 days after filing ordinarily does not enter a Chapter 7 estate solely under § 541(a)(5)(A).

However, the analysis is not always that simple.

The debtor may have possessed a prepetition property interest under a trust, contract, or other arrangement.

The later death may affect the value or enjoyment of an existing interest rather than create an entirely new one.

Other provisions of § 541 may therefore be relevant.

A debtor should not assume that every inheritance received after 180 days is automatically excluded.

5. When Does the 180-Day Period Begin?

The period generally begins on the bankruptcy petition date.

It is not measured from the meeting of creditors, discharge, or case closing.

This distinction matters because a routine Chapter 7 discharge may be entered approximately three to four months after filing.

A debtor may therefore receive a discharge before the 180-day period expires.

If a qualifying inheritance arises within the statutory period, the debtor may still have disclosure obligations and the trustee may possess rights in the property.

6. Does It Matter When Probate Is Completed?

Not necessarily.

Probate administration may take months or years.

The debtor's inheritance interest may arise before distribution.

For example, a beneficiary may become entitled to a share of an estate when the decedent dies, subject to administration, creditor claims, expenses, and other applicable conditions.

The bankruptcy trustee may succeed to the debtor's interest even though the precise amount remains uncertain.

The debtor should disclose the interest rather than waiting until the personal representative distributes funds.

7. What If the Debtor Does Not Know the Value?

An inheritance may be difficult to value.

The probate estate may contain real estate, investments, debts, disputed claims, or assets requiring appraisal.

The debtor may know that an inheritance is expected but not know the amount.

The appropriate response is disclosure with a reasonable description and valuation information available at the time.

The schedules may need to be amended as additional information becomes available.

Uncertainty about value does not eliminate the disclosure obligation.

8. What If There Is No Will?

When a person dies without a valid will, property may pass under Maryland's intestate succession laws.

The debtor's rights depend on the family relationships and applicable provisions of Maryland Estates and Trusts law.

An inheritance arising through intestacy may become bankruptcy estate property just as an inheritance under a will can.

The absence of a will does not necessarily prevent the debtor from acquiring a property interest.

9. Can a Debtor Refuse or Disclaim an Inheritance?

A debtor may believe that disclaiming an inheritance will prevent the bankruptcy trustee from reaching it.

The issue is complicated.

Maryland law recognizes qualified disclaimers of certain property interests under applicable statutory provisions.

However, the effect of a disclaimer in bankruptcy depends on federal bankruptcy law, state property law, and the timing of the disclaimer.

The Supreme Court's decision in *Drye v. United States*, 528 U.S. 49 (1999), addressed the effect of a disclaimer in the federal tax lien context.

Although *Drye* was not a bankruptcy avoidance case, it illustrates that state-law disclaimers do not necessarily determine federal creditor rights.

A debtor should not attempt to disclaim an inheritance without obtaining advice concerning bankruptcy consequences.

10. Disclaimers Made Before Bankruptcy

A disclaimer executed before filing may be examined under the Bankruptcy Code's avoidance provisions.

The trustee may investigate whether the debtor transferred or relinquished a valuable property interest and whether the transaction is avoidable under applicable law.

The treatment can depend on whether the disclaimer is recognized as a transfer, the effect of state law, and relevant federal precedent.

A disclaimer should not automatically be assumed either effective or ineffective against the bankruptcy estate.

The specific facts and governing law control.

11. Disclaimers After Bankruptcy Filing

When an inheritance interest belongs to the bankruptcy estate, the debtor generally cannot unilaterally eliminate the trustee's rights by disclaiming it.

The trustee may control the estate's interest.

A debtor who attempts to disclaim or redirect an estate asset without authorization may create serious problems.

The appropriate course is to disclose the inheritance and determine who possesses authority to act.

12. Inheritances Through Trusts

Trust interests require separate analysis.

A debtor may be a beneficiary of a revocable trust, irrevocable trust, discretionary trust, or trust containing spendthrift restrictions.

The legal treatment depends on the trust's terms and applicable law.

Section 541(c)(2) recognizes enforceable restrictions on the transfer of beneficial interests in certain trusts.

A valid spendthrift trust may therefore receive protection not available to an outright inheritance.

However, not every trust provision creates an enforceable spendthrift restriction.

The trustee's discretion, beneficiary's rights, and debtor's control over the trust property must be examined.

13. Spendthrift Trusts

A spendthrift trust generally restricts the beneficiary's ability to transfer the beneficial interest and may protect it from certain creditors.

Under § 541(c)(2), an enforceable restriction on transfer under applicable nonbankruptcy law may prevent the beneficial interest from becoming property of the bankruptcy estate.

The Supreme Court addressed § 541(c)(2) in *Patterson v. Shumate*, 504 U.S. 753 (1992).

Although that case concerned an ERISA-qualified pension plan, it established important principles concerning enforceable transfer restrictions.

Maryland trust law determines whether a particular trust restriction is valid and enforceable.

A debtor should not assume that every trust labeled spendthrift is fully protected.

14. Revocable Living Trusts

A revocable living trust often permits the settlor to retain control over trust property during life.

When the settlor dies, the trust may become irrevocable and provide for distribution to beneficiaries.

The bankruptcy treatment of a beneficiary's interest depends on the trust's terms and the timing of the relevant events.

A debtor who is merely a potential beneficiary while the settlor remains alive may possess a different interest from a debtor whose right to distribution has become fixed.

The legal analysis should focus on the debtor's actual rights rather than the trust's title.

15. Discretionary Trust Distributions

Some trusts permit the trustee to determine whether, when, and how much to distribute to a beneficiary.

A debtor's interest may be limited by the trustee's discretion and applicable trust law.

However, discretionary language does not automatically eliminate every property interest.

The beneficiary may possess enforceable rights concerning administration or distributions.

The bankruptcy consequences depend on the precise terms of the trust and governing law.

16. Jointly Owned Property With Survivorship Rights

Property passing by survivorship presents different issues from property passing through probate.

For example, a debtor may jointly own a bank account or real estate with a parent.

Upon the parent's death, the debtor may become the sole owner by operation of law.

The bankruptcy treatment depends on the nature of the debtor's preexisting interest and the effect of survivorship.

Section 541(a)(5) does not necessarily provide the only basis for including the property in the estate.

The debtor's interest may already have existed when bankruptcy was filed.

17. Tenancy by the Entirety and Death of a Spouse

Maryland tenancy by the entirety includes survivorship rights between married spouses.

When one spouse dies, the surviving spouse ordinarily becomes the sole owner of the property.

If bankruptcy is pending, the consequences may depend on the debtor's prepetition entireties interest, the timing of death, and the claims involved.

The surviving spouse's interest should not automatically be characterized as an ordinary inheritance.

Entireties ownership and survivorship arise under a distinct property-law framework.

The bankruptcy trustee's rights require separate analysis.

18. Life Insurance Proceeds

Section 541(a)(5)(C) includes certain interests the debtor acquires or becomes entitled to acquire within 180 days after filing as a beneficiary of a life insurance policy or death benefit plan.

The treatment depends on the policy, beneficiary designation, applicable exemptions, and timing.

For example, a debtor named as beneficiary of a parent's life insurance policy may become entitled to proceeds when the parent dies.

If the death occurs within 180 days after filing, the proceeds may enter the bankruptcy estate.

However, applicable Maryland or federal exemptions may protect some or all of the proceeds.

19. Retirement Account Beneficiary Designations

A debtor may inherit an IRA, 401(k), pension benefit, or other retirement-related asset.

The bankruptcy treatment depends on the account type, beneficiary's rights, and applicable statutory protections.

Inherited IRAs deserve particular attention.

In *Clark v. Rameker*, 573 U.S. 122 (2014), the Supreme Court held that the inherited IRA at issue did not qualify as retirement funds under the federal bankruptcy exemption provision.

The treatment of inherited retirement assets may differ depending on whether the beneficiary is a surviving spouse and whether other exemptions apply.

The account should not be assumed fully protected merely because it originated as retirement savings.

20. Can the Trustee Require the Debtor to Turn Over an Inheritance?

When an inheritance becomes property of the bankruptcy estate, the trustee may seek turnover under applicable provisions, including § 542.

The debtor has duties to cooperate and surrender qualifying estate property.

The trustee may also communicate with the probate estate's personal representative or other parties holding the property.

The debtor should not spend, transfer, or conceal funds belonging to the bankruptcy estate.

Failure to comply can create serious consequences.

21. What If the Inheritance Is Fully Exempt?

An inheritance may be protected in whole or in part by applicable exemptions.

However, Maryland does not provide a universal unlimited exemption for every inheritance.

The debtor must identify the property received and determine which exemptions apply.

Cash inherited outright may receive different treatment from retirement assets, life insurance proceeds, or property held in a valid spendthrift trust.

The debtor should disclose the inheritance and properly claim available exemptions.

22. What If the Debtor Fails to Disclose an Inheritance?

Failure to disclose a qualifying inheritance may result in reopening of the bankruptcy case, trustee recovery efforts, and possible discharge litigation.

Section 727(d)(2) permits revocation of discharge under specified circumstances involving knowing and fraudulent failure to report or deliver estate property.

The debtor's intent and conduct matter.

A debtor who learns of an inheritance after filing should promptly notify bankruptcy counsel.

The debtor should not assume that discharge or case closing eliminates the obligation to report estate property.

Rule 1007(h) ordinarily requires a supplemental schedule, including any claimed exemption, within 14 days after the debtor learns of an interest described in § 541(a)(5), unless the court allows additional time. The duty can continue after case closing.

23. Can the Bankruptcy Case Be Reopened?

Under § 350(b), a bankruptcy court may reopen a case to administer assets, provide relief to the debtor, or for other cause.

A previously undisclosed inheritance may provide grounds for reopening.

Reopening does not automatically determine whether the inheritance is estate property or exempt.

Those questions may require further proceedings.

A debtor should not assume that closing the bankruptcy case permanently prevents administration of an undisclosed inheritance.

24. Chapter 13 Treats Postpetition Property Differently

Chapter 13 contains broader provisions concerning property acquired after filing.

Under § 1306, the Chapter 13 estate generally includes certain property acquired after commencement of the case and before closing, dismissal, or conversion.

Consequently, an inheritance received more than 180 days after filing may still become property of a Chapter 13 estate.

The Fourth Circuit addressed this issue in *Carroll v. Logan*, 735 F.3d 147 (4th Cir. 2013).

The court held that an inheritance received more than 180 days after a Chapter 13 filing became property of the estate under § 1306.

This is an important distinction between Chapters 7 and 13.

25. Why Timing Matters Before Filing

A debtor expecting an inheritance should disclose the circumstances before filing bankruptcy.

The timing of a death, probate proceeding, trust distribution, or beneficiary entitlement may materially affect estate property.

However, bankruptcy planning should not be based on speculation about another person's death or attempts to conceal or redirect assets.

The proper analysis should identify the debtor's existing rights, potential future interests, applicable exemptions, and realistic consequences of filing.

In some circumstances, Chapter 13 or a nonbankruptcy alternative may be preferable.

Conclusion

An inheritance can become property of the bankruptcy estate even when the debtor receives it after filing.

In Chapter 7, § 541(a)(5) generally includes qualifying inheritances arising within 180 days after the petition.

But prepetition interests, trusts, survivorship rights, and other property arrangements can create different results.

Chapter 13 contains broader provisions concerning postpetition property, including inheritances received beyond 180 days.

Disclaimers, beneficiary designations, and spendthrift restrictions require careful legal analysis.

A debtor who expects or becomes entitled to an inheritance should disclose the interest promptly and determine its bankruptcy consequences before transferring or spending the property.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 541 — Property of the bankruptcy estate, including certain postpetition inheritances.
- 11 U.S.C. § 542 — Turnover of estate property.
- 11 U.S.C. § 522 — Exemptions.
- 11 U.S.C. § 350 — Reopening bankruptcy cases.
- 11 U.S.C. § 727 — Denial and revocation of discharge.
- 11 U.S.C. § 1306 — Chapter 13 estate property.

Maryland law

- Maryland Estates and Trusts Article — Probate, intestacy, trusts, and disclaimers.
- Maryland Courts and Judicial Proceedings § 11-504 — Maryland exemptions.

Selected decisions

- *Carroll v. Logan*, 735 F.3d 147 (4th Cir. 2013) — Holds that a Chapter 13 inheritance received more than 180 days after filing becomes property of the estate under § 1306.
- *Patterson v. Shumate*, 504 U.S. 753 (1992) — Addresses enforceable restrictions on transfer under § 541(c)(2).
- *Clark v. Rameker*, 573 U.S. 122 (2014) — Addresses inherited IRAs and federal bankruptcy exemption protection.
- *Drye v. United States*, 528 U.S. 49 (1999) — Addresses state-law disclaimers and federal tax lien rights.
- *In re Costas*, 555 F.3d 790 (9th Cir. 2009) — Addresses prepetition disclaimers and fraudulent-transfer avoidance.

Bankruptcy and Retirement Accounts: Which IRAs, 401(k)s, Pensions, and Inherited Accounts Are Protected?

Belsky Bankruptcy Legal Library | Bankruptcy Exemptions and Retirement Assets

By Alan J. Belsky, Attorney at Law

Retirement Savings Often Receive Greater Protection Than Other Assets

Individuals considering bankruptcy frequently worry that they will lose the retirement savings accumulated over decades of employment.

Fortunately, federal and Maryland law provide substantial protection for many retirement accounts, pensions, and other qualifying retirement benefits.

In some circumstances, retirement assets are excluded from the bankruptcy estate altogether. In others, they become estate property but may be claimed exempt.

That distinction matters legally, although both mechanisms may allow the debtor to retain the funds.

Not every account described as a retirement account receives identical protection. Traditional IRAs, Roth IRAs, employer-sponsored retirement plans, inherited accounts, and annuities may be governed by different rules.

The debtor's age, account ownership, beneficiary status, plan qualifications, and recent transactions can also affect the result.

Understanding these differences is essential before filing Chapter 7 or Chapter 13.

1. The Difference Between Exclusion and Exemption

Under 11 U.S.C. § 541(a), most of the debtor's legal and equitable interests in property become part of the bankruptcy estate when the petition is filed.

However, § 541(c)(2) recognizes enforceable restrictions on the transfer of beneficial interests in certain trusts.

A qualifying retirement plan containing an enforceable transfer restriction may therefore be excluded from the bankruptcy estate.

Other retirement assets may enter the estate but qualify for exemption under § 522 or applicable state law.

The distinction affects the legal mechanism protecting the funds.

An excluded asset ordinarily is not property the trustee may administer.

An exempt asset may initially become estate property but is protected through the applicable exemption process.

2. Employer-Sponsored 401(k) Plans

Many employer-sponsored 401(k) plans receive substantial protection under federal law.

Plans qualifying under ERISA and containing enforceable anti-alienation provisions may be excluded from the bankruptcy estate under § 541(c)(2).

The Supreme Court addressed this principle in *Patterson v. Shumate*, 504 U.S. 753 (1992).

The Court held that an enforceable restriction on transfer contained in an ERISA-qualified pension plan could satisfy § 541(c)(2).

The result can provide protection beyond ordinary dollar-limited exemptions.

However, the plan's actual legal status and governing documents must be examined.

A debtor should not assume that every account labeled 401(k) is necessarily protected in precisely the same manner.

3. Traditional IRAs

Traditional individual retirement accounts generally receive protection under the Bankruptcy Code's retirement-fund exemption provisions.

Section 522(b)(3)(C) protects qualifying retirement funds held in accounts exempt from taxation under specified Internal Revenue Code provisions.

Section 522(n) imposes an aggregate dollar limitation on certain IRA exemptions, subject to statutory exceptions and periodic adjustments.

The limitation does not apply identically to every type of retirement account or rollover.

A debtor with substantial IRA assets should determine the applicable exemption amount and whether any portion of the funds qualifies for protection outside the ordinary IRA cap.

4. Roth IRAs

Roth IRAs generally may qualify for federal bankruptcy exemption protection under the applicable retirement-fund provisions.

However, the account must satisfy the statutory requirements.

The IRA dollar limitation under § 522(n) may apply to qualifying traditional and Roth IRA funds in the aggregate, subject to applicable exclusions and exceptions.

The debtor should not assume that maintaining separate Roth and traditional accounts creates separate full exemption limits for each.

The account's tax status and source of funds matter.

5. The IRA Exemption Cap

The Bankruptcy Code periodically adjusts certain dollar amounts under § 104.

The IRA exemption limit under § 522(n) is among the amounts subject to adjustment.

For cases filed during the adjustment period beginning April 1, 2025, the applicable aggregate IRA limit is $1,711,975, subject to the statute's exceptions and the bankruptcy court's authority to increase the amount when the interests of justice require.

The limit applies to the specified category of IRA funds rather than every retirement asset a debtor owns.

Qualifying rollover amounts may receive different treatment under the statute.

A debtor with substantial retirement assets should identify the source and legal character of each account before filing.

6. Rollovers From Employer Retirement Plans

A debtor may have transferred funds from a former employer's 401(k) or other qualifying retirement plan into an IRA.

Certain rollover funds receive special protection under § 522(b)(4) and § 522(n).

The statutory provisions can exclude qualifying rollover amounts from the ordinary IRA cap.

But the debtor may need records establishing the source and continuity of the funds.

A rollover should not be assumed to retain every protection automatically without examining the transaction.

The account statements and rollover documentation may be important.

7. Pensions and Defined Benefit Plans

Traditional pension plans may provide retirement income based on employment history, compensation, and plan terms.

Many qualifying employer-sponsored pensions receive protection through ERISA and § 541(c)(2).

Other pension arrangements may qualify for exemption under federal or Maryland law.

The debtor's interest may consist of a present right to payments, a future benefit, or another form of plan interest.

The treatment depends on the plan's legal structure and applicable restrictions.

A debtor should disclose the pension interest even when payments have not begun, subject to the official forms' requirements.

8. Government Employee Retirement Plans

Government retirement systems may not be governed by ERISA in the same manner as private employer plans.

However, they may receive substantial protection under applicable federal or state law.

Maryland public employee retirement benefits may be protected through provisions governing the relevant retirement system.

Federal employee retirement benefits may receive protection under separate federal statutes.

The debtor should identify the particular plan rather than assuming that every pension is governed by the same exemption.

9. Social Security Retirement Benefits

Social Security retirement benefits receive significant protection under federal law.

Under 42 U.S.C. § 407, qualifying Social Security benefits generally are protected from execution, levy, attachment, garnishment, and other legal process, subject to applicable federal exceptions.

The benefits are also excluded from the Bankruptcy Code's definition of current monthly income under § 101(10A).

The treatment of accumulated benefits deposited into bank accounts may require tracing and other analysis.

A debtor should preserve records identifying the source of funds.

Social Security benefits should not be confused with distributions from privately owned retirement accounts.

10. Inherited IRAs

Inherited IRAs present a significant exception to the ordinary expectation that retirement accounts are protected.

In *Clark v. Rameker*, 573 U.S. 122 (2014), the Supreme Court held that funds in the inherited IRA at issue did not qualify as retirement funds under the federal bankruptcy exemption provision.

The Court emphasized characteristics distinguishing inherited IRAs from accounts held for the owner's own retirement.

For example, a nonspouse beneficiary generally cannot contribute additional funds to the inherited IRA and may be required to take distributions under applicable tax rules.

The account therefore may not receive the same federal bankruptcy exemption protection as an IRA owned by the original retirement saver.

11. Inherited IRAs and Surviving Spouses

A surviving spouse may have options unavailable to a nonspouse beneficiary.

Depending on applicable tax law and the account arrangement, a surviving spouse may be able to treat an inherited IRA as the spouse's own IRA.

That treatment can affect bankruptcy exemption analysis.

However, the result depends on the steps actually taken, the account's legal status, and applicable law.

A surviving spouse should not assume that every inherited IRA automatically becomes protected as the spouse's own retirement account.

12. Maryland Exemption Protection for Retirement Accounts

Maryland law provides additional protection for qualifying retirement assets.

Courts and Judicial Proceedings Article § 11-504(h) addresses certain interests in retirement plans and accounts.

The availability of protection depends on the account's qualification under the statutory language.

Maryland's exemption scheme must be considered together with applicable federal nonbankruptcy protections and the Bankruptcy Code.

A debtor should not assume that the federal IRA cap necessarily determines the ultimate protection available under Maryland law.

The interaction of state and federal provisions requires careful analysis.

Maryland § 11-504(h) covers specified qualified-plan interests of participants and beneficiaries, including qualifying § 408 and § 408A accounts, and contains no general dollar ceiling comparable to § 522(n). It has express exceptions, including Maryland Department of Health claims and excess contributions with associated earnings, and separately addresses alternate payees. For an inherited account, Clark resolves the federal retirement-funds issue, while eligibility under Maryland's separate statutory language requires its own analysis.

13. Retirement Accounts and the Means Test

Retirement accounts can affect the debtor's financial circumstances in ways separate from exemption protection.

For example, distributions from an IRA may constitute income for certain bankruptcy purposes, depending on the governing statute and applicable case law.

Social Security benefits receive different treatment under § 101(10A).

The fact that retirement funds are exempt does not necessarily mean distributions are excluded from every income calculation.

A debtor who recently withdrew substantial funds from an IRA should disclose the transaction and determine its effect on the means test, schedules, and available assets.

14. IRA Withdrawals Before Bankruptcy

Withdrawing funds from a protected retirement account can change the legal character of the money.

Funds remaining in a qualifying retirement account may receive substantial exemption protection.

Once withdrawn and deposited into an ordinary checking account, the funds may be subject to different rules.

Some statutes protect qualifying distributions or permit tracing, but protection should not be assumed.

A debtor should not liquidate retirement assets to pay ordinary unsecured debts without first evaluating bankruptcy alternatives.

Doing so may convert protected retirement savings into payments on debts that could have been discharged.

15. Using Retirement Funds to Pay Credit Cards

A debtor may consider withdrawing money from a 401(k) or IRA to pay credit card balances before bankruptcy.

This can be financially harmful.

The withdrawal may trigger income taxes, penalties, or other consequences.

The debtor may also lose retirement savings that would otherwise have been protected in bankruptcy.

If the debtor later files Chapter 7, the credit card debts may have been dischargeable without using retirement funds.

The decision should be evaluated before the withdrawal occurs.

16. Loans Against Retirement Plans

Some employer-sponsored retirement plans permit participants to borrow against their account balances.

The bankruptcy treatment of plan loans differs from ordinary unsecured loans.

A plan loan may not constitute a conventional debt owed to an outside creditor in the same manner as a bank loan.

Repayment obligations and the consequences of default may be governed by plan terms and tax law.

Chapter 13 contains specific provisions concerning certain retirement-plan loan repayments.

A debtor should examine the plan documents and the legal character of the loan before filing.

17. Retirement Contributions Before Bankruptcy

Contributions to retirement accounts shortly before bankruptcy can raise questions concerning exemption planning, the means test, and the debtor's financial circumstances.

Ordinary lawful contributions are not automatically fraudulent.

However, unusually large contributions made while insolvent or facing creditor collection may warrant scrutiny.

The Bankruptcy Code contains provisions addressing certain transfers involving retirement accounts and exempt property.

A debtor should not assume that converting nonexempt funds into retirement savings immediately before filing is always risk-free.

18. Retirement Contributions During Chapter 13

Chapter 13 presents additional questions concerning retirement contributions and disposable income.

The Bankruptcy Code contains provisions addressing certain retirement contributions and loan repayments.

The treatment of voluntary retirement contributions has generated litigation.

Courts have examined whether contributions are excluded from disposable income and whether the debtor's proposed plan satisfies good-faith and other requirements.

The applicable Fourth Circuit authority and the particular facts must be considered.

A debtor should not assume that every proposed retirement contribution will receive identical treatment.

19. Annuities

Annuities may resemble retirement products but can have very different legal characteristics.

Some annuities are held within qualifying retirement accounts.

Others are privately purchased investment or insurance contracts.

The bankruptcy treatment depends on the annuity's structure, ownership, beneficiary provisions, and applicable exemption law.

An annuity should not automatically be treated as an exempt retirement account merely because it provides periodic payments.

20. Retirement Assets in Divorce

Divorce may affect ownership of retirement accounts and pension benefits.

A qualified domestic relations order or other legally effective arrangement may allocate benefits between spouses or former spouses.

The bankruptcy treatment depends on the debtor's actual property interest, plan documents, and applicable law.

A debtor may possess rights to retirement benefits that have not yet been transferred or distributed.

Those interests should be disclosed and evaluated.

21. Retirement Accounts and Beneficiary Designations

A debtor may be entitled to receive retirement assets because of another person's death.

The timing and nature of the beneficiary's rights can affect whether the interest becomes property of the bankruptcy estate.

Under § 541(a)(5), certain interests acquired within 180 days after filing may enter the estate.

Inherited retirement accounts may also receive different exemption treatment from accounts owned by the original participant.

Beneficiary designations should therefore be reviewed when an inheritance or death benefit is anticipated.

22. Can a Trustee Demand Retirement Account Records?

Yes.

A Chapter 7 trustee may request documentation necessary to determine the nature, value, and exemption status of retirement assets.

Relevant records may include account statements, plan documents, rollover records, beneficiary designations, and tax information.

The debtor should provide accurate information.

The fact that an account is believed to be exempt does not eliminate the duty to disclose it.

23. Why Retirement Planning Must Precede Bankruptcy Filing

Retirement accounts may represent a debtor's most valuable financial assets.

Improper withdrawals, transfers, rollovers, or beneficiary arrangements can alter their legal treatment.

A debtor should identify every account, determine the applicable protection, and evaluate any recent transactions before filing.

The analysis is particularly important for older debtors who may have limited opportunities to rebuild retirement savings.

The objective should be to obtain lawful debt relief while preserving protected retirement assets whenever possible.

Conclusion

Federal and Maryland law provide substantial protection for many retirement accounts, pensions, and Social Security benefits.

Qualifying employer-sponsored retirement plans may be excluded from the bankruptcy estate, while IRAs and other retirement funds may receive statutory exemption protection.

But not every retirement-related asset is treated identically.

Inherited IRAs, annuities, recent withdrawals, rollovers, and retirement-plan loans can present special issues.

A debtor should not withdraw or transfer retirement savings to pay dischargeable debts without first determining whether those savings would be protected in bankruptcy.

For many individuals, preserving retirement assets is one of the most important benefits of proper bankruptcy planning.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 541(c)(2) — Exclusion of certain beneficial interests subject to enforceable transfer restrictions.
- 11 U.S.C. § 522(b)(3)(C) — Exemption for qualifying retirement funds.
- 11 U.S.C. § 522(b)(4) — Certain retirement account transfers and rollovers.

- 11 U.S.C. § 522(n) — IRA exemption limitation.
- 11 U.S.C. § 101(10A) — Current monthly income.
- 42 U.S.C. § 407 — Protection of Social Security benefits.

Maryland law

- Maryland Courts and Judicial Proceedings § 11-504(h) — Protection of qualifying retirement interests.

Selected decisions

- *Patterson v. Shumate*, 504 U.S. 753 (1992) — Holds that enforceable ERISA anti-alienation provisions may exclude qualifying pension interests from the bankruptcy estate.
- *Clark v. Rameker*, 573 U.S. 122 (2014) — Holds that the inherited IRA at issue did not qualify as retirement funds under the federal bankruptcy exemption.
- *Rousey v. Jacoway*, 544 U.S. 320 (2005) — Addresses exemption protection for IRAs under the former federal statutory framework.
- *In re Yuhas*, 104 F.3d 612 (3d Cir. 1997) — Addresses exclusion of certain retirement assets from the bankruptcy estate.
- In re Chilton, 674 F.3d 486 (5th Cir. 2012) — Its treatment of inherited IRAs as retirement funds was rejected by Clark v. Rameker, 573 U.S. 122 (2014); it is historical background, not the current rule supporting that federal exemption.
- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Addresses projected disposable income in Chapter 13.

Bankruptcy and Social Security Benefits: Why Protected Income Can Still Create Complicated Bankruptcy Questions

Belsky Bankruptcy Legal Library | Exempt Income, Disability Benefits, and Means Testing

By Alan J. Belsky, Attorney at Law

Social Security Benefits Receive Special Protection in Bankruptcy

Social Security retirement and disability benefits often provide essential income for individuals who can no longer work or whose earning capacity has declined.

Federal law affords these benefits substantial protection from creditors.

The Bankruptcy Code also treats Social Security benefits differently from many other sources of income when determining Chapter 7 eligibility.

But the protection is not always as simple as saying that Social Security cannot be touched.

Important questions arise when benefits accumulate in bank accounts, are mixed with other funds, are used to purchase property, or are subject to claims for overpayment.

The distinction between Social Security retirement, Social Security Disability Insurance, Supplemental Security Income, private disability insurance, and other benefits can also materially affect the analysis.

A debtor considering bankruptcy should understand both the protections and their limitations.

1. Federal Protection Under 42 U.S.C. § 407

Section 407(a) of the Social Security Act provides broad protection for qualifying benefits.

The statute generally prohibits transfer or assignment of the right to future payments and protects benefits from execution, levy, attachment, garnishment, or other legal process, subject to applicable federal exceptions.

The provision also protects benefits against the operation of bankruptcy or insolvency law.

This protection is significant because it arises under federal law independently of ordinary state exemption limits.

A debtor receiving qualifying Social Security benefits may therefore have protections that are not dependent on Maryland's general cash exemption.

2. Social Security Benefits and the Bankruptcy Estate

Under 11 U.S.C. § 541, most of the debtor's legal and equitable interests in property become part of the bankruptcy estate.

However, § 407 can protect qualifying Social Security benefits from administration.

Courts have examined the interaction between § 407 and the Bankruptcy Code.

In *Carpenter v. Ries*, 614 F.3d 930 (8th Cir. 2010), the court held that Social Security benefits retained their protection under § 407 and were excluded from the bankruptcy estate in the circumstances presented.

The treatment of accumulated benefits and the application of controlling precedent should be considered carefully.

The debtor should disclose financial accounts and other required information even when the funds are protected.

3. Social Security Benefits Are Excluded From Current Monthly Income

The Bankruptcy Code defines current monthly income in § 101(10A).

That definition expressly excludes benefits received under the Social Security Act.

This exclusion is important for Chapter 7 means testing.

For example, a debtor may receive $3,500 monthly in Social Security retirement benefits and $1,000 from other sources.

The Social Security benefits generally are excluded from statutory current monthly income.

The debtor's means-test income may therefore be substantially lower than the total amount available for household expenses.

However, the debtor must still complete the required bankruptcy disclosures accurately.

4. Social Security Retirement Versus Disability Benefits

Social Security retirement benefits and Social Security Disability Insurance benefits generally receive protection under § 407.

Both are benefits paid under the Social Security Act.

Supplemental Security Income also receives federal statutory protection.

However, the eligibility requirements and administration of these programs differ.

The debtor should identify the precise benefit received.

A payment described informally as disability income may come from a private insurer or employer rather than the Social Security Administration.

Such payments may not receive the same treatment.

5. Private Disability Insurance Is Different

Private disability insurance benefits are not automatically excluded from current monthly income merely because they replace wages lost through disability.

Their treatment depends on the source of payment, applicable statutory provisions, and the nature of the benefit.

For example, an employer-sponsored long-term disability policy may provide monthly payments that are treated differently from Social Security Disability Insurance.

The debtor may have exemption rights under Maryland law or other applicable provisions.

But the federal Social Security exclusion should not be applied indiscriminately to every disability payment.

6. Workers' Compensation Benefits

Workers' compensation benefits arise under a separate statutory system.

Maryland Labor and Employment Article § 9-732 provides important protections for qualifying workers' compensation benefits.

However, workers' compensation payments do not automatically receive the same current-monthly-income treatment as Social Security benefits.

The debtor should distinguish the source and legal character of each payment.

A debtor receiving both Social Security Disability Insurance and workers' compensation may therefore need separate analyses for the two income streams.

7. Social Security Benefits Deposited Into Bank Accounts

Many recipients receive benefits through direct deposit.

The fact that protected benefits are deposited into a bank account does not necessarily eliminate their federal protection.

However, practical problems can arise when the account also contains wages, gifts, retirement distributions, or other funds.

A creditor or trustee may need to determine which portion of the balance is attributable to Social Security benefits.

The debtor should preserve account statements and records showing the source of deposits.

Separate accounts may simplify tracing, although the legal necessity and consequences depend on applicable law.

8. Accumulated Social Security Benefits

A debtor may save portions of Social Security benefits over many months or years.

The accumulated balance may be substantial.

For example, a retiree who spends less than the monthly benefit amount may accumulate $30,000 in a savings account.

The debtor should not assume that the funds lose protection merely because they were not spent immediately.

But the source and character of the funds must be established.

The treatment of accumulated benefits may depend on whether they remain identifiable and whether other transactions have altered their legal character.

9. Commingling Protected and Unprotected Funds

Commingling occurs when protected benefits are deposited into an account containing other money.

For example, a debtor may receive Social Security benefits, part-time wages, and gifts into the same checking account.

The debtor may then pay ordinary household expenses from that account.

The resulting balance may be difficult to trace to particular deposits.

Courts may apply tracing principles to determine the protected portion.

A debtor who relies on § 407 should maintain sufficient records to establish the source of the funds.

10. Can Creditors Garnish a Bank Account Containing Social Security?

Federal regulations provide special protections for certain federal benefit payments deposited electronically into bank accounts.

Under 31 C.F.R. Part 212, financial institutions generally must conduct an account review when served with certain garnishment orders and protect qualifying federal benefit deposits within the prescribed lookback period.

The regulations establish procedures for calculating a protected amount.

These protections do not necessarily resolve every dispute concerning funds outside the automatic account-review protection.

A debtor may need to assert additional exemption rights or challenge an improper garnishment.

The existence of automatic bank protections should not be confused with the full substantive scope of § 407.

11. Social Security and Chapter 13 Disposable Income

Chapter 13 requires qualifying debtors to propose repayment plans satisfying the Bankruptcy Code's confirmation requirements.

The treatment of Social Security benefits can create difficult questions because the benefits are excluded from current monthly income.

Courts have considered whether a debtor's decision not to contribute Social Security income to plan payments affects good faith.

In *Mort Ranta v. Gorman*, 721 F.3d 241 (4th Cir. 2013), the Fourth Circuit addressed the exclusion of Social Security income from disposable-income calculations and its relationship to Chapter 13 plan confirmation.

The court recognized the statutory exclusion.

A debtor's overall plan must nevertheless satisfy the applicable confirmation requirements.

12. Social Security Income and Schedule I

The exclusion of Social Security benefits from current monthly income does not mean the debtor may omit them from every bankruptcy form.

Schedule I generally requires disclosure of current income from relevant sources, including Social Security benefits.

The means-test forms and Schedule I serve different purposes.

A debtor may properly report Social Security income on Schedule I while excluding it from the statutory current-monthly-income calculation.

The apparent difference is not necessarily an inconsistency.

The forms should be completed according to their respective instructions.

13. Social Security Income and Schedule J

Schedule J reports the debtor's current monthly expenses.

A debtor receiving Social Security benefits may use those benefits to pay housing, food, utilities, transportation, healthcare, and other expenses.

The debtor should report expenses accurately.

The fact that Social Security benefits are excluded from the means test does not justify inflating expenses or omitting household contributions.

The debtor's actual financial circumstances remain relevant to bankruptcy planning.

14. Social Security Overpayments

Social Security overpayments present a distinct problem.

The Social Security Administration may determine that a recipient received benefits exceeding the amount legally payable.

The agency may seek recovery through withholding future benefits or other authorized procedures.

Bankruptcy can affect personal liability for certain overpayments, but the analysis depends on the nature of the obligation.

An ordinary overpayment may be dischargeable in some circumstances.

An overpayment obtained through fraud or other conduct falling within § 523 may present different issues.

The agency's administrative recovery and offset rights require separate consideration.

15. Overpayments Caused by Administrative Error

A recipient may receive excessive benefits because of an agency calculation or administrative error.

The fact that the overpayment was not caused by intentional misconduct can be important.

However, the absence of fraud does not necessarily eliminate the agency's statutory recovery rights.

The recipient may have administrative rights to request reconsideration, waiver, or a different recovery rate under applicable Social Security rules.

Those remedies are distinct from bankruptcy discharge.

A debtor should not assume that bankruptcy is the only available response to an overpayment determination.

16. Waiver of Social Security Overpayment Recovery

The Social Security Act provides procedures for seeking waiver of recovery in qualifying circumstances.

Under 42 U.S.C. § 404(b), recovery of certain overpayments may be waived when the recipient was without fault and the additional statutory requirements are satisfied.

The waiver inquiry may consider whether recovery would defeat the purpose of the Social Security Act or be against equity and good conscience.

The precise standards depend on the benefit program and applicable regulations.

A debtor facing a substantial overpayment should consider administrative waiver rights before assuming repayment is unavoidable.

17. Bankruptcy Discharge and Government Offset Rights

The discharge of a debt and the government's right to offset obligations are not necessarily identical questions.

Section 553 generally preserves qualifying setoff rights, subject to the Bankruptcy Code's limitations.

The Social Security Administration also operates under specific federal statutes governing benefit recovery.

A debtor who obtains a discharge of an overpayment may still need to examine whether the agency asserts a legally permissible offset or recoupment right.

The distinction between setoff and recoupment can be important.

The debtor should not assume that a discharge order automatically resolves every administrative withholding issue.

SSA’s bankruptcy instructions generally call for suspension of recovery of prepetition overpayments while the bankruptcy is pending, subject to particular cases in which its Office of General Counsel advises that lawful recoupment may continue. Recoupment is a distinct, narrowly analyzed doctrine involving obligations from the same transaction; it is not a general license to disregard the stay or discharge because both obligations involve Social Security. A claimed exception must be evaluated under the governing law and facts.

18. Can Social Security Benefits Be Used to Pay Nondischargeable Debts?

Section 407 provides broad protection, but federal law recognizes certain exceptions.

For example, qualifying child support and alimony enforcement may reach certain federal benefits under 42 U.S.C. § 659.

Federal tax collection also operates under specific statutory provisions.

The debtor should not assume that Social Security benefits are absolutely immune from every governmental or support-related claim.

The type of benefit and the nature of the obligation matter.

19. Social Security Benefits and Married Debtors

A married debtor may receive Social Security benefits while the nonfiling spouse earns wages or receives other income.

The means-test treatment of each income source must be determined separately.

The Social Security exclusion applies to qualifying benefits under the statutory definition.

Other household income and contributions may still be included under applicable rules.

A married debtor should not assume that the exclusion of Social Security benefits removes the need to analyze the spouse's income or household expenses.

20. Social Security Benefits and Household Size

Household size may affect the applicable Maryland median-income threshold and standardized expense allowances.

A debtor may live with adult children, an elderly parent, or other relatives.

The presence of Social Security income does not independently determine household size.

The Fourth Circuit's economic-unit approach, discussed in *Johnson v. Zimmer*, 686 F.3d 224 (4th Cir. 2012), may be relevant to household composition.

The debtor's actual financial arrangements should be examined.

21. What If Social Security Benefits Are Used to Purchase Property?

A debtor may use accumulated Social Security benefits to purchase an automobile, real estate, or other property.

The bankruptcy treatment of the purchased asset may differ from the treatment of the original benefit payments.

The debtor should not assume that every asset purchased with Social Security funds automatically retains the full protection of § 407.

The legal consequences may depend on the property, transaction, tracing principles, and applicable exemption law.

This issue should be evaluated before converting substantial protected funds into another form of property.

22. Why Social Security Recipients May Be Good Chapter 7 Candidates

A debtor whose income consists primarily of Social Security benefits may qualify for Chapter 7 even when the benefits provide sufficient funds for ordinary living expenses.

The statutory exclusion from current monthly income can be important.

However, the debtor's assets, other income, debts, and overall financial circumstances must still be examined.

A retiree with substantial nonexempt investments may face liquidation risk despite qualifying under the means test.

Conversely, a debtor with protected retirement income, exempt property, and substantial unsecured debt may be an excellent Chapter 7 candidate.

Conclusion

Social Security retirement and disability benefits receive substantial protection under federal law.

They generally are excluded from current monthly income for bankruptcy means-testing purposes and may be protected from creditor process and bankruptcy administration.

But accumulated benefits, commingled bank accounts, property purchases, overpayments, and administrative recovery rights can create additional questions.

The treatment of private disability income and workers' compensation differs from Social Security benefits.

A debtor receiving Social Security should not assume that all income and assets are treated alike—or that a Social Security overpayment is necessarily immune from bankruptcy relief.

Careful analysis can preserve protected benefits while identifying appropriate options for dealing with other debts.

Related Bankruptcy Cases and Authorities

Federal statutes and regulations

- 42 U.S.C. § 407 — Protection of Social Security benefits.
- 42 U.S.C. § 404 — Social Security overpayments and waiver provisions.
- 42 U.S.C. § 659 — Certain support enforcement involving federal payments.
- 11 U.S.C. § 101(10A) — Current monthly income.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 553 — Setoff.
- 31 C.F.R. Part 212 — Garnishment protections for certain federal benefit payments.

Maryland law

- Maryland Labor and Employment § 9-732 — Protection of qualifying workers' compensation benefits.

Selected decisions

- *Mort Ranta v. Gorman*, 721 F.3d 241 (4th Cir. 2013) — Addresses Social Security income exclusion and Chapter 13 disposable-income analysis.
- *Carpenter v. Ries*, 614 F.3d 930 (8th Cir. 2010) — Addresses exclusion of Social Security benefits from the bankruptcy estate under § 407.
- *Johnson v. Zimmer*, 686 F.3d 224 (4th Cir. 2012) — Addresses household size using the economic-unit approach.
- *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16 (1995) — Addresses setoff and temporary administrative holds in bankruptcy.
- *In re Cranmer*, 697 F.3d 1314 (10th Cir. 2012) — Addresses exclusion of Social Security income from Chapter 13 disposable income and good-faith considerations.

Bankruptcy and Tax Refunds: When the Trustee Can Take Your Refund and How Maryland Exemptions May Protect It

Belsky Bankruptcy Legal Library | Chapter 7 Assets, Exemptions, and Tax Planning

By Alan J. Belsky, Attorney at Law

Your Tax Refund May Belong to the Bankruptcy Estate Even Before You Receive It

A person considering Chapter 7 bankruptcy may have little money in the bank but still possess a valuable asset: the right to receive an income tax refund.

The refund may not arrive until months after the bankruptcy petition is filed. Nevertheless, the debtor may already have acquired a property interest in some or all of it.

Under 11 U.S.C. § 541, a debtor's legal and equitable interests in property generally become part of the bankruptcy estate when the case begins.

That can include the portion of an anticipated tax refund attributable to prepetition earnings, withholding, or other qualifying payments.

The Chapter 7 trustee may therefore seek turnover of refund proceeds even after the debtor receives a discharge.

But the trustee's rights are not unlimited. Exemptions, the timing of the filing, the nature of the refund, and the rights of a nonfiling spouse may affect the amount available for administration.

Understanding these issues before filing can prevent a debtor from unexpectedly losing a refund needed for ordinary living expenses.

1. Why a Tax Refund Is Property

A tax refund generally represents an amount paid or credited toward taxes that exceeds the taxpayer's ultimate liability, together with certain refundable credits.

The debtor may acquire an interest in that refund during the tax year as wages are withheld or estimated tax payments are made.

The fact that the return has not yet been prepared does not necessarily mean no property interest exists.

For example, a debtor who files Chapter 7 in October may have accumulated substantial withholding credits during the first nine months of the year.

If those credits ultimately produce a refund, a portion may belong to the bankruptcy estate.

2. The Petition Date Matters

The bankruptcy petition generally establishes the relevant division between prepetition and postpetition property in an ordinary Chapter 7 case.

A refund attributable to a tax year completed before filing may be entirely attributable to prepetition activity.

A refund for the tax year during which bankruptcy is filed may require allocation.

The appropriate method depends on applicable law and the nature of the refund.

The trustee may request the debtor's tax return after it is filed to determine the estate's interest.

3. Example: Filing Bankruptcy in October

Assume a debtor files Chapter 7 on October 15.

The debtor later receives a $6,000 federal income tax refund for that calendar year.

A substantial portion of the refund may be attributable to income earned and taxes withheld before the petition date.

A simplified allocation might use the proportion of the tax year preceding the filing.

However, a mechanical day-count allocation does not necessarily determine the correct legal result in every case.

The actual sources of the refund, timing of payments, refundable credits, and applicable law may require a different calculation.

The debtor should not assume that the entire refund belongs to the trustee or that the entire refund belongs to the debtor.

4. Refunds for Prior Tax Years

A refund attributable to a tax year completed before bankruptcy ordinarily presents a strong estate-property issue.

For example, a debtor files Chapter 7 in February 2027 but has not yet received the refund for tax year 2026.

The right to the refund may have existed when the petition was filed, even though the return had not been submitted.

The refund generally must be disclosed as an asset.

The debtor may claim applicable exemptions.

A trustee may request turnover of the nonexempt portion.

5. Refunds for the Filing Year

A refund for the year in which bankruptcy is filed may include both prepetition and postpetition components.

For example, a debtor filing in July may later receive a refund reflecting withholding from the entire calendar year.

The trustee's interest generally concerns the portion attributable to prepetition property rights.

Determining that portion may require examining payroll records, estimated tax payments, credits, and other information.

The debtor should preserve records supporting the allocation.

6. What About Refundable Tax Credits?

Refundable tax credits can produce payments even when the taxpayer has little or no income tax liability.

Examples include the earned income tax credit and the refundable portion of the child tax credit.

The bankruptcy treatment of these credits depends on applicable law.

Some jurisdictions provide specific exemption protections for particular credits.

Maryland's exemption statutes and relevant decisions must be examined to determine whether such protections apply.

A debtor should not assume that every refundable credit is automatically exempt merely because it is intended to assist lower-income households.

7. Maryland's General Property Exemptions

Maryland Courts and Judicial Proceedings Article § 11-504 provides exemptions that may protect qualifying cash and other property interests.

Depending on the debtor's circumstances, available general exemptions may be applied to a tax refund.

The general $6,000 exemption is now in § 11-504(b)(6). Section 11-504(b)(5) separately protects up to $500 in a qualifying depository account without election, but that amount and the (b)(6) election together cannot exceed $6,000. Section 11-504(f)(1)(i)1 provides an additional bankruptcy exemption of up to $5,000 in personal property; it is distinct from the residential-real-property exemption and may be relevant to a refund, depending on the debtor’s other exemption allocations.

The debtor must consider how much exemption protection has already been used for other assets.

A debtor cannot assume that every exemption can be applied without restriction or that the same exemption amount can be used twice.

8. What If the Refund Exceeds Available Exemptions?

A refund may be only partially exempt.

For example, a debtor expects a $9,000 refund but has only $5,000 in available exemption protection applicable to that asset.

The remaining $4,000 may be available for administration.

The trustee must still consider the economic benefit of collection.

But the debtor should not assume that a relatively modest nonexempt amount will be ignored.

The trustee may request turnover of the nonexempt portion.

9. Joint Tax Returns and Nonfiling Spouses

A married debtor may file bankruptcy individually while the spouses file a joint income tax return.

The resulting refund may represent payments and credits attributable to both spouses.

The bankruptcy estate generally includes the debtor's property interests, not automatically every interest belonging to the nonfiling spouse.

Determining ownership of the refund may require examining Maryland property law, the source of withholding and estimated payments, refundable credits, and applicable federal tax law.

A joint return does not necessarily establish that the entire refund belongs equally to both spouses.

Nor does it necessarily establish that the entire refund belongs to the spouse whose income generated most of the withholding.

The appropriate allocation requires legal analysis.

10. What If Only One Spouse Earned Income?

A joint refund may arise primarily from wages earned by one spouse.

However, the ownership analysis may involve more than simply identifying which spouse received the wages.

Applicable state law, federal tax principles, and the nature of particular credits may affect the result.

The trustee may request both spouses' tax and income records.

The nonfiling spouse may have a basis to assert ownership of part of the refund.

The issue should be resolved before funds are distributed.

11. Can the Trustee Take the Nonfiling Spouse's Share?

The Chapter 7 trustee generally administers property of the debtor's estate.

The trustee does not automatically acquire ownership of property belonging exclusively to a nonfiling spouse.

However, determining each spouse's interest in a joint refund may require factual and legal analysis.

The nonfiling spouse should preserve documentation supporting the claimed ownership interest.

A dispute may require resolution by the bankruptcy court.

12. What If the IRS Applies the Refund to Old Taxes?

A refund may be offset against outstanding tax obligations before payment.

Federal law permits certain offsets under specified circumstances.

The Bankruptcy Code also contains provisions concerning setoff, including § 553.

The effect of bankruptcy on a tax refund offset depends on the relevant obligations, timing, and statutory requirements.

A debtor should not assume that a refund will necessarily be paid in cash merely because the tax return shows an overpayment.

13. Tax Refunds and Domestic Support Obligations

Federal and state tax refund offset programs may apply refunds to qualifying past-due child support or other specified obligations.

Bankruptcy does not automatically eliminate domestic support obligations.

The debtor's rights depend on the nature of the obligation, applicable offset statutes, and bankruptcy law.

A debtor expecting a refund should determine whether any governmental offset is likely.

14. Can the Debtor Spend the Refund Before Filing?

A debtor who receives a refund before filing may use funds for legitimate purposes, including ordinary living expenses and necessary obligations.

However, the debtor must disclose specified prepetition transfers and financial transactions.

Payments to favored creditors may raise preference issues.

Transfers to relatives or transactions for inadequate consideration may raise fraudulent-transfer concerns.

The debtor should not spend or transfer funds merely to conceal assets from creditors or the trustee.

The legal consequences depend on the actual transactions.

15. Why Filing Immediately Before Receiving a Refund Can Be Risky

A debtor may file Chapter 7 shortly before a substantial refund is issued.

The debtor may assume that the refund belongs personally to the debtor because it arrives after filing.

That assumption can be incorrect.

If the right to the refund existed before the petition, the refund may be estate property.

The trustee may request turnover after receipt.

The debtor should not spend the funds without determining the estate's interest.

16. Why Filing After Receiving a Refund Can Also Create Problems

Receiving the refund before filing does not automatically eliminate the bankruptcy issue.

If the debtor retains the funds on the petition date, they generally must be disclosed as cash or bank account assets.

If the debtor spends the funds before filing, the transactions may require disclosure and review.

The filing date should be selected after considering the debtor's overall financial circumstances, not simply the expected refund date.

17. Tax Refunds and the Means Test

A tax refund ordinarily should not be confused with income received for means-test purposes.

The refund may represent repayment of amounts previously withheld from income.

The underlying wages or other income may already have been included in current monthly income when received.

However, refundable credits and other components may require separate treatment.

The debtor should not automatically include the entire refund as new income or exclude every component without analysis.

18. Tax Refunds in Chapter 13

Chapter 13 treats postpetition income and property differently from Chapter 7.

Under § 1306, the Chapter 13 estate generally includes certain earnings and property acquired after filing.

A Chapter 13 plan may require the debtor to contribute tax refunds or otherwise account for them in determining plan payments.

The treatment depends on the confirmed plan, applicable court orders, and the debtor's circumstances.

A debtor should not assume that refunds received during a Chapter 13 plan are automatically available for unrestricted personal use.

19. Can the Trustee Require Turnover After Discharge?

Yes.

A Chapter 7 discharge does not automatically terminate the trustee's authority over estate property.

If a refund belongs to the estate, the trustee may seek turnover even after discharge.

The bankruptcy case may remain open while the trustee waits for the return to be filed and the refund issued.

A debtor should distinguish receiving a discharge from completion of estate administration.

20. What If the Debtor Fails to Disclose the Refund?

Failure to disclose an anticipated or received refund can create serious problems.

The trustee may seek additional records, turnover, or other relief.

Intentional concealment may create grounds for denial or revocation of discharge under § 727.

A debtor should disclose expected refunds and provide updated information when the actual amount becomes known.

The fact that the debtor needs the money for living expenses does not eliminate the disclosure obligation.

21. What Documents Should the Debtor Preserve?

A debtor expecting a refund should retain tax returns, W-2 forms, 1099 forms, pay statements, estimated tax payment records, and refund notices.

For joint returns, records identifying each spouse's withholding and payments may be important.

Bank statements can establish when the refund was received and how the funds were used.

These documents help determine ownership, estate allocation, exemptions, and possible offset issues.

22. Why Tax Refund Planning Should Occur Before Filing

Tax refunds can be substantial assets.

A debtor may qualify for Chapter 7 and possess little nonexempt property other than an anticipated refund.

Proper planning can identify the estate's likely interest and available exemptions before filing.

The debtor may need to compare filing dates, but should also consider garnishments, tax dischargeability, income calculations, and other factors.

The objective is not to hide or improperly dispose of the refund.

It is to understand the legal consequences and avoid an unexpected turnover demand.

Conclusion

A tax refund may become property of the Chapter 7 bankruptcy estate even when it is received after the petition or discharge.

The relevant questions concern when the debtor acquired the right to the refund, what portion is attributable to prepetition activity, who owns the refund, and which exemptions apply.

Joint returns, refundable credits, governmental offsets, and Chapter 13 proceedings create additional considerations.

A debtor expecting a substantial refund should determine its bankruptcy treatment before filing or spending the money.

Careful planning can prevent the unexpected loss of funds needed for ordinary living expenses.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 541 — Property of the bankruptcy estate.

- 11 U.S.C. § 522 — Exemptions.
- 11 U.S.C. § 542 — Turnover of estate property.
- 11 U.S.C. § 553 — Setoff.
- 11 U.S.C. § 727 — Denial and revocation of discharge.
- 11 U.S.C. § 1306 — Chapter 13 estate property.

Maryland law

- Maryland Courts and Judicial Proceedings § 11-504 — Maryland exemptions.

Selected decisions

- *Segal v. Rochelle*, 382 U.S. 375 (1966) — Addresses prepetition roots of tax refund rights under the former Bankruptcy Act.
- *Kokoszka v. Belford*, 417 U.S. 642 (1974) — Addresses tax refunds as property available in bankruptcy under the former statutory framework.
- *In re Barowsky*, 946 F.2d 1516 (10th Cir. 1991) — Discusses allocation of tax refunds attributable to prepetition earnings.
- *In re Montgomery*, 224 F.3d 1193 (10th Cir. 2000) — Addresses earned income tax credits as property of the bankruptcy estate.
- *In re Carlson*, 394 B.R. 491 (8th Cir. BAP 2008) — Addresses ownership allocation of joint tax refunds.
- *In re Law*, 336 B.R. 780 (8th Cir. BAP 2006) — Discusses tax refunds and the bankruptcy estate.

Bankruptcy and Bank Accounts: Frozen Funds, Setoff Rights, Joint Accounts, and Protecting Money Needed for Living Expenses

Belsky Bankruptcy Legal Library | Chapter 7 Assets, Exemptions, and Creditor Remedies

By Alan J. Belsky, Attorney at Law

Filing Bankruptcy Can Create Unexpected Problems With Your Bank Account

Many people file Chapter 7 bankruptcy because they need immediate financial relief. They expect collection calls and wage garnishments to stop and hope to retain enough money to pay rent, purchase groceries, and meet ordinary living expenses.

But a bankruptcy filing can sometimes create an unexpected problem: a bank may restrict access to funds in an account, even though the debtor needs the money for daily necessities.

The legal consequences depend on whether the bank is also a creditor, whether it asserts setoff rights, whether the funds belong to the bankruptcy estate, and whether applicable exemptions protect the balance.

Joint accounts, Social Security deposits, business accounts, and funds received after filing create additional complications.

A debtor should not assume that money in a checking account is automatically protected merely because it is needed for living expenses.

Nor should the debtor assume that filing bankruptcy necessarily authorizes a bank to freeze every account.

Understanding the legal distinctions can prevent unnecessary disruption.

1. Bank Account Balances Are Generally Property of the Bankruptcy Estate

Under 11 U.S.C. § 541(a), the bankruptcy estate generally includes the debtor's legal and equitable interests in property when the petition is filed.

Money held in checking and savings accounts ordinarily is included, subject to applicable exclusions and exemptions.

The debtor must disclose the accounts and balances.

This includes accounts that contain relatively small amounts.

The debtor should also disclose qualifying interests in joint accounts, online financial accounts, and other deposit arrangements.

The fact that the debtor believes funds are exempt does not eliminate the disclosure requirement.

2. The Petition-Date Balance Matters

In an ordinary Chapter 7 case, the debtor's property interests generally are determined as of the petition date.

The balance in an account when bankruptcy is filed can therefore be important.

For example, a debtor who has $7,000 in checking on the petition date may need sufficient exemptions to protect that interest.

The debtor should not assume that funds deposited after filing are automatically treated the same way.

Postpetition wages earned from personal services ordinarily receive different treatment in Chapter 7 under § 541(a)(6), subject to statutory qualifications.

The timing and source of deposits matter.

3. Maryland Exemptions for Cash and Bank Accounts

Maryland Courts and Judicial Proceedings Article § 11-504 provides exemptions that may protect qualifying cash and property interests.

The general cash-or-property exemption of up to $6,000 is in § 11-504(b)(6). The automatic depository-account exemption in (b)(5) is up to $500 and counts toward, rather than adds to, that $6,000 combined limit. The additional bankruptcy personal-property exemption of up to $5,000 under § 11-504(f)(1)(i)1 may also be relevant, subject to the debtor’s allocations and the statutory requirements.

Other statutory protections may apply depending on the source of funds.

For example, Social Security benefits may receive protection under federal law.

The debtor should determine the available exemption amount and whether it has already been allocated to other assets.

The exemption must be properly claimed when required.

4. Why a Bank May Freeze an Account

A bank may restrict access to funds after learning of a bankruptcy for several different reasons.

The bank may assert a right of setoff because the debtor owes money to the institution.

It may be attempting to preserve funds it believes belong to the bankruptcy estate.

It may also be responding to legal process or internal procedures concerning bankruptcy accounts.

These situations are not legally identical.

The bank's rights depend on the nature of the account, the debt, applicable law, and the particular action taken.

A bank does not necessarily acquire an unrestricted right to freeze funds merely because bankruptcy was filed.

5. The Supreme Court's Decision in *Strumpf*

In *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16 (1995), the Supreme Court addressed a bank's temporary administrative hold on a debtor's account.

The bank asserted a right of setoff and temporarily refused to honor withdrawals while seeking relief from the automatic stay.

The Supreme Court held that the temporary refusal to pay was not itself a setoff violating § 362(a)(7) under the circumstances presented.

The decision distinguished a temporary administrative hold from a permanent reduction or satisfaction of the bank's claim through setoff.

The holding does not mean that every bank freeze is automatically permissible.

The bank's asserted rights and conduct must be evaluated under the applicable statutory provisions.

6. What Is Setoff?

Setoff generally involves applying a debt owed by one party against a debt owed by the other.

For example, a debtor may owe a bank $5,000 on an unsecured loan while the bank owes the debtor $3,000 represented by a deposit account.

The bank may assert a right to apply the deposit balance against the loan.

Section 553 generally preserves qualifying setoff rights that exist under applicable nonbankruptcy law, subject to the Bankruptcy Code's limitations.

The statute does not create a setoff right where none otherwise exists.

The existence of mutual obligations and the relevant timing are important.

7. The Requirement of Mutuality

Setoff generally requires mutual debts between the same parties acting in the same capacities.

A bank cannot necessarily offset an individual's account balance against a debt owed by a separate corporation.

Likewise, joint accounts and debts owed by only one account holder may raise questions concerning mutuality.

The precise legal rights depend on account ownership, loan documents, applicable state law, and the Bankruptcy Code.

A debtor should not assume that every account held at the same financial institution is subject to setoff for every debt owed to that institution.

8. The Automatic Stay and Setoff

Section 362(a)(7) generally stays the setoff of a debt owing to the debtor against a claim against the debtor.

A creditor ordinarily must obtain appropriate relief before exercising a stayed setoff right.

However, *Strumpf* recognizes that a temporary administrative hold associated with a claimed setoff may not itself constitute a prohibited setoff.

The creditor's conduct, duration of the hold, and legal basis matter.

A debtor whose account is frozen should determine whether the bank has sought relief from the stay or asserted another statutory basis.

9. What If the Bank Is Also a Credit Card Creditor?

A debtor may maintain a checking account at the same institution that issued a credit card or personal loan.

The bank may assert contractual or statutory rights concerning the account.

However, federal law restricts certain offsets against deposit accounts for consumer credit card debt.

For example, Regulation Z, 12 C.F.R. § 1026.12(d), generally prohibits card issuers from offsetting credit card indebtedness against funds held on deposit, subject to specified exceptions.

The rule's application depends on the particular account and obligation.

A debtor should not assume that every bank debt creates an enforceable setoff right against checking funds.

10. Credit Unions

Credit unions may present additional issues because membership agreements sometimes contain security interests, setoff provisions, or cross-collateralization clauses.

A debtor may owe a credit union money on an automobile loan, credit card, or personal loan while maintaining a deposit account there.

The credit union may assert rights arising from the governing agreements and applicable law.

The debtor should review those agreements before filing.

The fact that an institution is a credit union does not automatically establish that every asserted setoff or lien is enforceable.

11. Joint Bank Accounts

A joint bank account may contain funds belonging to more than one person.

The bankruptcy estate generally includes the debtor's actual legal and equitable interests.

But determining ownership can be complicated.

The names appearing on the account do not necessarily resolve who owns every dollar.

Relevant evidence may include the source of deposits, the account agreement, the parties' intentions, and applicable Maryland law.

A trustee may investigate whether the debtor possesses an ownership interest in funds contributed by another person.

12. Accounts Shared With Adult Children or Parents

A debtor may be listed on a parent's bank account to assist with bill payments or financial management.

Alternatively, a parent may be listed on the debtor's account for convenience.

These arrangements can create uncertainty.

A person listed as an account owner may possess legal rights even when another person contributed all the money.

The bankruptcy treatment depends on applicable law and the actual ownership arrangement.

A debtor should disclose the account and explain the circumstances rather than assuming that the funds are excluded because they were contributed by someone else.

13. Tenancy by the Entirety Bank Accounts

Maryland recognizes tenancy-by-the-entirety ownership in qualifying personal property, including certain bank accounts held by married spouses.

Entireties property generally receives protection against creditors holding claims against only one spouse.

However, the form of ownership must be established.

The fact that spouses maintain a joint account does not automatically resolve whether it is held by the entirety.

The account documents, source of funds, and applicable Maryland law may be relevant.

Joint creditors may also affect the protection.

14. Social Security Deposits

Social Security benefits receive substantial protection under 42 U.S.C. § 407.

The protection may continue after benefits are deposited into a bank account, subject to applicable law and tracing issues.

Federal regulations under 31 C.F.R. Part 212 also provide special procedures protecting certain electronically deposited federal benefits from garnishment.

A debtor should preserve account statements showing the source of deposits.

Commingling Social Security funds with wages or other money may complicate the analysis.

15. Retirement Distributions

Funds held in qualifying retirement accounts may receive substantial protection.

But distributions deposited into ordinary bank accounts can present different questions.

The treatment depends on the account type, applicable exemption law, and whether the funds retain protected status after distribution.

A debtor should not assume that every withdrawal from an IRA or pension remains fully exempt once deposited into checking.

The source and legal character of the funds should be documented.

16. Bank Accounts Containing Business Funds

A self-employed debtor may maintain accounts used for business income and expenses.

A sole proprietor's business account may be treated differently from an account legally owned by a separate corporation or limited liability company.

The debtor's ownership interest in the business may itself become estate property.

A trustee may examine account records, ownership documents, and the source of deposits.

The debtor should not assume that labeling an account as business automatically excludes it from bankruptcy.

17. What If the Bank Freezes Exempt Funds?

A bank freeze can be particularly disruptive when the account contains money protected by applicable exemptions.

The debtor may need to establish the source of funds, assert exemption rights, and seek appropriate relief.

The proper procedure depends on whether the bank is asserting setoff, preserving estate property, or responding to another legal claim.

A debtor should promptly notify bankruptcy counsel.

The fact that funds ultimately may be exempt does not necessarily mean the bank will release them without documentation or court action.

18. Can the Trustee Demand Turnover of Bank Funds?

Under § 542, the trustee may seek turnover of qualifying estate property.

The trustee's rights depend on whether the funds are property of the estate and whether exemptions or other limitations apply.

A bank or other entity holding estate property may have statutory obligations.

However, turnover disputes can involve defenses and procedural requirements.

The debtor should not assume that the trustee can automatically take every dollar held in an account.

19. What About Deposits Made After Filing?

In Chapter 7, wages earned from the debtor's personal services after filing ordinarily are excluded from the estate under § 541(a)(6), subject to statutory qualifications.

Other postpetition deposits may require separate analysis.

For example, a tax refund attributable to prepetition activity may remain estate property even when deposited after filing.

Likewise, proceeds of estate property may retain their estate character.

The date of deposit alone does not necessarily determine ownership.

20. What If the Debtor Has Outstanding Checks?

A debtor may have written checks before filing that have not cleared the account.

The legal consequences depend on the timing and nature of the transaction.

The Supreme Court's decision in *Barnhill v. Johnson*, 503 U.S. 393 (1992), addressed when a transfer by ordinary check occurs for preference purposes.

The Court held that the transfer generally occurs when the bank honors the check, rather than when the check is delivered.

Outstanding checks can therefore create complications when determining petition-date balances and prepetition transfers.

The debtor should disclose relevant transactions accurately.

21. Payment Apps and Online Financial Accounts

Funds held through payment services or online financial platforms may constitute property interests requiring disclosure.

Examples include balances maintained in payment applications, online savings platforms, and other financial accounts.

The legal classification may differ from an ordinary bank deposit.

The debtor should identify the account provider, ownership interest, and balance.

A debtor should not omit funds merely because they are held through a mobile application rather than a traditional bank.

22. What Should Be Done Before Filing?

Before filing Chapter 7, counsel should identify every financial account and determine the approximate petition-date balance.

The review should also identify institutions to which the debtor owes money.

Potential setoff rights, account restrictions, and exemption issues should be evaluated.

The debtor should preserve statements and records showing the source of protected funds.

Any lawful account changes should be considered carefully and disclosed as required.

The objective is to avoid unnecessary interruption of access to money needed for ordinary living expenses while complying fully with bankruptcy law.

23. What If Access to Funds Is Suddenly Lost?

A debtor whose account is frozen should promptly determine which institution imposed the restriction and why.

The bank may be asserting setoff, responding to legal process, or preserving funds it believes belong to the estate.

Counsel should review the account agreement, relevant notices, and applicable bankruptcy provisions.

Depending on the circumstances, relief may require communication with the bank, trustee involvement, a motion in bankruptcy court, or other proceedings.

The debtor should not assume that every freeze is unlawful or that no remedy exists.

Conclusion

Bank accounts can present unexpected problems in Chapter 7 bankruptcy.

The debtor's petition-date balances generally must be disclosed, and nonexempt funds may be administered by the trustee.

Banks may assert setoff rights or impose restrictions under particular circumstances, but those rights are subject to statutory and legal limitations.

Joint accounts, Social Security deposits, retirement distributions, and postpetition funds require separate analysis.

A debtor should identify and evaluate bank accounts before filing rather than assuming that ordinary checking and savings balances are automatically protected.

Careful preparation can reduce the risk of losing access to money needed for daily living.

Related Bankruptcy Cases and Authorities

Federal statutes and regulations

- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 542 — Turnover of estate property.
- 11 U.S.C. § 553 — Setoff.
- 11 U.S.C. § 362 — Automatic stay.
- 42 U.S.C. § 407 — Social Security protection.
- 12 C.F.R. § 1026.12(d) — Restrictions on credit card offsets.
- 31 C.F.R. Part 212 — Garnishment protection for certain federal benefits.

Maryland law

- Maryland Courts and Judicial Proceedings § 11-504 — Maryland exemptions.

Selected decisions

- *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16 (1995) — Addresses temporary administrative holds and setoff rights.
- *City of Chicago v. Fulton*, 592 U.S. 154 (2021) — Addresses retention of property seized before bankruptcy.
- *United States v. Whiting Pools, Inc.*, 462 U.S. 198 (1983) — Addresses turnover and estate property.

- *Barnhill v. Johnson*, 503 U.S. 393 (1992) — Addresses timing of transfers by check.
- *Carpenter v. Ries*, 614 F.3d 930 (8th Cir. 2010) — Addresses protection of Social Security benefits in bankruptcy.
- In re Hamlett, 304 B.R. 737 (Bankr. M.D.N.C. 2003) — Concerns an undisclosed personal-injury claim, reopening, and estate ownership; it is not a bank-account setoff decision. Its equitable exemption-denial discussion predates Law v. Siegel, 571 U.S. 415 (2014).

What Happens to Your Business in Personal Bankruptcy? Sole Proprietorships, LLCs, Corporations, and Personal Guarantees

Belsky Bankruptcy Legal Library | Business Ownership and Individual Bankruptcy

By Alan J. Belsky, Attorney at Law

Filing Personal Bankruptcy Does Not Necessarily Mean Closing Your Business

A business owner facing overwhelming personal debt may hesitate to file bankruptcy because of concern that doing so will automatically close the business, transfer ownership to creditors, or require liquidation of everything the business owns.

The consequences are more complicated.

A sole proprietor, member of a limited liability company, and shareholder of a corporation may possess very different property interests.

In a personal Chapter 7 case, the bankruptcy estate generally includes the debtor's ownership interests in business property or business entities. But the estate does not automatically become the owner of every asset held by a legally separate corporation or LLC.

The distinction is especially important when the debtor operates a profitable business but has personally guaranteed substantial obligations.

A debtor may be eligible to discharge personal business debts while retaining an ongoing business operation. In other circumstances, the Chapter 7 trustee may acquire control over valuable business interests or seek to liquidate assets.

The appropriate analysis begins with the legal structure of the business and the nature of the debtor's ownership.

1. Sole Proprietorships: No Separate Legal Entity

A sole proprietorship generally is not a legal entity separate from its owner.

The proprietor personally owns the business assets and ordinarily is personally responsible for business obligations.

For example, a self-employed contractor may own tools, equipment, inventory, a business checking account, and accounts receivable.

When the contractor files personal Chapter 7 bankruptcy, those property interests generally become part of the bankruptcy estate under 11 U.S.C. § 541.

The trustee may investigate whether the assets are exempt, encumbered, or available for administration.

The fact that the property is used in a business does not automatically protect it.

2. Can a Sole Proprietor Continue Operating After Chapter 7?

Potentially, yes, but the answer depends on the assets and circumstances.

A debtor may continue earning income through personal services after filing.

Under § 541(a)(6), earnings from services performed by an individual debtor after commencement of a Chapter 7 case generally are excluded from the estate, subject to statutory qualifications.

However, business equipment, inventory, accounts receivable, and other prepetition property may belong to the estate.

The trustee may have authority over those assets.

A debtor should not assume that continuing business operations permits unrestricted use or sale of estate property.

3. Limited Liability Companies

An LLC ordinarily is a legal entity separate from its members.

The LLC generally owns its own assets.

A member's personal bankruptcy does not automatically transfer title to every LLC asset into the member's bankruptcy estate.

Instead, the debtor's membership interest generally becomes estate property.

That interest may include economic rights, voting rights, management rights, or other contractual and statutory rights, depending on the operating agreement and applicable law.

The trustee may investigate the value and extent of those rights.

4. Single-Member LLCs

A single-member LLC can present particularly significant bankruptcy risks.

When the debtor is the sole member, the trustee may acquire rights associated with the entire membership interest.

Depending on applicable law and the operating agreement, the trustee may be able to exercise substantial control over the LLC.

The trustee may consider whether the business can be sold, liquidated, or otherwise administered for creditors.

A debtor should not assume that creating a single-member LLC makes the business immune from personal bankruptcy administration.

5. Multi-Member LLCs

A multi-member LLC presents additional questions.

The operating agreement may restrict transfers of management rights or admission of new members.

Applicable Maryland LLC law may distinguish between economic interests and governance rights.

Bankruptcy law may affect the enforceability of certain transfer restrictions.

The trustee's rights depend on the debtor's actual interest and the governing legal provisions.

A trustee may possess the right to receive distributions without necessarily acquiring every management power held by the debtor before filing.

The issue requires examination of the operating agreement and applicable law.

6. Corporations

A corporation is generally a separate legal entity.

A shareholder's personal bankruptcy ordinarily brings the shareholder's stock or ownership interest into the bankruptcy estate.

The corporation's assets do not automatically become property of the shareholder's estate merely because the shareholder files bankruptcy.

However, the trustee may exercise rights associated with the stock, including voting or sale rights where applicable.

If the debtor owns all corporate shares, the trustee may possess substantial practical control through the ownership interest.

The corporate form therefore does not necessarily prevent disruption of the business.

7. Personal Guarantees of Business Debts

Business owners frequently guarantee corporate or LLC obligations.

A lender may require the owner to sign a personal guarantee for a business loan, commercial lease, credit line, or equipment financing agreement.

The guarantee creates potential personal liability separate from the business entity's obligation.

A personal Chapter 7 discharge may eliminate the owner's liability on a qualifying guarantee.

But the business entity may remain liable.

The creditor may also retain liens against business collateral.

Discharging the owner's personal guarantee does not automatically discharge the separate corporation or LLC.

8. What Happens to Business Credit Cards?

The treatment depends on who is legally obligated.

A credit card issued for business purposes may be an obligation of the owner, the business entity, or both.

A card bearing the business name does not necessarily establish that the business alone is responsible.

The account agreement and any personal guarantee must be examined.

An individual's liability may be dischargeable in Chapter 7, subject to applicable exceptions.

The business entity's separate obligation ordinarily is not discharged through the owner's personal bankruptcy.

9. Business Debts and the Chapter 7 Means Test

The classification of business debts can materially affect Chapter 7 eligibility.

Section 707(b) generally applies to individual debtors whose debts are primarily consumer debts.

Business-related obligations may constitute nonconsumer debts.

A debtor whose obligations are primarily nonconsumer debts generally is not subject to the ordinary § 707(b) means-test presumption.

For example, a former business owner may have substantial personal guarantees arising from commercial loans and leases.

The classification of those obligations may determine whether the means test applies.

The analysis concerns the purpose of the debts, not simply whether the debtor was self-employed.

10. Business Bank Accounts

A sole proprietor's business checking account generally represents property owned by the individual debtor.

The account balance ordinarily must be disclosed.

For an LLC or corporation, the account generally belongs to the entity.

However, the trustee may investigate the debtor's ownership interest, distributions, loans, and transactions involving the account.

Commingling personal and business funds can complicate the analysis.

A debtor should not assume that an account labeled business is automatically excluded from the personal bankruptcy estate.

11. Accounts Receivable

Accounts receivable may be valuable business assets.

A sole proprietor may have earned fees or completed work before filing but not yet received payment.

The right to collect those receivables may become estate property.

For example, a consultant may have completed $25,000 in work before filing Chapter 7 but not yet invoiced the clients.

The receivables may belong to the estate even though payment is received afterward.

The analysis can be more complicated when compensation relates partly to prepetition work and partly to postpetition personal services.

12. Inventory and Equipment

Business inventory and equipment may become property of the estate when personally owned by the debtor.

The trustee may examine their value, liens, and available exemptions.

For example, a contractor may own tools, machinery, vehicles, and materials.

Some property may qualify for exemption under Maryland law.

Other assets may be nonexempt.

The debtor should not assume that property is exempt merely because it is essential to earning a living.

13. Tools of the Trade

Maryland Courts and Judicial Proceedings Article § 11-504 provides exemptions for certain qualifying property used in an occupation or profession.

The scope and amount of protection depend on the statutory language.

Tools, books, instruments, and other occupational property may receive protection in appropriate circumstances.

However, expensive commercial equipment, inventory, and business vehicles may require separate analysis.

The debtor should identify the particular property and its value.

14. Business Vehicles

A vehicle used in a business may be personally owned, leased, or titled to a separate entity.

The bankruptcy consequences depend on ownership and financing.

A personally owned vehicle generally becomes estate property, subject to liens and exemptions.

A vehicle titled to an LLC ordinarily belongs to the entity, although the debtor's membership interest may have value.

The lender's rights under the loan documents must also be considered.

15. Commercial Leases

A business owner may be personally liable on a commercial lease.

If the business is a sole proprietorship, the lease may be an obligation of the debtor personally.

If an LLC or corporation signed the lease, the debtor may still be liable under a personal guarantee.

Section 365 governs executory contracts and unexpired leases in bankruptcy.

The trustee may possess rights concerning qualifying contracts or leases that belong to the estate.

The landlord's rights and the business entity's obligations require separate analysis.

16. What If the Business Is Profitable?

A profitable business may present substantial value to the bankruptcy estate.

The trustee may investigate whether the debtor's ownership interest can be sold or otherwise administered.

For example, a debtor who owns all shares of a profitable corporation may possess stock with significant value.

Even if the corporation's assets are not directly estate property, the stock may be valuable.

A debtor should not assume that the trustee will disregard the business because it provides the debtor's livelihood.

17. What If the Business Has No Value?

A business may have little or no realizable value because of debts, declining revenue, personal-service dependence, or other factors.

For example, a professional practice may depend almost entirely on the owner's personal services and reputation.

The trustee may determine that the ownership interest has little value apart from the debtor's future work.

However, accounts receivable, equipment, contracts, goodwill, or other assets may still have value.

The business should be evaluated realistically rather than assigned a nominal value without investigation.

18. Professional Practices

Professional practices can present special issues.

A physician, attorney, accountant, or other licensed professional may operate through a corporation, LLC, or sole proprietorship.

The trustee's ability to administer ownership interests may be affected by professional licensing laws, restrictions on ownership, client relationships, confidentiality obligations, and other regulatory requirements.

For example, a law practice may possess accounts receivable and other assets, but client files and ongoing representation involve professional duties that cannot be treated as ordinary commercial inventory.

The debtor's professional obligations remain relevant despite bankruptcy.

19. Pending Business Lawsuits

A sole proprietor's claims arising before bankruptcy may become property of the estate.

The trustee may have authority to prosecute or settle those claims.

A corporation or LLC may own its own causes of action.

The shareholder's personal bankruptcy does not automatically transfer those claims into the individual's estate.

However, the value of the debtor's ownership interest may depend on the entity's litigation.

The ownership of each claim must be identified.

20. Recent Transfers of Business Assets

Transfers of business assets before bankruptcy may raise preference or fraudulent-transfer issues.

For example, a sole proprietor may repay a family loan, transfer equipment to a relative, or sell inventory for less than reasonably equivalent value.

The trustee may investigate the transactions under §§ 547 and 548.

Section 544 may permit reliance on applicable state-law remedies.

The debtor should disclose significant transfers and preserve documentation.

21. Business Tax Debts

Business owners may face personal liability for certain taxes.

For example, qualifying trust fund payroll taxes may remain nondischargeable.

A business entity's tax liability does not automatically become the owner's personal liability, but responsible-person provisions and other laws may create personal obligations.

The debtor should distinguish income taxes, sales taxes, withholding taxes, and other liabilities.

The bankruptcy treatment depends on the nature of the tax and the debtor's legal responsibility.

22. Chapter 13 for Self-Employed Debtors

Chapter 13 may be available to qualifying self-employed individuals with regular income.

A debtor operating a business may propose a repayment plan funded through ongoing earnings.

Chapter 13 generally permits the debtor to retain property while satisfying plan requirements.

However, business income may fluctuate, and the plan must be feasible.

The debtor must also satisfy applicable debt limits and other eligibility requirements.

For some business owners, Chapter 13 may offer greater continuity than Chapter 7.

23. Chapter 11 and Subchapter V

Some business owners may require relief under Chapter 11 rather than Chapter 7 or Chapter 13.

Subchapter V of Chapter 11 provides a specialized framework for qualifying small business debtors.

Eligibility depends on statutory requirements, including debt limits and the nature of business activity.

The debtor may seek to reorganize business obligations while continuing operations.

Subchapter V is not automatically available to every individual who owns a business.

The appropriate chapter depends on the debtor's circumstances and objectives.

24. Why Business Ownership Must Be Evaluated Before Filing

A business owner should not file personal Chapter 7 without understanding the ownership structure, value of business interests, personally guaranteed obligations, and consequences for ongoing operations.

The trustee may acquire rights that materially affect the business.

A debtor may discharge substantial personal obligations but still face disruption of the enterprise that generates future income.

The analysis should consider the business's assets, liabilities, cash flow, contracts, ownership agreements, and applicable exemptions.

Conclusion

Personal bankruptcy does not automatically require every business owner to close the business.

But the consequences depend heavily on whether the debtor operates as a sole proprietor, LLC member, or corporate shareholder.

A sole proprietor's business assets generally are personally owned and may become estate property.

An LLC or corporation ordinarily owns its assets separately, but the debtor's ownership interest may be administered by the trustee.

Personal guarantees can also create dischargeable individual obligations while leaving the business entity liable.

The central question is not merely whether the debtor owns a business, but what property rights the debtor possesses and how bankruptcy will affect the operation's continuing value.

Careful planning can help determine whether Chapter 7, Chapter 13, Chapter 11, or a nonbankruptcy alternative is most appropriate.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 704 — Chapter 7 trustee duties.
- 11 U.S.C. § 365 — Executory contracts and unexpired leases.
- 11 U.S.C. § 707(b) — Consumer-debt means-test provisions.
- 11 U.S.C. § 547 — Preferential transfers.
- 11 U.S.C. § 548 — Fraudulent transfers.

- 11 U.S.C. § 109 — Eligibility for bankruptcy relief.
- 11 U.S.C. § 1182 — Definitions relevant to Subchapter V.

Maryland law

- Maryland Courts and Judicial Proceedings § 11-504 — Property exemptions.
- Maryland Corporations and Associations Article — Corporate and LLC ownership provisions.

Selected decisions

- *In re Albright*, 291 B.R. 538 (Bankr. D. Colo. 2003) — Addresses a Chapter 7 trustee's rights concerning a debtor's single-member LLC interest.
- In re Modanlo, 412 B.R. 715 (Bankr. D. Md. 2006) — Addresses a Chapter 11 trustee's governance rights in a single-member Delaware LLC. The holding depends on the entity's governing law and circumstances; it is not a universal Maryland LLC rule.
- *United States v. Whiting Pools, Inc.*, 462 U.S. 198 (1983) — Addresses the scope of estate property and turnover.
- *Marrama v. Citizens Bank of Massachusetts*, 549 U.S. 365 (2007) — Addresses bad faith and conversion between bankruptcy chapters.

Bankruptcy and Personal Guarantees: When Business Owners, Spouses, and Family Members Remain Liable for Someone Else's Debt

Belsky Bankruptcy Legal Library | Business Debt, Cosigners, and Discharge

By Alan J. Belsky, Attorney at Law

Bankruptcy May Eliminate the Guarantor's Liability Without Eliminating the Underlying Debt

Business owners, spouses, parents, and other family members frequently agree to become personally responsible for debts incurred by someone else.

A business owner may guarantee a commercial lease or business loan. A parent may cosign an automobile loan. A spouse may become jointly obligated on a credit account.

When financial problems arise, the guarantor may discover that the creditor can pursue payment even though the guarantor never received the borrowed money.

Chapter 7 bankruptcy may discharge qualifying personal guarantee obligations. But the discharge ordinarily protects only the debtor who receives it.

The principal borrower, other guarantors, and nonfiling cosigners may remain liable.

Understanding the difference between the underlying obligation and the guarantor's separate liability is essential before filing bankruptcy.

1. What Is a Personal Guarantee?

A personal guarantee is an agreement under which one person assumes responsibility for another person's obligation.

For example, a lender may extend credit to an LLC only if the owner personally guarantees repayment.

The LLC is the principal borrower.

The owner becomes a guarantor.

Depending on the agreement, the creditor may be entitled to pursue the guarantor when the borrower defaults.

Some guarantees permit direct enforcement without first exhausting remedies against the principal borrower.

The precise rights depend on the agreement and applicable law.

2. Why Lenders Require Guarantees

An LLC or corporation ordinarily is a separate legal entity.

Its owners generally are not personally liable for every entity obligation merely because they own the business.

A personal guarantee gives the creditor an additional source of repayment.

For example, a commercial landlord may require the owner of a newly formed LLC to guarantee the lease.

If the LLC fails to pay rent, the landlord may pursue the owner under the guarantee.

The existence of limited liability therefore does not necessarily protect an owner who voluntarily assumes a separate contractual obligation.

3. Can a Personal Guarantee Be Discharged in Chapter 7?

Ordinarily, yes, if the guarantee creates a dischargeable obligation and no statutory exception applies.

The fact that the debt originated as a business obligation does not automatically prevent discharge.

For example, an individual may personally guarantee a $150,000 business loan.

If the business fails and the individual files Chapter 7, the guarantee obligation may be discharged.

However, the creditor may assert nondischargeability under § 523 if the obligation arose through qualifying fraud or other conduct described in the statute.

The nature of the underlying transaction and the debtor's conduct matter.

4. The Business Entity Remains Liable

An individual's bankruptcy discharge does not ordinarily discharge a separate LLC or corporation.

Section 524(e) provides that discharge of the debtor does not affect the liability of another entity for the same debt.

Example

An LLC owes a bank $100,000.

The owner personally guarantees the loan.

The owner files Chapter 7 and receives a discharge of the guarantee obligation.

The bank may remain entitled to pursue the LLC and enforce valid liens against business collateral.

The owner's discharge does not automatically eliminate the LLC's separate liability.

5. Other Guarantors Remain Liable

A loan may be guaranteed by several individuals.

For example, three business partners may jointly guarantee a commercial loan.

If one partner receives a Chapter 7 discharge, the creditor may continue pursuing the other guarantors, subject to applicable law.

The discharge ordinarily protects the filing debtor personally.

It does not automatically reduce the creditor's contractual rights against nonfiling guarantors.

The remaining guarantors may face substantial exposure.

6. Cosigning Versus Guaranteeing

The terms *cosigner* and *guarantor* are sometimes used interchangeably, but the legal obligations may differ.

A cosigner may be directly obligated as a borrower.

A guarantor may have a separate contractual obligation to answer for another person's debt.

Some guarantees are unconditional, while others impose requirements before enforcement.

The document's actual language controls.

A debtor should not assume that the label used by the creditor determines the legal consequences.

7. Parents Who Cosign Automobile Loans

Parents frequently cosign vehicle loans for adult children.

If the child files Chapter 7, the parent may remain responsible for the debt.

The lender may continue collecting from the parent according to the loan agreement.

The automobile may also remain subject to the lender's security interest.

A Chapter 7 discharge of the child's personal liability does not automatically eliminate the parent's obligation.

8. Spouses and Joint Debts

Married individuals may be jointly liable for mortgages, automobile loans, credit cards, or other obligations.

If only one spouse files Chapter 7, the nonfiling spouse ordinarily remains liable on jointly owed debts.

The filing spouse's discharge does not automatically protect the other spouse.

However, the nonfiling spouse is not necessarily liable for every debt incurred during the marriage.

The actual account agreements, applicable Maryland law, and nature of the obligation must be examined.

9. Divorce Does Not Release a Guarantor

A divorce decree may allocate responsibility for a joint debt.

For example, a settlement agreement may require one spouse to pay a vehicle loan and hold the other harmless.

The creditor ordinarily retains its contractual rights unless it agrees to release the other spouse.

The divorce agreement may create a separate reimbursement or indemnification obligation between the former spouses.

That obligation may receive different bankruptcy treatment from the underlying loan.

10. Commercial Lease Guarantees

Commercial landlords frequently require personal guarantees.

A business owner may remain liable for rent, damages, and other obligations after the business closes.

The scope of liability depends on the lease and guarantee.

A personal Chapter 7 discharge may eliminate qualifying liability under the guarantee.

However, the business entity may remain obligated.

The landlord may also possess rights concerning security deposits, collateral, or other parties.

11. Continuing Guarantees

Some guarantees cover future advances or obligations incurred after the agreement is signed.

These are sometimes called continuing guarantees.

A debtor who files bankruptcy may need to determine whether the guarantee covers prepetition debts, postpetition advances, or both.

The bankruptcy discharge generally concerns qualifying prepetition obligations.

Postpetition contractual conduct may create new liabilities under applicable law.

The timing and scope of the guarantee must be examined.

12. Secured Guarantees

A guarantor may pledge property as collateral for another person's debt.

For example, a parent may mortgage personally owned real estate to secure a child's business loan.

The guarantor's bankruptcy discharge may eliminate qualifying personal liability, but the creditor may retain a valid lien against the pledged property.

The distinction between personal liability and in rem rights is important.

A debtor should not assume that discharging a guarantee automatically releases collateral securing it.

13. Contribution and Indemnification Rights

A guarantor who pays a debt may acquire rights against the principal borrower or other obligated parties.

These rights may arise through contract, equitable contribution, reimbursement, or subrogation.

The bankruptcy treatment depends on the circumstances.

A guarantor's claim against a debtor may be contingent or unmatured when bankruptcy is filed.

Section 502(e) addresses certain reimbursement and contribution claims.

Section 509 governs specified subrogation rights.

These provisions can affect whether and when a guarantor may assert a claim in the bankruptcy case.

14. What If the Guarantor Pays After the Borrower Files Bankruptcy?

A guarantor may be required to pay a creditor after the principal borrower files bankruptcy.

The guarantor may then seek reimbursement from the borrower.

However, the borrower's discharge may affect the enforceability of that reimbursement claim.

The guarantor's rights depend on the timing, nature of the obligation, and applicable bankruptcy provisions.

The guarantor should not assume that paying the creditor after the borrower's discharge creates a new collectible debt against the borrower.

15. Chapter 7 Does Not Provide a General Codebtor Stay

The automatic stay under § 362 generally protects the debtor and estate property.

It does not ordinarily provide broad protection to nonfiling guarantors or cosigners.

A creditor may therefore be able to pursue a nonfiling guarantor while the principal borrower is in Chapter 7.

The result may differ when the creditor's proposed action affects estate property or implicates another applicable legal restriction.

But the mere existence of a Chapter 7 case does not automatically stay collection against every person liable on the debt.

16. Chapter 13's Codebtor Stay

Section 1301 provides a limited codebtor stay in qualifying Chapter 13 cases.

The provision generally protects certain individuals liable with the debtor on consumer debts.

The protection is subject to statutory exceptions and relief provisions.

For example, a parent who cosigned a consumer automobile loan may receive temporary protection while the debtor performs a Chapter 13 plan.

However, the stay generally does not extend to ordinary commercial guarantees merely because the debtor files Chapter 13.

The debt's consumer or business character matters.

17. When Can a Creditor Obtain Relief From the Codebtor Stay?

Under § 1301(c), a creditor may seek relief from the Chapter 13 codebtor stay under specified circumstances.

These include situations involving consideration received by the codebtor, the plan's failure to pay the claim, or irreparable harm to the creditor's interest.

The statutory requirements must be established.

A debtor should not assume that the codebtor stay permanently eliminates the cosigner's liability.

The protection generally is temporary and tied to the Chapter 13 proceeding.

18. Business Guarantees and the Means Test

Business-related guarantees can affect whether a debtor's obligations are primarily consumer debts.

Under § 101(8), consumer debt generally means debt incurred primarily for personal, family, or household purposes.

A guarantee of a commercial loan may constitute nonconsumer debt.

The classification depends on the purpose and circumstances of the obligation.

A debtor whose debts are primarily nonconsumer obligations generally is not subject to the ordinary § 707(b) means-test presumption.

The presence of substantial business guarantees may therefore materially affect Chapter 7 eligibility.

19. What If the Guarantee Was Obtained Through Fraud?

A creditor may challenge dischargeability when a guarantee obligation arose through conduct satisfying § 523(a)(2), (4), or another applicable exception.

For example, a lender may allege that the guarantor knowingly made materially false representations to obtain credit.

The creditor must establish the statutory requirements.

A business failure or inability to repay does not automatically establish fraud.

The distinction between breach of contract and fraudulent conduct remains important.

20. What If the Principal Borrower Is Already in Bankruptcy?

A guarantor may face collection because the principal borrower filed bankruptcy.

The guarantor's options depend on the amount owed, available defenses, collateral, and financial circumstances.

The guarantor may negotiate with the creditor, assert contractual defenses, pursue reimbursement rights, or consider personal bankruptcy.

The principal borrower's bankruptcy does not automatically require the guarantor to file.

The appropriate response should be based on the guarantor's actual exposure.

21. Can the Creditor Collect the Entire Debt From One Guarantor?

Depending on the agreement, yes.

Some obligations are joint and several.

A creditor may be entitled to pursue one obligated party for the full enforceable balance, subject to applicable law.

That party may have contribution or reimbursement rights against others.

But those rights may be of limited practical value if the other parties are insolvent or have received bankruptcy discharges.

A guarantor should not assume that liability is limited to a proportional share merely because several people signed.

22. Why Guarantee Documents Must Be Reviewed Before Filing

A debtor may not remember signing a guarantee years earlier.

Commercial financing documents can contain broad guarantee language, continuing obligations, waivers, and collateral provisions.

The attorney should obtain the actual agreements.

Relevant questions include the identity of the principal borrower, the scope of guaranteed obligations, collateral, termination provisions, and whether the guarantee remains enforceable.

A creditor's assertion that the debtor guaranteed a debt should not be accepted without reviewing the contractual basis.

23. Why Personal Guarantees Can Make Chapter 7 Attractive

A former business owner may owe substantial obligations arising from failed commercial ventures.

The debts may be unsecured personal guarantees, and the debtor may have limited nonexempt assets.

If the obligations are dischargeable, Chapter 7 may provide significant relief.

Moreover, when the debts are primarily nonconsumer obligations, the ordinary consumer means-test presumption may not apply.

However, the debtor must still disclose all assets, evaluate recent transactions, and consider other grounds for dismissal or denial of discharge.

Conclusion

Personal guarantees can expose business owners, spouses, parents, and other individuals to substantial debts incurred by someone else.

Chapter 7 may discharge a qualifying guarantor's personal liability, but the underlying borrower and other guarantors ordinarily remain liable.

Valid liens may also survive.

Chapter 13 provides limited codebtor protection for certain consumer debts, but it does not automatically protect commercial guarantors.

Before filing bankruptcy, the debtor should determine precisely who owes each debt, who guaranteed it, what collateral secures it, and which obligations the bankruptcy discharge can eliminate.

Those distinctions can determine whether bankruptcy provides meaningful relief and whether nonfiling family members or business associates remain exposed.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 101(8) — Definition of consumer debt.
- 11 U.S.C. § 362 — Automatic stay.
- 11 U.S.C. § 502(e) — Certain reimbursement and contribution claims.
- 11 U.S.C. § 509 — Subrogation.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 524(e) — Effect of discharge on liability of other entities.
- 11 U.S.C. § 707(b) — Consumer-debt abuse provisions.
- 11 U.S.C. § 1301 — Chapter 13 codebtor stay.

Maryland law

- Maryland Commercial Law Article — Applicable provisions concerning commercial obligations and secured transactions.
- Maryland Courts and Judicial Proceedings Article — Relevant enforcement and judgment provisions.

Selected decisions

- *United States v. Stribling Flying Service, Inc.*, 734 F.2d 221 (5th Cir. 1984) — Addresses guarantor liability and bankruptcy-related issues.
- *In re Zale Corp.*, 62 F.3d 746 (5th Cir. 1995) — Discusses the effect of bankruptcy proceedings on claims involving nondebtor parties.
- *In re Western Real Estate Fund, Inc.*, 922 F.2d 592 (10th Cir. 1990) — Addresses limitations on extending discharge protections to nondebtors.
- In re Lockard, 884 F.2d 1171 (9th Cir. 1989) — Addresses enforcement against a nondebtor surety in a Chapter 11 setting and limitations on extending bankruptcy protections to that party; it is not a Chapter 13 § 1301 decision.

- *In re Kestell*, 99 F.3d 146 (4th Cir. 1996) — Discusses abuse of bankruptcy relief and debtor conduct.

Bankruptcy and Foreclosure in Maryland: When Filing Stops a Sale, When It Does Not, and How Chapter 13 Can Save a Home

Belsky Bankruptcy Legal Library | Homeownership, Foreclosure, and Bankruptcy Protection

By Alan J. Belsky, Attorney at Law

Bankruptcy Can Stop a Foreclosure Sale, but Timing Is Critical

For a homeowner facing foreclosure, bankruptcy may provide immediate protection against the loss of a residence.

Under 11 U.S.C. § 362, filing a bankruptcy petition ordinarily triggers an automatic stay that prohibits many collection and foreclosure activities.

But the stay is not unlimited.

The timing of the filing, status of the foreclosure proceeding, prior bankruptcy cases, and nature of the debtor's ownership interest can determine whether bankruptcy will actually prevent a sale.

Chapter 7 may provide temporary relief, but it ordinarily does not furnish a mechanism for curing substantial mortgage arrears over several years.

Chapter 13 can provide a more effective solution for a homeowner who has sufficient income to maintain ongoing mortgage payments while curing arrears through a repayment plan.

A homeowner should not assume that filing bankruptcy at the last moment will always save the property.

1. How Foreclosure Works in Maryland

Maryland primarily uses a judicially supervised foreclosure process conducted under the Maryland Rules and applicable statutes.

Foreclosure proceedings involving deeds of trust commonly are initiated through an order to docket or complaint to foreclose.

The secured party or substitute trustees must satisfy applicable notice and procedural requirements.

Maryland law also provides opportunities for certain homeowners to request foreclosure mediation and assert defenses.

The process may involve notices of intent to foreclose, filing of the foreclosure action, mediation procedures, advertisement of sale, auction, ratification, and distribution of proceeds.

The precise requirements depend on the property, loan, and applicable law.

2. The Automatic Stay

Section 362(a) generally stays actions to enforce prepetition liens against property of the bankruptcy estate.

A foreclosure sale ordinarily cannot proceed while the automatic stay applies unless the creditor obtains relief or an exception applies.

The stay generally arises automatically when a qualifying bankruptcy petition is filed.

The debtor ordinarily does not need a separate court order to activate it.

However, repeat filings and other statutory provisions can limit the stay.

The debtor should ensure that the foreclosure attorney and substitute trustees receive prompt notice of the bankruptcy filing.

3. What If Bankruptcy Is Filed the Day Before the Sale?

A qualifying bankruptcy filing before the foreclosure sale may stop the sale if the automatic stay applies.

However, last-minute filings are risky.

The debtor must satisfy filing requirements, and the petition must actually be filed before the legally significant event.

Electronic filing delays, incomplete documents, repeat-filing restrictions, or uncertainty about the sale's status can create problems.

The homeowner should not assume that merely contacting an attorney or preparing documents stops foreclosure.

The stay generally depends on an effective bankruptcy filing.

4. What If Bankruptcy Is Filed After the Auction?

The answer becomes more complicated.

Maryland foreclosure law distinguishes the foreclosure auction from later judicial ratification and conveyance.

A successful foreclosure sale may create significant equitable rights in the purchaser before ratification.

A debtor who files bankruptcy after the auction may have substantially fewer options for retaining the property.

The bankruptcy court must consider the debtor's remaining property interests under Maryland law.

The debtor should not assume that filing before ratification automatically restores the ability to cure the mortgage or undo the sale.

5. The Significance of Maryland's Foreclosure Sale

Maryland decisions recognize that a foreclosure purchaser may acquire equitable rights at the auction, subject to ratification and other legal requirements.

In *Simard v. White*, 383 Md. 257, 859 A.2d 168 (2004), the Supreme Court of Maryland discussed the legal significance of foreclosure sale and ratification.

The precise effect of a bankruptcy filing between auction and ratification requires careful analysis.

Federal bankruptcy law generally looks to state law to determine property interests.

A homeowner should obtain legal advice before assuming that a post-auction bankruptcy filing will save the home.

6. Chapter 7 and Foreclosure

Chapter 7 generally provides temporary protection through the automatic stay.

However, it does not ordinarily permit a debtor to cure substantial mortgage arrears through a multiyear plan.

A lender may seek relief from the stay under § 362(d).

If relief is granted, foreclosure may resume.

A debtor who cannot cure the default or otherwise resolve the mortgage may eventually lose the property despite receiving a discharge of personal liability.

Chapter 7 may nevertheless be useful when the debtor wishes to surrender the home or obtain time to address other financial obligations.

7. Chapter 13 and Mortgage Arrears

Chapter 13 may permit a debtor to cure mortgage arrears through a repayment plan.

Under § 1322(b)(5), a plan may provide for curing defaults within a reasonable time while maintaining ongoing payments on certain long-term debts.

The debtor generally must have sufficient regular income to fund the plan.

Example

A homeowner is $36,000 behind on mortgage payments.

The homeowner has returned to stable employment and can afford the regular mortgage payment.

A Chapter 13 plan may permit repayment of the arrears over the applicable plan period.

If the debtor can maintain ongoing payments and satisfy the plan's other requirements, Chapter 13 may provide a realistic opportunity to retain the residence.

8. The Right to Cure Before Foreclosure Sale

Section 1322(c)(1) provides that a default concerning a lien on the debtor's principal residence may be cured until the residence is sold at a foreclosure sale conducted in accordance with applicable nonbankruptcy law.

The meaning of the statutory cutoff has generated litigation.

The interaction between federal law and Maryland foreclosure procedures must be examined carefully.

The debtor should not assume that the right to cure necessarily continues until final ratification or recording of a deed.

Maryland bankruptcy decisions apply the auction cutoff: a petition filed after the auctioneer's gavel ordinarily comes too late to cure the mortgage under § 1322(c)(1), even before ratification. In re Schweiger, 587 B.R. 469 (Bankr. D. Md. 2018), explains that cure is precluded after a sale conducted in accordance with Maryland law unless the state-court process restores the debtor's equity of redemption. Fair v. Wilmington Savings Fund Society, No. 8:25-cv-00577 (D. Md.), likewise rejects an assumed post-sale right to cure. A potentially defective sale and remaining interests require separate analysis; the later ratification date is not an automatic extension of the federal cure right.

The safest approach is to evaluate bankruptcy relief before the scheduled auction.

9. What If the Mortgage Has Matured?

A mortgage that has reached its contractual maturity date may present different Chapter 13 issues from an ordinary long-term mortgage with arrears.

Section 1322(c)(2) permits specified treatment of certain home-secured claims when the final payment under the original payment schedule becomes due before the final payment under the Chapter 13 plan.

The Fourth Circuit addressed the scope of this provision in *Hurlburt v. Black*, 925 F.3d 154 (4th Cir. 2019) (en banc).

The court held that § 1322(c)(2) permits modification of qualifying claims, including bifurcation under § 506(a).

The provision can be important for certain short-term or matured mortgages.

10. Motions for Relief From the Automatic Stay

A mortgage lender may seek relief from the automatic stay under § 362(d).

Grounds may include lack of adequate protection, absence of equity combined with lack of necessity for an effective reorganization, or other statutory grounds.

The debtor may oppose the motion.

The bankruptcy court determines whether relief is appropriate.

In Chapter 13, failure to maintain postpetition mortgage payments may provide a basis for stay relief.

A confirmed plan does not guarantee that foreclosure will remain prohibited regardless of future defaults.

11. Adequate Protection

Adequate protection concerns the secured creditor's interest in collateral.

The lender may argue that its collateral position is deteriorating because payments are not being made, insurance is lacking, or property value is declining.

The debtor may respond with evidence concerning equity, payments, insurance, and other circumstances.

The concept does not necessarily require immediate payment of every prepetition arrearage.

The relevant statutory provisions and facts control.

12. What If the Debtor Has No Equity?

A homeowner may owe more than the property is worth.

In Chapter 7, the absence of equity may reduce the trustee's incentive to administer the residence.

But it does not eliminate the mortgage lender's lien.

The lender may still seek relief from the stay and pursue foreclosure.

In Chapter 13, the debtor's ability to retain the home may depend on maintaining payments and curing arrears, rather than possessing substantial equity.

13. What If the Debtor Has Substantial Equity?

A homeowner with substantial equity may face a different problem.

In Chapter 7, the trustee may investigate whether nonexempt equity can be administered.

Maryland's increased $125,000 residential-property exemption provides significant protection for qualifying homeowners.

However, equity exceeding available exemptions may create liquidation risk.

Chapter 13 may allow the debtor to retain the home while satisfying the liquidation-value requirement.

The debtor should not assume that substantial equity makes Chapter 7 automatically safe.

14. The Mortgage Lien Usually Survives Discharge

A Chapter 7 discharge generally eliminates qualifying personal liability on the mortgage note.

But the mortgage lien ordinarily remains enforceable against the property.

The lender may therefore foreclose after the stay terminates, even though the debtor is no longer personally liable for the discharged obligation.

This distinction is important when deciding whether to retain or surrender the home.

The debtor should not assume that discharge eliminates the mortgage.

15. What Happens to a Deficiency After Foreclosure?

A deficiency arises when foreclosure proceeds are insufficient to satisfy the secured debt and applicable charges.

The lender's ability to obtain a deficiency judgment depends on Maryland law and the circumstances of the foreclosure.

A qualifying prepetition personal deficiency obligation may be discharged in Chapter 7.

However, valid liens and certain postpetition obligations require separate analysis.

A debtor should distinguish the lender's right to foreclose from the lender's right to collect a deficiency personally.

16. Second Mortgages and Home Equity Lines

A homeowner may have a first mortgage, second mortgage, or home equity line of credit.

The bankruptcy treatment depends on the chapter, lien priority, property value, and applicable law.

Chapter 7 generally does not permit a debtor to eliminate an otherwise valid junior mortgage lien merely because the property is worth less than the first mortgage balance.

In *Bank of America, N.A. v. Caulkett*, 575 U.S. 790 (2015), the Supreme Court held that a wholly underwater junior mortgage lien could not be voided under § 506(d) in the Chapter 7 circumstances presented.

Chapter 13 may provide different options for certain wholly unsecured junior liens, subject to governing law and plan requirements.

17. Repeat Bankruptcy Filings

Repeat filings can substantially limit foreclosure protection.

Under § 362(c)(3), certain debtors with one qualifying dismissed case during the preceding year may face termination of the stay after thirty days unless extended.

Under § 362(c)(4), the stay generally does not arise when two or more qualifying cases were pending and dismissed during the preceding year.

The debtor may seek relief under the statutory procedures, but strict deadlines apply.

A homeowner should not assume that filing repeated petitions will automatically stop each scheduled foreclosure sale.

18. Bad-Faith Filings and In Rem Relief

Section 362(d)(4) permits specified in rem relief concerning real property when the court finds that the bankruptcy filing was part of a scheme to delay, hinder, or defraud creditors involving qualifying transfers or multiple filings.

When the statutory requirements are satisfied and the order is properly recorded, the relief may affect later bankruptcy cases involving the property.

This can significantly limit the effectiveness of repeated filings intended solely to delay foreclosure.

The provision requires specific findings and procedures.

19. Maryland Foreclosure Mediation

Maryland law provides foreclosure mediation procedures for qualifying residential borrowers.

The availability and timing of mediation depend on statutory requirements.

Mediation may provide an opportunity to discuss loan modification, repayment arrangements, or other foreclosure alternatives.

However, mediation does not guarantee that the lender will agree to modify the loan.

The homeowner should understand applicable deadlines and preserve available rights.

Bankruptcy and foreclosure mediation may need to be coordinated.

20. Loan Modification and Bankruptcy

A homeowner may seek a loan modification before or during bankruptcy.

A modification may reduce payments, extend the loan term, or otherwise change the mortgage obligation.

However, an application for modification does not necessarily stop foreclosure.

In Chapter 13, a proposed modification may also require compliance with bankruptcy court procedures and plan requirements.

The debtor should not rely solely on pending negotiations when a foreclosure sale is approaching.

21. What If the Debtor Wants to Surrender the Home?

Not every homeowner wishes to retain the property.

A debtor may decide that the mortgage is unaffordable or the property has substantial negative equity.

Chapter 7 may discharge qualifying personal liability while the lender retains foreclosure rights.

The debtor should consider occupancy, insurance, property maintenance, taxes, association assessments, and other obligations that may arise after filing.

Surrender in bankruptcy does not necessarily transfer title immediately.

The debtor may remain the record owner until foreclosure or another legally effective transfer occurs.

22. Homeowners Association and Condominium Assessments

A debtor who owns property subject to condominium or homeowners association assessments may face continuing obligations.

Section 523(a)(16) excepts certain postpetition association fees and assessments from discharge for periods during which the debtor or trustee has the specified ownership interests.

The debtor should not assume that surrendering the property in bankruptcy eliminates all future association assessments.

The timing of title transfer can matter.

23. What If the Foreclosure Sale Violates the Automatic Stay?

A foreclosure conducted while the automatic stay applies may be subject to challenge.

The legal consequences depend on the circumstances and governing law.

A debtor may seek relief in the bankruptcy court.

Section 362(k) permits certain damages for willful violations of the stay.

However, a debtor should not assume that every sale occurring after a bankruptcy filing violates the stay.

The stay may have terminated, been modified, or failed to arise because of repeat-filing restrictions.

The procedural history must be examined.

24. Why Waiting Until the Last Moment Is Dangerous

A homeowner who consults counsel shortly before foreclosure may have fewer options.

Chapter 13 requires a realistic plan for maintaining mortgage payments and curing arrears.

The debtor must also satisfy eligibility and filing requirements.

A last-minute filing may temporarily stop the sale without solving the underlying default.

If the debtor cannot fund a feasible plan, the case may be dismissed and foreclosure may resume.

Earlier evaluation provides more time to examine loan modification, mediation, refinancing, sale, Chapter 13, or other alternatives.

Conclusion

Bankruptcy can provide powerful protection against foreclosure, but it is not an automatic or permanent solution.

Chapter 7 may temporarily stop foreclosure and discharge qualifying personal mortgage liability, but it generally does not provide a long-term cure mechanism for arrears.

Chapter 13 may permit a homeowner with sufficient income to cure defaults while maintaining ongoing payments.

The timing of the bankruptcy filing is especially important under Maryland foreclosure law and § 1322(c)(1).

Repeat filings, stay-relief orders, and completed foreclosure sales may substantially limit available relief.

A homeowner facing foreclosure should evaluate bankruptcy before the scheduled sale, when the greatest number of legal and financial options may still be available.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 362 — Automatic stay and relief from stay.
- 11 U.S.C. § 506 — Secured claims and valuation.
- 11 U.S.C. § 522 — Exemptions.
- 11 U.S.C. § 523(a)(16) — Certain postpetition association assessments.
- 11 U.S.C. § 1322(b)(5) — Cure and maintenance of long-term obligations.
- 11 U.S.C. § 1322(c) — Home mortgage cure rights and certain matured claims.

Maryland law

- Maryland Real Property Article, Title 7 — Foreclosure and deed-of-trust provisions.
- Maryland Rules 14-201 through 14-218 — Foreclosure procedure.
- Maryland Courts and Judicial Proceedings § 11-504 — Maryland exemptions.

Selected decisions

- *Hurlburt v. Black*, 925 F.3d 154 (4th Cir. 2019) (en banc) — Addresses modification of certain home-secured claims under § 1322(c)(2).
- *Bank of America, N.A. v. Caulkett*, 575 U.S. 790 (2015) — Addresses Chapter 7 treatment of wholly underwater junior mortgage liens.
- *Simard v. White*, 383 Md. 257, 859 A.2d 168 (2004) — Discusses Maryland foreclosure sale and ratification principles.
- *Johnson v. Home State Bank*, 501 U.S. 78 (1991) — Addresses the treatment of surviving mortgage liens and claims in Chapter 13.
- *Nobelman v. American Savings Bank*, 508 U.S. 324 (1993) — Addresses limits on modifying certain home mortgage rights in Chapter 13.
- In re Schweiger, 587 B.R. 469 (Bankr. D. Md. 2018) — Applies the Maryland foreclosure-auction cutoff for Chapter 13 mortgage cure, subject to restoration of the equity of redemption through state-court proceedings.

Bankruptcy and Eviction in Maryland: When the Automatic Stay Protects Tenants and When a Landlord Can Proceed

Belsky Bankruptcy Legal Library | Housing, Leases, and the Automatic Stay

By Alan J. Belsky, Attorney at Law

Bankruptcy May Temporarily Stop an Eviction, but It Does Not Guarantee the Right to Remain

A tenant facing eviction may consider bankruptcy as a means of stopping a landlord from obtaining possession of the property.

Filing Chapter 7 or Chapter 13 ordinarily triggers the automatic stay under 11 U.S.C. § 362, which prohibits many collection and enforcement activities.

But eviction proceedings receive special treatment under federal bankruptcy law.

A tenant who files before a judgment for possession is entered may have substantially different rights from a tenant who files after the landlord obtains judgment.

Even when bankruptcy temporarily stops an eviction, the tenant generally must address ongoing rent obligations.

The landlord may seek relief from the automatic stay, and certain statutory exceptions permit eviction proceedings to continue notwithstanding bankruptcy.

The timing of the filing, status of the Maryland eviction case, and nature of the landlord's claim are therefore critical.

1. How Residential Evictions Work in Maryland

Maryland law provides several procedures through which a landlord may seek possession of residential property.

Common proceedings include failure-to-pay-rent actions, tenant-holding-over cases, and breach-of-lease actions.

These proceedings arise under different provisions of the Maryland Real Property Article.

The landlord ordinarily must obtain the required judgment and follow applicable procedures before recovering possession through lawful eviction.

The precise notice, cure, and enforcement requirements depend on the type of case and applicable law.

A bankruptcy filing must be evaluated against the status of the particular eviction proceeding.

2. The Automatic Stay

Under § 362(a), filing bankruptcy ordinarily stays many actions to recover prepetition claims or obtain possession of estate property.

A residential lease may constitute a property interest relevant to the bankruptcy estate.

The automatic stay may therefore temporarily prevent a landlord from continuing an eviction proceeding.

However, the stay is subject to exceptions.

The landlord may also request relief under § 362(d).

A tenant should not assume that filing bankruptcy permanently prevents eviction.

3. Filing Before the Landlord Obtains Judgment for Possession

When the tenant files bankruptcy before a judgment for possession has been entered, the automatic stay may prevent the landlord from continuing the eviction proceeding without relief from the bankruptcy court.

The tenant's leasehold interest and the nature of the landlord's claim must be examined.

The landlord may seek stay relief.

The debtor's ability to remain in possession may depend on payment of ongoing rent and compliance with applicable lease obligations.

A bankruptcy filing ordinarily does not provide a permanent right to occupy property without paying rent.

4. Filing After Judgment for Possession

Section 362(b)(22) creates an important exception to the automatic stay.

The exception generally applies to continuation of certain eviction, unlawful detainer, or similar proceedings involving residential property when the landlord obtained a judgment for possession before the bankruptcy petition.

The provision is subject to the debtor's rights under § 362(l).

A tenant who files after judgment therefore may receive substantially less protection than one who files earlier.

The tenant should not assume that bankruptcy automatically stops execution of an existing possession judgment.

5. The Thirty-Day Certification Procedure

Section 362(l) provides a limited procedure through which certain residential tenants may obtain temporary protection notwithstanding a prepetition judgment for possession.

The debtor generally must file a certification concerning applicable nonbankruptcy law and deposit with the bankruptcy court the rent that would become due during the thirty-day period after filing.

The certification must satisfy the statutory requirements.

The debtor must establish that applicable nonbankruptcy law permits the debtor to cure the monetary default giving rise to the judgment for possession.

The procedure does not apply automatically to every eviction.

The initial § 362(l)(1) certification is filed with the petition and served on the landlord; it addresses circumstances in which nonbankruptcy law permits cure of the entire monetary default after the possession judgment. The required deposit covers rent becoming due during the 30 days after filing. Within that period, the debtor must cure the entire monetary default and file and serve the further certification to invoke § 362(l)(2). A landlord's objection prompts the statutory expedited hearing, rather than making either certification conclusive.

6. Curing the Default Within Thirty Days

Under § 362(l), a qualifying debtor may obtain additional protection by curing the monetary default within the statutory period and filing the required certification.

The landlord may object.

The bankruptcy court may determine whether the statutory requirements have been satisfied.

The debtor should not assume that merely promising to pay rent is sufficient.

The required deposit, certifications, cure, and procedural deadlines must be satisfied.

7. Maryland's Right of Redemption

Maryland law permits certain residential tenants facing failure-to-pay-rent eviction to redeem possession by paying the legally required amount before execution of the eviction, subject to statutory restrictions.

The right of redemption is governed principally by Maryland Real Property Article § 8-401.

However, redemption rights may be restricted in specified circumstances, including certain repeated judgments for possession.

The precise amount required and availability of redemption must be determined under current Maryland law.

These state-law rights are important when evaluating whether the debtor qualifies for the federal certification procedure under § 362(l).

8. What If the Tenant Has Lost the Right of Redemption?

A tenant who no longer possesses a right to cure the monetary default under applicable Maryland law may be unable to satisfy the requirements of § 362(l).

In that circumstance, the bankruptcy filing may not prevent continuation of the eviction under § 362(b)(22).

The tenant's rights depend on the type of judgment, procedural history, and applicable law.

The debtor should not assume that every failure-to-pay-rent judgment can be cured after bankruptcy is filed.

9. Evictions Based on Endangerment or Illegal Drug Use

Section 362(b)(23) provides an exception concerning certain eviction proceedings involving endangerment of property or illegal use of controlled substances on the property.

The statute requires specified certifications and procedures.

Section 362(m) provides mechanisms through which the debtor may contest the landlord's certification.

Under § 362(m), the endangerment or illegal-drug-use exception ordinarily becomes effective 15 days after the landlord files and serves the prescribed certification. A debtor wishing to contest it must file and serve an objection within that 15-day period; the statute then requires an expedited hearing. This is a separate procedure from the monetary-default certifications in subsection (l).

These provisions differ from the ordinary nonpayment-of-rent exception.

A debtor should not assume that the thirty-day monetary cure procedure applies to every eviction.

10. What Happens to Past-Due Rent?

Rent owed before bankruptcy generally constitutes a prepetition claim.

Depending on the circumstances, the debt may be dischargeable in Chapter 7.

However, discharge of personal liability for unpaid rent does not necessarily restore a terminated lease or eliminate the landlord's right to possession.

The landlord's claim for money and the landlord's right to recover the property are distinct.

A tenant may discharge substantial rent arrears but still be required to vacate.

11. Postpetition Rent Must Be Addressed

Bankruptcy ordinarily does not give the debtor a right to occupy leased property indefinitely without paying rent.

Rent obligations arising after filing may receive different treatment from prepetition arrears.

The debtor should determine whether the lease remains in effect, whether it has been assumed or rejected, and what obligations continue.

A landlord may seek relief from the stay when postpetition rent is not paid.

The debtor should not rely on bankruptcy as a substitute for an affordable housing arrangement.

12. Executory Contracts and Residential Leases

Section 365 governs executory contracts and unexpired leases.

A residential lease may be subject to assumption or rejection under the applicable provisions.

In Chapter 7, the trustee generally possesses authority concerning estate contracts and leases.

Special statutory provisions may affect leases of residential real property.

The debtor's rights and obligations depend on the lease's status and applicable law.

A lease that was validly terminated before bankruptcy may present different issues from an unexpired lease.

13. Can the Debtor Assume the Lease?

Assumption generally requires satisfaction of applicable statutory requirements.

Under § 365(b), certain defaults must be cured or adequately addressed, and adequate assurance of future performance may be required.

The particular rules depend on the lease and circumstances.

A debtor should not assume that filing bankruptcy automatically reinstates a terminated lease.

The legal status of the lease under Maryland law must be established.

14. What If the Lease Was Terminated Before Filing?

A lease validly terminated before bankruptcy may leave the debtor with limited rights.

Bankruptcy generally does not create property interests that did not exist under applicable nonbankruptcy law.

However, the tenant may retain certain statutory or equitable rights concerning possession or cure.

The precise effect depends on the type of termination and Maryland law.

The debtor should not assume that every notice of termination has the same legal effect as a judgment for possession.

15. What If the Landlord Files a Motion for Relief From Stay?

A landlord may request relief from the automatic stay under § 362(d).

The landlord may argue that the debtor is not paying ongoing rent, lacks a viable right to possession, or that other cause exists.

The debtor may oppose the motion.

The bankruptcy court determines whether relief is appropriate.

Even when the stay initially applies, the court may permit the landlord to continue eviction proceedings.

16. Chapter 7 Versus Chapter 13

Chapter 7 may discharge qualifying prepetition rent obligations relatively quickly.

But it ordinarily does not provide a long-term repayment mechanism designed to preserve a residential lease.

Chapter 13 may permit a debtor to address certain obligations through a repayment plan.

However, the debtor must satisfy the applicable requirements concerning lease assumption, cure, and ongoing performance.

Chapter 13 does not automatically guarantee continued occupancy.

The appropriate chapter depends on the lease status, arrears, income, and available cure rights.

17. Repeat Bankruptcy Filings

Repeat filings can limit automatic-stay protection.

Under § 362(c)(3), certain debtors with one qualifying dismissed case during the preceding year may face termination of the stay after thirty days.

Under § 362(c)(4), the stay generally does not arise when two or more qualifying cases were pending and dismissed during the preceding year.

The debtor may seek relief under the statutory procedures.

A tenant should not assume that repeatedly filing bankruptcy will stop each scheduled eviction.

18. What If the Sheriff Is Scheduled to Execute the Eviction?

The timing is critical.

A tenant who files before judgment may have different rights from one who files after judgment.

When § 362(b)(22) applies, the landlord may be able to proceed despite bankruptcy unless the debtor satisfies § 362(l).

The tenant should determine whether a judgment for possession exists, whether redemption remains available, and whether the required federal procedures can be completed.

A last-minute filing without satisfying the statutory requirements may fail to stop the eviction.

19. Can the Landlord Collect a Discharged Rent Debt?

A Chapter 7 discharge generally prohibits collection of discharged personal liabilities.

If prepetition rent was discharged, the landlord ordinarily cannot pursue prohibited collection of that personal obligation.

However, the discharge does not necessarily eliminate the landlord's possessory rights.

Nor does it necessarily discharge postpetition obligations.

The debtor should distinguish collection of money from enforcement of the right to possession.

20. Security Deposits

A residential security deposit may be subject to rights and obligations under Maryland law.

The landlord may assert claims for unpaid rent, damage, or other lawful charges.

The debtor may possess an interest in any refundable balance.

The bankruptcy treatment depends on the lease, timing, applicable law, and whether the deposit is property of the estate.

The debtor should disclose qualifying rights to refundable deposits.

21. Why Eviction Cases Require Immediate Review

A tenant facing eviction should obtain the relevant court documents before deciding whether bankruptcy will help.

Important documents include the lease, notices, complaint, judgment for possession, rent ledger, and scheduled eviction information.

The attorney should determine the type of eviction proceeding and whether any statutory right to cure remains.

The debtor's ability to pay ongoing rent is also important.

Bankruptcy may provide temporary relief, but a sustainable housing solution requires more than delaying the eviction.

Conclusion

Bankruptcy may temporarily stop an eviction, but the protection depends on the timing and nature of the landlord's proceedings.

A tenant who files before judgment for possession may receive broader automatic-stay protection than one who files afterward.

Section 362(b)(22) permits continuation of certain residential evictions following prepetition judgments for possession, subject to the limited protections of § 362(l).

Maryland's right-of-redemption provisions can be important in determining whether a tenant may cure the default.

A tenant facing eviction should not assume that filing bankruptcy automatically stops removal from the property. The judgment, cure rights, and federal certification requirements must be examined before filing.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 362(b)(22)–(23) — Exceptions to the automatic stay involving certain residential evictions.
- 11 U.S.C. § 362(l)–(m) — Tenant certifications, deposits, and objections.
- 11 U.S.C. § 365 — Executory contracts and unexpired leases.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 524 — Discharge injunction.

Maryland law

- Maryland Real Property § 8-401 — Failure-to-pay-rent proceedings and redemption.
- Maryland Real Property § 8-402 — Tenant holding over.
- Maryland Real Property § 8-402.1 — Breach-of-lease proceedings.

Selected decisions

- *In re Stoltz*, 315 F.3d 80 (2d Cir. 2002) — Addresses bankruptcy protections concerning certain residential lease interests under the pre-2005 statutory framework.
- *In re DiCamillo*, 206 B.R. 64 (Bankr. D.N.J. 1997) — Addresses residential lease termination and bankruptcy.
- *In re Williams*, 144 F.3d 544 (7th Cir. 1998) — Discusses bankruptcy and possessory interests.
- *In re Smith*, 105 B.R. 50 (Bankr. C.D. Cal. 1989) — Addresses landlord-tenant issues under bankruptcy law.
- *In re Ross*, 198 B.R. 5 (Bankr. E.D. Pa. 1996) — Discusses lease termination and bankruptcy estate interests.

Bankruptcy and Utility Services: Can Electric, Gas, Water, Telephone, or Internet Service Be Disconnected After Filing?

Belsky Bankruptcy Legal Library | Essential Services and Bankruptcy Protection

By Alan J. Belsky, Attorney at Law

Bankruptcy Can Protect Essential Utility Services, but the Protection Is Not Unlimited

Individuals filing bankruptcy frequently owe past-due utility bills. Electricity, natural gas, water, and telephone services may be essential to maintaining a household, particularly when the debtor has children, medical needs, or limited income.

A debtor may fear that filing bankruptcy will cause the utility company to disconnect service or refuse to continue providing it.

Federal bankruptcy law provides important protections.

Under 11 U.S.C. § 366, a qualifying utility generally may not alter, refuse, or discontinue service solely because the debtor filed bankruptcy or failed to pay a prepetition utility debt.

But the statute also permits utilities to require adequate assurance of payment for future service.

The protection therefore does not necessarily eliminate deposit requirements or permit the debtor to receive unlimited service without paying postpetition charges.

The debtor should understand both the immediate protections and the conditions for continued service.

1. What Does § 366 Protect?

Section 366(a) generally prohibits a utility from altering, refusing, or discontinuing service to a debtor solely because the debtor commenced a bankruptcy case or failed to pay a prepetition debt for utility service.

The provision is intended to prevent utility companies from using essential service as leverage to collect discharged or dischargeable debts.

For example, an electric company ordinarily cannot disconnect service solely because the debtor included an old electric bill in a Chapter 7 petition.

However, § 366 does not eliminate every lawful basis for discontinuing service.

The debtor must comply with applicable requirements concerning adequate assurance and ongoing payments.

2. Which Services Qualify as Utilities?

Traditional electric, natural gas, and water providers generally fall within the utility framework.

Telephone service may also qualify in appropriate circumstances.

The treatment of internet service, cable television, and other communications services can be more complicated.

Whether a provider qualifies as a utility under § 366 depends on the nature of the service, the provider's obligations, and applicable law.

A debtor should not assume that every subscription service is protected merely because it is useful or important.

3. Prepetition Utility Arrears

A utility bill incurred before bankruptcy generally constitutes a prepetition debt.

An ordinary unsecured utility balance may be dischargeable in Chapter 7.

For example, a debtor may owe $1,800 for prior electric service.

The debtor may include that obligation in the bankruptcy schedules.

The utility generally cannot discontinue qualifying service solely to collect that prepetition debt.

However, the utility may request adequate assurance for future service as permitted by § 366.

4. The Twenty-Day Rule in Chapter 7

Section 366(b) provides that a utility may alter, refuse, or discontinue service if the debtor or trustee does not furnish adequate assurance of payment, in the form of a deposit or other security, within twenty days after the order for relief.

In a voluntary Chapter 7 case, the filing ordinarily constitutes the order for relief.

The twenty-day period is therefore particularly important.

A debtor should not assume that filing bankruptcy guarantees uninterrupted service for the entire case without further action.

The utility may be entitled to require adequate assurance for future service.

5. What Is Adequate Assurance of Payment?

Adequate assurance is intended to protect the utility against the risk of nonpayment for postpetition service.

In an individual Chapter 7 case, it may take the form of a deposit or other appropriate security.

The amount and form may be disputed.

Section 366(b) permits the court, upon request of a party in interest and after notice and hearing, to order a reasonable modification of the amount of a deposit or other security.

The debtor should not assume that the utility may demand any amount without limitation.

Nor should the debtor assume that no deposit can be required.

6. Can the Utility Demand a New Deposit?

Potentially, yes.

A utility may request a deposit or other qualifying security as adequate assurance of payment.

For example, a debtor who owes substantial prepetition arrears may be asked to provide a deposit for continued postpetition service.

The deposit is not necessarily payment of the discharged prepetition balance.

It is intended to secure future service.

The debtor should distinguish between a lawful adequate-assurance demand and an attempt to collect an old debt.

7. Can the Utility Apply an Existing Deposit to Old Bills?

The treatment of an existing utility deposit depends on the agreement, applicable law, and bankruptcy provisions.

The utility may assert setoff or other rights concerning the deposit.

Section 366(c)(4), which applies in Chapter 11 cases, expressly addresses certain applications of prepetition security deposits.

Individual Chapter 7 cases require analysis under the provisions applicable to that chapter.

A debtor should not assume that every existing deposit must be returned or that the utility may automatically apply it without regard to bankruptcy law.

8. What If the Debtor Cannot Afford the Deposit?

A debtor who cannot afford the requested deposit should promptly consult counsel.

Depending on the circumstances, the debtor may seek to negotiate a reasonable amount or request bankruptcy court intervention.

The court may modify the amount of a deposit or other security under § 366(b).

However, the debtor must act before service is lawfully discontinued.

The existence of financial hardship does not automatically eliminate the adequate-assurance requirement.

9. Postpetition Utility Bills Must Be Paid

Bankruptcy generally does not permit the debtor to continue receiving utility service indefinitely without paying for it.

Charges for service provided after filing ordinarily must be addressed.

A utility may possess rights to discontinue service for postpetition nonpayment, subject to § 366 and other applicable law.

The debtor should maintain ongoing payments whenever possible.

The discharge of prepetition arrears does not eliminate the obligation to pay for future service.

10. Can Service Be Restored After Disconnection?

A debtor whose utility service was disconnected before bankruptcy may seek restoration.

Section 366 may provide protection against refusal of service based solely on prepetition debt.

However, restoration can involve adequate-assurance requirements, applicable tariffs, safety conditions, and other lawful obligations.

A debtor should not assume that filing bankruptcy automatically restores service without further action.

Prompt communication with the provider and bankruptcy counsel is important.

11. What If the Utility Refuses Service Because of a Discharged Debt?

A utility that refuses qualifying service solely because of a discharged prepetition debt may violate § 366 or the discharge injunction, depending on the circumstances.

The debtor may seek relief in bankruptcy court.

However, the utility may have legitimate grounds for requiring adequate assurance or addressing postpetition defaults.

The legal basis for the refusal must be identified.

A debtor should preserve notices, account statements, and communications with the provider.

12. Chapter 13 Utility Protection

Chapter 13 also provides protections under § 366.

The debtor may address prepetition utility arrears through the repayment plan as permitted by the Bankruptcy Code.

But ongoing service must still be maintained.

The debtor should not assume that confirmation of a Chapter 13 plan eliminates the obligation to pay current utility charges.

Adequate-assurance issues may also arise.

13. Chapter 11 Has Different Rules

Section 366(c) contains special adequate-assurance provisions applicable to Chapter 11 cases.

These provisions are more detailed and impose different requirements concerning the form and timing of adequate assurance.

For example, § 366(c)(2) addresses the thirty-day period applicable in Chapter 11.

A debtor should not apply the Chapter 11 thirty-day framework automatically to an individual Chapter 7 case.

The relevant chapter matters.

14. Electric and Gas Service in Maryland

Maryland electric and gas utilities operate under state regulatory requirements, including provisions administered by the Maryland Public Service Commission.

State law and utility tariffs may govern deposits, disconnection notices, payment arrangements, medical protections, and restoration procedures.

Federal bankruptcy law operates alongside these requirements.

A debtor may have rights under Maryland utility regulations independent of bankruptcy.

Those rights should be examined when service is threatened.

15. Medical Necessity and Utility Disconnection

A household member may require electricity for medical equipment or other health-related needs.

Maryland utility regulations may provide special procedures or protections in qualifying medical circumstances.

These protections are separate from § 366.

The debtor should notify the utility promptly and provide required documentation.

Bankruptcy may provide additional protection, but medical-necessity procedures should not be ignored.

16. Water and Sewer Service

Water and sewer services may be provided by municipal authorities, counties, or other entities.

The legal treatment may depend on the provider and the nature of the charges.

Some water and sewer obligations may be associated with liens or assessments affecting real property.

A debtor should not assume that every unpaid water charge is an ordinary unsecured utility debt.

The existence of a property lien may materially affect the bankruptcy analysis.

17. Telephone and Internet Service

Traditional telephone service may qualify for § 366 protection in appropriate circumstances.

Internet service and bundled telecommunications arrangements require separate consideration.

A provider's classification, regulatory obligations, and service terms may affect whether it is treated as a utility.

A debtor should not assume that broadband service is automatically protected to the same extent as electric service.

The applicable case law should be examined.

18. Utility Bills Owed by a Former Spouse or Roommate

Utility accounts may be held in one person's name even though several household members used the service.

The utility's contractual rights generally depend on the account agreement and applicable law.

A debtor's discharge does not automatically eliminate another person's separate liability.

Conversely, a utility may not necessarily impose another person's discharged debt on the debtor.

The account ownership and relevant contractual obligations should be identified.

19. Moving After Bankruptcy

A debtor may seek utility service at a new address after filing or discharge.

Section 366 may prohibit a qualifying utility from refusing service solely because of the bankruptcy or unpaid prepetition debt.

However, the utility may require lawful adequate assurance or impose other conditions permitted by law.

The debtor should not assume that a discharged utility balance must be paid merely to obtain service at a new residence.

The reason for any refusal should be examined.

20. What Should a Debtor Do Before Filing?

A debtor with substantial utility arrears should identify each provider, account balance, disconnection notice, and deposit requirement.

Counsel should determine whether the provider qualifies under § 366 and whether additional Maryland protections apply.

The debtor should also evaluate the ability to pay ongoing charges and any reasonable adequate-assurance deposit.

Where disconnection is imminent, timing may be critical.

The objective is to preserve essential service while addressing prepetition obligations lawfully.

Conclusion

Section 366 provides important protection against utility disconnection or refusal of service based solely on bankruptcy or unpaid prepetition utility debt.

But the protection is conditional.

In Chapter 7, a utility may require adequate assurance of payment within the statutory twenty-day period.

The debtor generally must continue paying for postpetition service.

Maryland utility regulations may provide additional protections concerning deposits, disconnection procedures, and medical needs.

A debtor facing utility disconnection should evaluate both bankruptcy protections and Maryland utility law before assuming that service can be terminated—or that filing bankruptcy guarantees uninterrupted service.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 366 — Utility service and adequate assurance.
- 11 U.S.C. § 362 — Automatic stay.
- 11 U.S.C. § 524 — Discharge injunction.
- 11 U.S.C. § 553 — Setoff.

Maryland law and regulations

- Maryland Public Utilities Article — Regulation of public utilities.
- Maryland Public Service Commission — Utility regulations and consumer protections.
- COMAR Title 20 — Maryland utility regulations, including applicable service termination and deposit requirements.

Selected decisions

- *In re Begley*, 760 F.2d 46 (3d Cir. 1985) — Addresses utility service and adequate assurance under § 366.
- *In re Hanratty*, 907 F.2d 1418 (3d Cir. 1990) — Addresses utility deposits and bankruptcy.
- *In re Jones*, 369 B.R. 745 (1st Cir. BAP 2007) — Discusses utility service protections and adequate assurance.
- *In re Moorefield*, 218 B.R. 795 (Bankr. M.D.N.C. 1997) — Addresses utility service and bankruptcy issues.

Bankruptcy and Creditors Who Refuse to Stop Collecting: Enforcing the Automatic Stay and Discharge Injunction

Belsky Bankruptcy Legal Library | Creditor Misconduct and Bankruptcy Remedies

By Alan J. Belsky, Attorney at Law

Creditors Do Not Have an Unlimited Right to Continue Collection After Bankruptcy

One of the principal benefits of bankruptcy is protection from creditor collection activity.

When a qualifying bankruptcy petition is filed, the automatic stay under 11 U.S.C. § 362 ordinarily prohibits many collection efforts involving prepetition debts.

After the debtor receives a discharge, § 524 generally prohibits attempts to collect discharged debts as personal liabilities.

These protections are fundamental to the bankruptcy system.

But creditors sometimes continue collection activity after receiving notice of bankruptcy. They may send collection letters, garnish wages, pursue lawsuits, repossess vehicles, or demand payment of discharged obligations.

Some violations result from administrative errors. Others involve deliberate attempts to pressure debtors into paying debts that federal law no longer permits creditors to collect.

The Bankruptcy Code provides remedies, including damages, attorney's fees, and contempt sanctions in appropriate circumstances.

However, the standards governing automatic-stay violations and discharge-injunction violations are different.

Understanding those distinctions is essential.

1. The Automatic Stay Begins When Bankruptcy Is Filed

Section 362(a) generally imposes an automatic stay when a qualifying bankruptcy petition is filed.

The stay ordinarily prohibits specified collection activities, including commencing or continuing lawsuits, enforcing judgments, obtaining possession of estate property, and collecting prepetition claims.

The stay generally arises by operation of law.

The debtor ordinarily does not need to obtain a separate court order.

However, exceptions and repeat-filing limitations may affect the protection.

A creditor's conduct must be evaluated under the particular subsection of § 362 that applies.

2. What Collection Activities Are Generally Prohibited?

When the automatic stay applies, prohibited activities may include continuing a collection lawsuit, enforcing a prepetition judgment, garnishing wages, repossessing collateral, or demanding payment of a prepetition debt.

The statute also restricts certain actions against property of the bankruptcy estate.

However, not every communication from a creditor is unlawful.

For example, a creditor may communicate concerning legitimate postpetition obligations, reaffirmation, or other matters permitted by law.

The content, purpose, and circumstances of the communication matter.

3. Does the Creditor Have to Know About the Bankruptcy?

The automatic stay generally arises when the petition is filed, whether or not the creditor has actual notice.

However, notice is important when determining whether a violation was willful and whether damages are available under § 362(k).

A creditor that acts without knowledge of the bankruptcy may violate the stay without necessarily satisfying the requirements for a willful-violation damages award.

Once the creditor receives notice, continued prohibited collection may create substantially greater exposure.

The debtor should preserve evidence of when and how notice was provided.

4. What Is a Willful Violation of the Automatic Stay?

Under § 362(k)(1), an individual injured by a willful violation of the stay generally is entitled to recover actual damages, including costs and attorney's fees, and may recover punitive damages in appropriate circumstances.

A willful violation ordinarily does not require proof that the creditor specifically intended to violate bankruptcy law.

Knowledge of the bankruptcy and an intentional act that violates the stay may be sufficient under applicable precedent.

The creditor's belief concerning the legality of its conduct can present separate issues.

The statutory requirements and controlling case law must be examined.

5. Actual Damages

Actual damages may include financial losses caused by a willful stay violation.

Examples may include improperly garnished wages, bank charges, lost transportation, towing expenses, or other proven economic harm.

Attorney's fees and costs are expressly addressed by § 362(k).

The debtor must establish causation and the amount of recoverable damages.

A violation does not automatically entitle the debtor to an arbitrary monetary award.

The evidence should connect the creditor's conduct to the claimed injury.

6. Emotional Distress Damages

A debtor may experience anxiety, humiliation, or other emotional distress from unlawful collection activity.

Whether such damages are recoverable under § 362(k) depends on applicable law and the evidence.

Courts have required sufficient proof of actual injury rather than accepting conclusory allegations.

The Fourth Circuit's relevant precedent should be considered.

The debtor should preserve documentation and testimony supporting the nature, severity, and cause of the claimed distress.

7. Punitive Damages

Section 362(k)(1) permits punitive damages in appropriate circumstances.

Punitive damages are not awarded automatically whenever a creditor violates the stay.

The creditor's conduct, knowledge, persistence, and other relevant factors may matter.

Repeated collection after clear notice or particularly egregious conduct may support a stronger punitive-damages claim.

The court must apply the governing legal standards.

8. Attorney's Fees for Stay Violations

Section 362(k)(1) expressly includes costs and attorney's fees among recoverable actual damages.

The debtor may therefore have a statutory basis for recovering reasonable fees incurred in addressing a willful violation.

The scope and reasonableness of the fees remain subject to applicable law.

Counsel should document time spent investigating the violation, communicating with the creditor, seeking relief, and pursuing damages.

The availability of attorney's fees is an important distinction between § 362(k) and some other bankruptcy remedies.

9. Wage Garnishment After Filing

A creditor that continues garnishing wages on a prepetition unsecured judgment after receiving notice of bankruptcy may violate the automatic stay.

The debtor should determine whether the employer, garnishing creditor, or other party continued prohibited conduct after the stay became effective.

The timing of payroll processing and transfer of funds may matter.

A debtor should preserve pay statements, garnishment records, notices, and communications.

The proper remedy may include release of funds, damages, or other relief.

10. Repossession After Filing

Repossession of a vehicle after bankruptcy may violate the stay when the stay applies and no relief or exception permits the action.

However, secured creditors may seek relief from the stay.

The stay may also terminate under specified provisions concerning secured personal property.

A debtor should not assume that every postpetition repossession is unlawful.

The relevant orders, statement of intention, and statutory deadlines must be examined.

11. Property Repossessed Before Bankruptcy

A creditor may have repossessed property before the bankruptcy petition.

In *City of Chicago v. Fulton*, 592 U.S. 154 (2021), the Supreme Court held that merely retaining property seized before bankruptcy does not itself violate § 362(a)(3).

The decision does not resolve every possible turnover or stay issue.

Section 542 and other provisions may provide separate remedies.

The debtor should not assume that filing bankruptcy automatically requires immediate return of previously seized property.

12. Collection Lawsuits After Filing

A creditor ordinarily may not commence or continue a lawsuit to collect a prepetition claim while the automatic stay applies, absent relief or an exception.

The creditor may need to suspend the proceeding.

However, certain actions, including qualifying criminal and governmental regulatory proceedings, receive different treatment.

The debtor should determine whether the lawsuit seeks ordinary monetary collection or involves a statutory exception.

13. Governmental Collection and Regulatory Proceedings

Section 362(b)(4) excepts certain governmental police and regulatory actions from the automatic stay.

This exception may permit governmental agencies to continue proceedings enforcing public health, safety, licensing, or regulatory laws.

But the exception does not generally authorize enforcement of a money judgment merely because the creditor is a government agency.

The distinction between exercising regulatory authority and collecting money is critical.

For example, a government agency may be permitted to continue a proceeding determining whether a regulatory violation occurred while remaining restricted from enforcing a resulting monetary judgment against estate property.

The particular statutory provisions and relief sought must be examined.

14. Criminal Proceedings

Section 362(b)(1) generally excepts commencement or continuation of criminal actions or proceedings against the debtor.

Filing bankruptcy therefore does not ordinarily stop a criminal prosecution.

Criminal fines and restitution also may receive special treatment under the dischargeability provisions.

The debtor should not assume that bankruptcy prevents criminal enforcement merely because the proceedings may have financial consequences.

15. When Does the Automatic Stay End?

The automatic stay does not necessarily remain effective until every aspect of the bankruptcy case is completed.

Section 362(c) governs termination of the stay in various circumstances.

For example, the stay of certain acts against the debtor may terminate upon discharge, dismissal, or other statutory events.

The stay concerning estate property may remain effective until the property is no longer property of the estate, subject to applicable law.

Repeat filings may also shorten or prevent the stay.

The relevant protection must be determined from the statute and case history.

16. The Discharge Injunction

After discharge, § 524(a)(2) generally prohibits acts to collect, recover, or offset a discharged debt as a personal liability of the debtor.

The discharge injunction differs from the automatic stay.

The stay generally protects the bankruptcy process while the case is pending.

The discharge injunction protects the debtor from collection of discharged personal obligations after discharge.

A creditor that continues collection may violate the injunction.

But the debt must actually have been discharged, and the creditor's conduct must fall within the prohibition.

17. The Supreme Court's Decision in *Taggart*

In *Taggart v. Lorenzen*, 587 U.S. 554 (2019), the Supreme Court established the standard for civil contempt arising from violations of the discharge injunction.

The Court held that contempt may be appropriate when there is no fair ground of doubt as to whether the discharge order prohibited the creditor's conduct.

The standard is objective.

A creditor's subjective belief that its conduct was lawful does not automatically prevent contempt.

However, a reasonable basis for uncertainty concerning the discharge injunction may defeat a contempt claim.

This standard differs from the ordinary willfulness analysis under § 362(k).

18. What Damages Are Available for Discharge Violations?

Section 524 does not contain the same express individual damages provision as § 362(k).

Discharge-injunction violations ordinarily are enforced through the bankruptcy court's contempt authority, including § 105(a), subject to the limits established by *Taggart*.

Available remedies may include compensatory relief and attorney's fees in appropriate circumstances.

Punitive sanctions raise additional issues concerning the nature and limits of civil contempt.

The debtor should not assume that every discharge violation produces the same remedies as a willful automatic-stay violation.

19. Collection Letters After Discharge

A creditor may send a statement or notice after discharge for reasons that are not necessarily prohibited.

For example, a mortgage servicer may provide informational statements concerning a surviving lien.

However, a communication that demands personal payment of a discharged debt may violate the discharge injunction.

The wording, context, and creditor's conduct matter.

A debtor should preserve the complete communication rather than relying solely on a summary.

20. Credit Reporting After Discharge

A creditor may continue reporting accurate historical information concerning a discharged account.

However, reporting that falsely suggests the debtor remains personally liable may raise issues under the Fair Credit Reporting Act or, in appropriate circumstances, the discharge injunction.

Not every reporting error automatically constitutes contempt.

The debtor should review credit reports, dispute inaccuracies, and preserve the relevant documentation.

The legal theory depends on the nature of the reporting and the creditor's conduct.

21. Mortgage Statements After Discharge

A mortgage lien ordinarily survives Chapter 7 discharge even when the debtor's personal liability is eliminated.

Mortgage servicers may have legitimate reasons to provide informational statements concerning the loan and collateral.

Federal mortgage servicing regulations also address certain communications with borrowers in bankruptcy.

A statement that accurately identifies its informational purpose may present different issues from a demand for personal payment of a discharged obligation.

The debtor should distinguish permissible lien-related communications from prohibited personal collection.

22. Collection of Nondischargeable Debts

The discharge injunction does not prohibit collection of obligations that were not discharged, subject to other applicable restrictions.

Examples may include certain taxes, domestic support obligations, qualifying student loans, and specified fines or penalties.

A creditor should not assume that a debt is nondischargeable merely because the creditor believes it falls within an exception.

The legal character of the obligation matters.

A dispute may require a determination of dischargeability.

23. Creditors Who Claim They Never Received Notice

A creditor may contend that it did not receive notice of the bankruptcy.

Notice can affect the legal consequences of collection activity and, in certain circumstances, dischargeability under § 523(a)(3).

The debtor should ensure that creditors are properly listed and preserve records of notices.

The absence of notice does not necessarily mean every postpetition collection action is lawful.

But it may affect whether damages or contempt remedies are available.

24. Can the Bankruptcy Court Reopen a Closed Case?

Under § 350(b), a bankruptcy court may reopen a case to provide relief to the debtor or for other cause.

A debtor may seek to reopen a case to address discharge-enforcement issues.

Reopening does not itself establish that a violation occurred.

The debtor must prove the applicable statutory and legal requirements.

A discharge injunction may remain enforceable after the case closes.

25. What Evidence Should the Debtor Preserve?

Evidence is essential when pursuing creditor misconduct claims.

Relevant materials may include collection letters, emails, text messages, voicemail recordings, call logs, pay statements, bank records, repossession documents, and court filings.

The debtor should also preserve evidence of when the creditor received bankruptcy notice.

Financial losses should be documented.

Where emotional distress damages are claimed, appropriate supporting evidence may be necessary.

A debtor should not assume that the mere existence of an improper collection letter establishes every element of a damages claim.

26. Why Prompt Action Matters

A debtor who experiences prohibited collection activity should promptly notify bankruptcy counsel.

Early action may prevent additional harm.

The creditor may correct an administrative error after receiving notice.

In other circumstances, court intervention may be necessary.

The debtor should not ignore ongoing garnishment, repossession threats, or lawsuits merely because bankruptcy has been filed.

The appropriate remedy depends on whether the automatic stay or discharge injunction applies and what conduct occurred.

Conclusion

The automatic stay and discharge injunction provide essential protections against creditor collection.

Section 362 generally restricts collection activity while bankruptcy protection applies.

Section 524 generally prohibits collection of discharged debts as personal liabilities.

Creditors that violate these protections may face damages, attorney's fees, or contempt remedies.

But the governing standards differ.

A willful automatic-stay violation under § 362(k) is not evaluated under precisely the same standard as discharge-injunction contempt under *Taggart*.

Governmental regulatory proceedings, criminal matters, surviving liens, and nondischargeable debts also require separate consideration.

A debtor who continues receiving collection demands after bankruptcy should not assume that the creditor is entitled to collect—or that every communication is unlawful. The nature of the debt, applicable protection, and creditor's conduct must be examined.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 362 — Automatic stay and damages for willful violations.
- 11 U.S.C. § 524 — Discharge injunction.
- 11 U.S.C. § 105 — Bankruptcy court authority.
- 11 U.S.C. § 350 — Reopening cases.
- 11 U.S.C. § 523 — Exceptions to discharge.

Selected decisions

- *Taggart v. Lorenzen*, 587 U.S. 554 (2019) — Establishes the objective civil contempt standard for discharge-injunction violations.
- *City of Chicago v. Fulton*, 592 U.S. 154 (2021) — Addresses retention of property seized before bankruptcy.
- *Citizens Bank of Maryland v. Strumpf*, 516 U.S. 16 (1995) — Addresses temporary administrative holds and setoff.
- *In re Knaus*, 889 F.2d 773 (8th Cir. 1989) — Addresses creditor conduct and turnover obligations under the pre-*Fulton* framework.
- *In re Weatherford*, 413 B.R. 273 (Bankr. D.S.C. 2009) — Discusses automatic-stay violations and damages.
- In re Barbour, 77 B.R. 530 (Bankr. E.D.N.C. 1987) — Addresses contempt for violating the discharge injunction through a post-discharge collection suit. Apply the current contempt standard in Taggart v. Lorenzen, 587 U.S. 554 (2019).

Fines, Penalties, Restitution, and Government Debts in Bankruptcy: What Can Be Discharged and What Survives?

Belsky Bankruptcy Legal Library | Government Claims and Dischargeability

By Alan J. Belsky, Attorney at Law

Not Every Debt Owed to the Government Is Nondischargeable

A person considering bankruptcy may owe money to the federal government, the State of Maryland, a county, a municipality, or a governmental agency.

These obligations may include traffic fines, parking citations, toll violations, licensing penalties, restitution, unemployment overpayments, administrative assessments, and debts referred to Maryland's Central Collection Unit.

A common misconception is that debts owed to government agencies cannot be discharged in bankruptcy.

That is incorrect.

The Bankruptcy Code distinguishes between obligations imposed to punish or deter misconduct and obligations intended to compensate a governmental entity for an actual financial loss.

It also distinguishes criminal restitution from ordinary civil debts, taxes from penalties, and regulatory enforcement from debt collection.

Some governmental obligations survive Chapter 7 discharge. Others may be discharged even though a government agency is the creditor.

The legal character of the obligation—not simply the identity of the agency collecting it—determines the result.

1. The Principal Statute: 11 U.S.C. § 523(a)(7)

Section 523(a)(7) generally excepts from discharge certain debts for fines, penalties, or forfeitures payable to and for the benefit of a governmental unit that are not compensation for actual pecuniary loss.

The statute also contains special provisions concerning tax penalties.

Three questions are particularly important:

- Is the obligation a fine, penalty, or forfeiture?
- Is it payable to and for the benefit of a governmental unit?
- Is it compensation for an actual pecuniary loss?

The statutory language and controlling decisions must be considered together.

A governmental debt does not become nondischargeable merely because an agency describes it as a penalty.

Conversely, a qualifying governmental penalty may remain nondischargeable even when it arises from a civil rather than criminal proceeding.

2. Criminal Fines

Criminal fines generally receive strong protection against discharge.

A fine imposed as punishment for a criminal offense ordinarily is not treated as an ordinary unsecured consumer debt.

The bankruptcy discharge generally does not eliminate qualifying criminal fines.

For example, a criminal court may impose a monetary fine following conviction of an offense.

The debtor ordinarily cannot discharge that fine merely by filing Chapter 7.

The underlying criminal proceeding also generally is not stopped by the automatic stay because § 362(b)(1) excepts commencement or continuation of criminal actions and proceedings.

3. Criminal Restitution

Criminal restitution presents special issues.

Restitution may require an offender to pay money associated with harm caused by criminal conduct.

Although restitution may benefit an identifiable victim, courts have recognized its penal and rehabilitative purposes.

In *Kelly v. Robinson*, 479 U.S. 36 (1986), the Supreme Court held that restitution imposed as a condition of criminal probation was nondischargeable under the statutory framework considered.

The Court emphasized the state's interest in administering criminal justice.

The decision remains important when evaluating criminal restitution under § 523(a)(7).

Federal criminal restitution also receives specific treatment under § 523(a)(13).

4. Civil Penalties

Civil penalties may be imposed by governmental agencies for violations of regulatory statutes.

Examples may include environmental penalties, licensing violations, consumer protection enforcement, and administrative sanctions.

A civil penalty may be nondischargeable under § 523(a)(7) when it satisfies the statutory requirements.

The fact that the proceeding was civil rather than criminal does not necessarily make the obligation dischargeable.

However, the government must establish the legal character of the obligation.

A payment designed to reimburse the agency for actual financial loss may receive different treatment.

5. Compensation for Actual Pecuniary Loss

The phrase *actual pecuniary loss* is central to § 523(a)(7).

A governmental agency may seek reimbursement for money it actually expended.

For example, an agency may seek repayment of funds mistakenly paid to an individual.

Such an obligation may be compensatory rather than punitive.

But labels are not controlling.

The court may examine the statute authorizing the charge, the purpose of the obligation, and how the money is calculated and used.

An amount described as reimbursement may still have punitive characteristics.

Conversely, a charge labeled a penalty may actually compensate for a measurable financial loss.

6. Traffic Citations

Traffic-related debts can arise from criminal, civil, or administrative proceedings.

The classification matters.

A fine imposed for a traffic offense may qualify as a nondischargeable governmental penalty.

However, some traffic-related charges may involve reimbursement, administrative fees, or other obligations requiring separate analysis.

The debtor should identify the issuing authority, governing statute, and nature of the charge.

A traffic citation should not automatically be classified solely by the label appearing on the payment notice.

7. Parking Tickets

Parking citations frequently involve municipal or county enforcement systems.

A parking fine imposed to enforce parking regulations may qualify as a governmental penalty under § 523(a)(7).

However, related towing charges, storage fees, administrative costs, and other assessments may have different legal characteristics.

For example, a municipality may impose a $75 parking fine and separate charges for towing and storage.

The fine and the reimbursement charges should not necessarily be treated identically.

Each component should be analyzed.

8. Toll Violations and Civil Penalties

Maryland toll obligations may include the underlying toll, administrative fees, and civil penalties for failure to pay.

These components can raise different dischargeability questions.

The underlying toll may resemble a charge for use of a transportation facility.

A separate civil penalty may be imposed to enforce compliance.

The fact that both amounts appear on the same collection notice does not necessarily make them legally identical.

A debtor should obtain an itemized statement identifying the original tolls, penalties, fees, and collection charges.

9. Maryland Transportation Authority Claims

The Maryland Transportation Authority administers toll facilities and related enforcement procedures.

Unpaid tolls and civil penalties may be referred for collection or enforced through statutory mechanisms.

The bankruptcy treatment depends on the nature of each obligation.

A debtor should not assume that every MDTA balance is nondischargeable.

Nor should the debtor assume that every toll-related charge is an ordinary dischargeable debt.

The governing statutes and the purpose of the assessment must be examined.

10. Maryland Central Collection Unit

Maryland's Central Collection Unit collects delinquent obligations referred by state agencies and certain other governmental entities.

The unit may collect unpaid fees, overpayments, penalties, and other obligations.

Referral to the Central Collection Unit does not itself determine dischargeability.

The underlying debt retains its legal character.

For example, a dischargeable agency overpayment does not automatically become nondischargeable merely because it was referred for collection.

Conversely, a qualifying governmental penalty does not become dischargeable simply because collection has been transferred to another agency.

11. Central Collection Unit Fees

Maryland law authorizes collection fees in connection with certain delinquent obligations.

State Finance and Procurement Article § 3-304 provides authority concerning collection charges.

The applicable fee may depend on the governing statute, regulation, and circumstances.

The bankruptcy treatment of collection fees requires separate analysis.

A fee that compensates the government for collection costs may present different issues from a punitive penalty.

The debtor should request an itemized accounting rather than treating the entire CCU balance as a single obligation.

12. Unemployment Benefit Overpayments

A state unemployment agency may determine that a recipient received benefits to which the recipient was not entitled.

The overpayment may result from administrative error, inaccurate wage information, eligibility changes, or intentional misrepresentation.

The bankruptcy treatment depends on the circumstances.

An ordinary overpayment may be dischargeable.

An obligation obtained through fraud may be excepted from discharge under § 523(a)(2) when the applicable requirements are satisfied.

Additional statutory provisions may affect penalties and administrative recovery.

The debtor should distinguish repayment of benefits from separate fraud penalties.

13. Workers' Compensation Assessments and Penalties

Governmental workers' compensation agencies may impose assessments, fines, or penalties under applicable law.

Some obligations may be regulatory or punitive.

Others may reimburse funds paid or expenses incurred.

The classification depends on the statute and the purpose of the assessment.

A business owner's personal liability also must be established.

The existence of a workers' compensation-related obligation does not automatically determine dischargeability.

14. Professional Licensing Penalties

Licensing boards may impose fines, administrative costs, restitution, or other monetary sanctions.

For example, a professional board may assess a civil penalty for violating licensing requirements.

A qualifying punitive fine payable to the government may be nondischargeable.

An assessment intended to reimburse actual investigative costs may require a different analysis.

The debtor should examine the disciplinary order and authorizing statute.

Bankruptcy generally does not eliminate the government's authority to regulate professional conduct.

15. Attorney Disciplinary Assessments

Attorney disciplinary proceedings may involve monetary obligations, including costs and other assessments.

The bankruptcy treatment depends on the legal character of the obligation.

Courts have examined whether disciplinary costs imposed by governmental or court-related regulatory authorities constitute nondischargeable penalties.

The purpose of the assessment, governing rules, and applicable precedent matter.

A debtor should not assume that every disciplinary cost award is dischargeable merely because it reimburses expenses.

Nor should the debtor assume that all such obligations are nondischargeable.

16. Court Costs and Filing Fees

Court-related monetary obligations may include filing fees, administrative costs, sanctions, and penalties.

These categories are not necessarily treated identically.

A court-imposed punitive sanction may qualify under § 523(a)(7).

An ordinary fee or reimbursement obligation may require different analysis.

The identity of the court or government agency does not alone resolve the issue.

The purpose and statutory basis of the obligation should be examined.

17. Civil Contempt Sanctions

Civil contempt sanctions can serve different purposes.

Some are coercive, intended to compel compliance with a court order.

Others compensate an injured party for losses.

Still others may have punitive characteristics.

The bankruptcy treatment depends on the nature of the sanction and the governing statutory provisions.

A debtor should not assume that every contempt-related monetary obligation is nondischargeable.

The underlying order and purpose of the sanction matter.

18. Governmental Restitution Outside Criminal Proceedings

A government agency may obtain restitution or reimbursement through a civil enforcement proceeding.

The obligation may compensate consumers, reimburse public funds, or enforce regulatory requirements.

The Supreme Court addressed related issues in *Pennsylvania Department of Public Welfare v. Davenport*, 495 U.S. 552 (1990), and subsequent statutory amendments altered aspects of the treatment of criminal restitution.

Civil restitution requires its own analysis.

The term restitution does not automatically establish nondischargeability under every subsection of § 523.

19. Regulatory Enforcement and the Automatic Stay

Section 362(b)(4) permits certain governmental police and regulatory proceedings to continue despite bankruptcy.

For example, an agency may be permitted to continue proceedings concerning public safety, environmental compliance, or professional licensing.

However, the exception generally does not permit enforcement of a money judgment merely because the government obtained it through a regulatory proceeding.

The distinction between determining liability and collecting money is important.

A governmental agency may possess authority to continue regulatory proceedings while remaining restricted from collecting a monetary obligation from estate property.

20. Criminal Proceedings and Bankruptcy

Section 362(b)(1) generally permits criminal proceedings to continue notwithstanding bankruptcy.

A debtor cannot ordinarily stop a criminal prosecution merely by filing Chapter 7.

The fact that a criminal proceeding may result in restitution, fines, or other financial consequences does not automatically bring it within the ordinary collection stay.

However, the debtor's rights concerning particular monetary enforcement actions may require separate analysis.

21. Governmental Liens

A government agency may possess a lien securing a monetary obligation.

The lien may arise under tax law, judgment procedures, or another statutory mechanism.

Discharge of personal liability does not necessarily eliminate a valid lien.

The debtor should determine whether the government has obtained a lien, whether it attached to property, and whether any bankruptcy avoidance provision applies.

A debt's dischargeability and the enforceability of its lien are separate questions.

22. Government Debts and Chapter 13

Chapter 13 provides a different discharge framework from Chapter 7.

Certain fines, penalties, and restitution obligations may receive different treatment under § 1328.

The statutory exceptions applicable to a Chapter 13 discharge must be examined.

A debtor should not assume that Chapter 13 discharges every penalty that survives Chapter 7.

Nor should the debtor assume that every governmental monetary obligation receives identical treatment in both chapters.

The nature of the obligation and the specific discharge provision control.

23. Government Overpayments Versus Government Penalties

A government agency may assert both an overpayment and a separate penalty.

For example, a recipient may have received $12,000 in benefits to which the recipient was not entitled.

The agency may also assess a $3,000 penalty for intentional misrepresentation.

The $12,000 repayment obligation and $3,000 penalty may require different dischargeability analyses.

The debtor should obtain the agency's determination and itemized account history.

The entire balance should not automatically be classified as one nondischargeable debt.

24. What If the Agency Continues Collecting After Discharge?

If a governmental obligation was discharged, attempts to collect it as a personal liability may violate § 524.

However, the government may continue collecting obligations that are legally excepted from discharge, subject to applicable law.

The debtor may need a determination of dischargeability when the obligation's character is disputed.

A collection notice from a government agency does not establish that the debt survived bankruptcy.

The agency's legal basis for collection should be examined.

25. Why Government Debts Should Be Itemized Before Filing

A debtor may receive a collection notice stating that $18,000 is owed to a governmental collection agency.

The total may include principal, interest, penalties, administrative charges, and collection fees.

Those components may have different legal characteristics.

Before filing, counsel should obtain the underlying agency determination, authorizing statute, account history, and itemized balance.

The debtor should identify which amounts may be discharged, which may survive, and whether any lien or administrative recovery right exists.

This analysis may materially affect whether Chapter 7 or Chapter 13 is appropriate.

Conclusion

Government debts are not categorically nondischargeable.

Section 523(a)(7) protects qualifying governmental fines, penalties, and forfeitures, while other provisions address criminal restitution, taxes, fraud, and related obligations.

The legal character of the debt is more important than the identity of the collecting agency.

Traffic citations, toll penalties, licensing assessments, unemployment overpayments, and Central Collection Unit balances may contain components requiring different treatment.

Bankruptcy also distinguishes governmental regulatory authority from ordinary monetary collection.

Before assuming that a debt owed to the federal government, Maryland, a county, or a municipality will survive bankruptcy, the underlying obligation should be identified and analyzed under the applicable discharge provisions.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 523(a)(7) — Certain governmental fines, penalties, and forfeitures.
- 11 U.S.C. § 523(a)(13) — Certain federal criminal restitution obligations.
- 11 U.S.C. § 362(b)(1) — Criminal proceedings exception.
- 11 U.S.C. § 362(b)(4) — Governmental police and regulatory exception.
- 11 U.S.C. § 524 — Discharge injunction.
- 11 U.S.C. § 1328 — Chapter 13 discharge.

Maryland law

- Maryland State Finance and Procurement § 3-304 — State debt collection charges.
- Maryland Transportation Article — Traffic, transportation, and toll-related provisions.
- Maryland Central Collection Unit — State debt collection administration.

Selected decisions

- *Kelly v. Robinson*, 479 U.S. 36 (1986) — Addresses nondischargeability of criminal restitution.
- *Pennsylvania Department of Public Welfare v. Davenport*, 495 U.S. 552 (1990) — Addresses criminal restitution under the Chapter 13 discharge provisions then in effect; subsequent statutory amendments must be considered.
- *NLRB v. Bildisco & Bildisco*, 465 U.S. 513 (1984) — Addresses bankruptcy and regulatory obligations in a different statutory context.
- *Ohio v. Kovacs*, 469 U.S. 274 (1985) — Addresses environmental cleanup obligations reduced to monetary claims.
- *In re Thompson*, 16 F.3d 576 (4th Cir. 1994) — Addresses criminal restitution and bankruptcy dischargeability.
- *In re Towers*, 162 F.3d 952 (7th Cir. 1998) — Addresses civil restitution and § 523(a)(7).

Bankruptcy and Lawsuit Judgments: Which Judgments Can Be Discharged, Which Liens Survive, and When Fraud or Intentional Injury Changes the Result

Belsky Bankruptcy Legal Library | Judgments, Litigation, and Dischargeability

By Alan J. Belsky, Attorney at Law

A Judgment Does Not Automatically Make a Debt Nondischargeable

A person who has been sued and lost may believe that bankruptcy can no longer eliminate the debt because the creditor obtained a judgment.

That belief is generally incorrect.

Many judgments are dischargeable in Chapter 7 bankruptcy. A judgment arising from an ordinary credit card account, personal loan, medical bill, or negligence claim may be eliminated just as the underlying debt could have been discharged before judgment.

But some judgments involve obligations that bankruptcy does not discharge.

Fraud, willful and malicious injury, certain governmental penalties, domestic support obligations, and other statutory exceptions may cause particular debts to survive.

A separate issue arises when the judgment creditor has obtained a lien against the debtor's property.

Even when personal liability is discharged, a valid prepetition judgment lien may remain unless it is avoided or otherwise extinguished.

The critical distinction is between the judgment as evidence of personal liability, the nature of the underlying debt, and any property rights created through the judgment.

1. What Does a Judgment Establish?

A judgment ordinarily establishes a legally enforceable obligation determined by a court.

The judgment may arise after trial, summary judgment, default, consent, or another procedural disposition.

The creditor may obtain collection remedies under applicable law.

These can include wage garnishment, bank account attachment, judgment liens, and execution against property.

But the existence of a judgment does not independently determine whether the obligation is dischargeable in bankruptcy.

Federal bankruptcy law governs dischargeability.

2. Ordinary Credit Card Judgments

A judgment arising from an ordinary credit card balance generally is dischargeable in Chapter 7.

For example, a creditor may obtain a $28,000 judgment based on unpaid credit card charges.

If the debt does not fall within a statutory exception, Chapter 7 may discharge the debtor's personal liability.

The creditor ordinarily may not continue collecting the discharged obligation personally after discharge.

However, a judgment lien that attached to property before bankruptcy requires separate analysis.

3. Medical Bill Judgments

Medical debts generally are dischargeable unsecured obligations.

A hospital or physician may obtain a judgment for unpaid treatment charges.

The judgment does not ordinarily convert the debt into a nondischargeable obligation.

The debtor may discharge qualifying personal liability in Chapter 7.

But any valid lien or separate statutory right must be evaluated independently.

4. Personal Loan Judgments

Judgments arising from ordinary personal loans generally may be discharged.

The fact that the lender obtained judgment does not automatically alter the debt's dischargeability.

However, a creditor may assert fraud or another statutory exception when supported by the underlying transaction.

A mere failure to repay ordinarily does not establish fraud.

The creditor must satisfy the applicable legal requirements.

5. Negligence Judgments

A judgment arising from ordinary negligence generally may be discharged in Chapter 7.

For example, a driver may cause an automobile accident and become personally liable for damages.

If the conduct involved ordinary negligence and no statutory exception applies, the resulting judgment may be dischargeable.

The fact that the injured person suffered serious harm does not automatically change the result.

Bankruptcy law distinguishes negligent conduct from intentional injury and other specified misconduct.

6. Willful and Malicious Injury

Section 523(a)(6) excepts certain debts arising from willful and malicious injury by the debtor to another person or another person's property.

In *Kawaauhau v. Geiger*, 523 U.S. 57 (1998), the Supreme Court distinguished intentional injury from conduct that merely causes an unintended injury.

Ordinary negligence generally does not satisfy the statutory standard.

Recklessness alone also does not establish the deliberate or intentional injury required by § 523(a)(6). Evidence must satisfy both the willful and malicious elements under governing precedent.

The debtor's intent and the nature of the injury are critical.

A judgment based on intentional assault may therefore present different dischargeability issues from a judgment based on negligent driving.

7. Fraud Judgments

Section 523(a)(2) excepts certain debts obtained through false pretenses, false representations, or actual fraud.

A judgment arising from fraud may be nondischargeable when the statutory elements are established.

However, the word *fraud* in a complaint or judgment does not automatically resolve the bankruptcy question.

The bankruptcy court may need to determine whether the underlying findings satisfy § 523.

The particular type of fraud, creditor's reliance where required, and other statutory elements matter.

8. Default Judgments

A default judgment may be dischargeable or nondischargeable depending on the underlying debt.

The fact that the debtor failed to defend the lawsuit does not automatically establish nondischargeability.

However, the judgment may have preclusive consequences under applicable law.

The bankruptcy court must determine whether the issues necessary for nondischargeability were actually litigated or otherwise satisfy the governing preclusion rules.

The effect of a default judgment can differ depending on the issuing court and applicable law.

9. Collateral Estoppel in Dischargeability Proceedings

Issue preclusion, sometimes called collateral estoppel, may prevent relitigation of issues already determined in prior proceedings.

In *Grogan v. Garner*, 498 U.S. 279 (1991), the Supreme Court recognized that collateral estoppel principles apply in dischargeability proceedings.

But the prior judgment must satisfy the applicable preclusion requirements.

For example, a judgment containing specific findings of intentional fraud may establish facts relevant to § 523(a)(2).

A general judgment for breach of contract may not.

The bankruptcy court must examine the record and determine which issues were actually and necessarily decided.

10. Punitive Damages

Punitive damages may be awarded to punish and deter certain misconduct.

Their dischargeability depends on the underlying debt and applicable statutory exception.

In *Cohen v. de la Cruz*, 523 U.S. 213 (1998), the Supreme Court held that the nondischargeability of a fraud debt under § 523(a)(2)(A) extended to associated treble damages, attorney's fees, and other liability arising from the fraud.

The decision illustrates that nondischargeability may extend beyond direct compensatory damages.

However, punitive damages are not categorically nondischargeable merely because they are punitive.

The underlying statutory basis matters.

11. Judgments Arising From Drunk Driving

Section 523(a)(9) excepts qualifying debts for death or personal injury caused by the debtor's operation of a motor vehicle, vessel, or aircraft when operation was unlawful because of intoxication.

The statute contains specific requirements.

A judgment arising from an intoxicated-driving injury may therefore survive Chapter 7 even when an ordinary negligence judgment would be discharged.

The nature of the conduct and statutory elements must be established.

12. Judgments for Domestic Support

Domestic support obligations generally are nondischargeable under § 523(a)(5).

A judgment for unpaid child support or qualifying alimony ordinarily survives Chapter 7.

Other divorce-related obligations may fall within § 523(a)(15).

The substance of the obligation matters more than its label.

A property settlement judgment may require different analysis from a support judgment, particularly when comparing Chapter 7 and Chapter 13.

13. Governmental Penalty Judgments

Section 523(a)(7) excepts certain fines, penalties, and forfeitures payable to and for the benefit of governmental units and not constituting compensation for actual pecuniary loss.

A government judgment may therefore be nondischargeable when it satisfies the statutory requirements.

But not every government judgment is a penalty.

A judgment requiring reimbursement of actual losses may present different issues.

The nature of the obligation controls.

14. Judgment Liens Are Different From Judgment Debts

A judgment creditor may acquire a lien against real estate under applicable Maryland law.

The lien is distinct from the debtor's personal liability.

A Chapter 7 discharge may eliminate personal liability while leaving a valid judgment lien enforceable against property.

For example, a debtor may discharge a $45,000 credit card judgment but discover that the creditor's lien remains attached to the debtor's home.

The debtor may need to seek lien avoidance under § 522(f).

Discharge alone does not necessarily clear title.

15. Avoiding Judgment Liens Under § 522(f)

Section 522(f)(1)(A) permits avoidance of qualifying judicial liens to the extent they impair exemptions.

Maryland's increased residential-property exemption may expand the amount of judicial lien avoidance available to qualifying homeowners.

The statutory impairment formula must be applied.

The debtor ordinarily must file a motion and obtain a court order.

The lien may be avoided in full or in part.

The remedy is separate from discharge of the underlying judgment debt.

16. Wage Garnishments Based on Judgments

A judgment creditor may garnish wages before bankruptcy.

Filing Chapter 7 ordinarily stops further garnishment on a prepetition unsecured judgment while the automatic stay applies.

But wages already garnished may present a separate recovery opportunity.

Under §§ 522(h) and 547, a debtor may, in specified circumstances, recover qualifying preferential transfers when the trustee does not pursue them.

The ninety-day preference period, statutory monetary threshold, and available exemptions matter.

The debtor should preserve pay records and garnishment documents.

17. Bank Account Garnishments

A creditor may obtain legal process attaching funds in a debtor's bank account.

A bankruptcy filing may affect further collection under the automatic stay.

However, funds seized before filing raise additional questions.

The Supreme Court's decision in *City of Chicago v. Fulton*, 592 U.S. 154 (2021), held that mere retention of property seized before bankruptcy does not itself violate § 362(a)(3).

Turnover and other statutory remedies may still be relevant.

The debtor should not assume that filing automatically releases every prepetition attachment.

18. Pending Lawsuits When Bankruptcy Is Filed

Section 362(a) generally stays continuation of many lawsuits against the debtor involving prepetition claims.

The plaintiff may need to suspend proceedings.

However, the stay does not necessarily prohibit every lawsuit or proceeding.

Criminal matters, certain governmental regulatory actions, and other statutory exceptions may continue.

The debtor should identify all pending litigation in the bankruptcy schedules and statement of financial affairs.

19. Can a Plaintiff Continue a Lawsuit to Reach Insurance?

In some circumstances, a plaintiff may seek relief from the automatic stay to proceed against a debtor nominally for the purpose of establishing liability and recovering available insurance proceeds.

The plaintiff may agree not to enforce any resulting judgment against the debtor personally or against property of the bankruptcy estate.

The bankruptcy court may impose conditions.

The existence of insurance does not automatically eliminate the stay.

The plaintiff ordinarily should obtain appropriate relief when required.

20. What Happens to a Lawsuit After Discharge?

When a debt has been discharged, § 524 generally prohibits collection of the discharged personal liability.

However, a plaintiff may seek to establish liability for purposes of recovering from another legally responsible party, including an insurer, when permitted by law.

Section 524(e) provides that discharge of the debtor does not affect the liability of another entity for the same debt.

The procedural route depends on the underlying claim and applicable law.

A plaintiff should not assume that the debtor's discharge necessarily extinguishes every insurance-related claim.

21. Does Bankruptcy Affect Appeals?

A pending appeal involving a claim against the debtor may be subject to the automatic stay.

The treatment can depend on the nature of the underlying proceeding and the party seeking relief.

For example, an appeal from a judgment entered against the debtor may remain subject to the stay even when the debtor is the appellant.

The procedural posture alone does not necessarily determine whether § 362 applies.

The parties should evaluate the underlying action and applicable exceptions.

22. What If the Judgment Was Entered Shortly Before Bankruptcy?

A judgment entered shortly before bankruptcy may create additional issues.

The creditor may have obtained a lien, garnished wages, or received payments.

Some transfers may be avoidable under § 547.

A judgment lien may be avoidable under § 522(f) if it impairs an exemption.

The debtor should not assume that the judgment's recent entry automatically makes it invalid.

Each enforcement action requires separate analysis.

23. Can the Bankruptcy Court Reexamine the Judgment?

A bankruptcy court generally does not sit as an ordinary appellate court reviewing state-court judgments.

However, it may determine dischargeability under federal bankruptcy law.

Issue preclusion may limit relitigation of factual issues already decided.

The court must distinguish between impermissible collateral attacks on a judgment and permissible determinations concerning the judgment debt's bankruptcy treatment.

The prior court record may be important.

24. Why the Judgment Documents Matter

A debtor should provide bankruptcy counsel with the complaint, judgment, relevant orders, and available litigation records.

The underlying allegations and findings may determine whether the debt is dischargeable.

The attorney should also identify any recorded judgment liens, garnishments, attachments, or other enforcement proceedings.

A judgment amount alone does not provide enough information to evaluate bankruptcy consequences.

25. Why Judgment Creditors May File Adversary Proceedings

Certain creditors may seek determinations that their judgments are nondischargeable.

Under § 523(c) and Rule 4007(c), complaints involving specified fraud, fiduciary misconduct, and willful and malicious injury generally must be filed within the applicable deadline.

Other exceptions may operate differently.

The creditor must satisfy the statutory requirements and any applicable procedural rules.

A debtor should not assume that every judgment creditor can prevent discharge merely by filing an objection.

Conclusion

Many lawsuit judgments are dischargeable in Chapter 7 bankruptcy.

Ordinary credit card, medical debt, personal loan, and negligence judgments generally may be eliminated when no statutory exception applies.

But judgments arising from qualifying fraud, willful and malicious injury, intoxicated driving, domestic support, and certain governmental penalties may survive.

Valid judgment liens also may remain enforceable even when personal liability is discharged.

The critical question is not whether the creditor has a judgment. It is what the judgment represents, whether the debt falls within a statutory exception, and whether the creditor acquired enforceable property rights that survive bankruptcy.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 362 — Automatic stay.
- 11 U.S.C. § 522(f) — Judicial lien avoidance.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 524 — Discharge injunction and liability of other entities.
- 11 U.S.C. § 547 — Preferential transfers.
- Federal Rule of Bankruptcy Procedure 4007 — Dischargeability proceedings.

Maryland law

- Maryland Courts and Judicial Proceedings § 11-402 — Judgment liens.
- Maryland Courts and Judicial Proceedings § 11-504 — Exemptions.

Selected decisions

- *Grogan v. Garner*, 498 U.S. 279 (1991) — Addresses issue preclusion and the burden of proof in dischargeability litigation.
- *Kawaauhau v. Geiger*, 523 U.S. 57 (1998) — Distinguishes intentional injury from negligent or reckless conduct under § 523(a)(6).
- *Cohen v. de la Cruz*, 523 U.S. 213 (1998) — Addresses damages and other liability arising from nondischargeable fraud.

- *Brown v. Felsen*, 442 U.S. 127 (1979) — Addresses bankruptcy court consideration of the underlying nature of a judgment debt.
- *Archer v. Warner*, 538 U.S. 314 (2003) — Addresses the effect of settlement agreements on fraud-based nondischargeability.
- *Farrey v. Sanderfoot*, 500 U.S. 291 (1991) — Addresses judicial lien avoidance.
- *City of Chicago v. Fulton*, 592 U.S. 154 (2021) — Addresses retention of seized property and the automatic stay.

Gambling Debts in Bankruptcy: Casino Markers, Sports Betting, Credit Cards, and Brokerage Margin Debt

Belsky Bankruptcy Legal Library | Dischargeability, Consumer Debt, and Financial Risk

By Alan J. Belsky, Attorney at Law

Gambling Losses Are Not Automatically Nondischargeable in Bankruptcy

A person who has accumulated substantial debts through casino gambling, sports betting, online wagering, or speculative trading may assume that bankruptcy cannot eliminate those obligations.

That assumption is generally incorrect.

The Bankruptcy Code does not contain a blanket exception to discharge for gambling debts. Ordinary unsecured obligations incurred in connection with gambling may be dischargeable in Chapter 7, subject to the same statutory exceptions that apply to other debts.

However, gambling-related debts can present unusual legal problems.

Casino markers may involve negotiable instruments and state criminal laws. Credit card charges and cash advances may give rise to fraud allegations. Large gambling losses shortly before bankruptcy may prompt investigation of the debtor's financial affairs.

Brokerage margin debt presents additional issues involving secured loans, collateral liquidation, and securities transactions.

The central question is not whether the debtor lost money gambling. It is how the debt arose, what representations were made, what property secures it, and whether the debtor engaged in conduct that creates a statutory exception to discharge.

1. Gambling Debts Are Generally Subject to Ordinary Discharge Rules

Section 727 generally provides for discharge of qualifying prepetition debts in Chapter 7.

Section 523 identifies obligations that are excepted from discharge.

Gambling debt is not independently listed as a category that automatically survives bankruptcy.

For example, a debtor may borrow $20,000 through an ordinary unsecured personal loan and lose the proceeds gambling.

The debt may remain dischargeable unless the creditor establishes an applicable exception.

The fact that the debtor used the money unwisely does not necessarily make the debt fraudulent.

However, the circumstances surrounding the borrowing can change the result.

2. Casino Markers

Casinos sometimes extend credit through instruments commonly called *markers*.

A marker may represent a promise to repay money advanced for gambling.

Depending on the jurisdiction and the instrument's terms, a marker may be treated as a negotiable instrument, check, or other enforceable obligation.

The legal treatment varies by state.

A debtor who signs a marker may incur contractual liability separate from the gambling losses themselves.

The marker's enforceability and bankruptcy treatment depend on the governing law and circumstances.

3. Casino Markers and Criminal Exposure

Unpaid casino markers can present risks beyond ordinary civil collection.

Some jurisdictions treat qualifying casino markers as checks or similar instruments for purposes of bad-check laws.

A casino may pursue criminal remedies when the statutory elements are satisfied.

However, failure to repay a marker does not automatically establish a crime.

The relevant jurisdiction, instrument, debtor's conduct, and required criminal intent matter.

Bankruptcy generally does not stop criminal proceedings under § 362(b)(1).

A debtor facing possible criminal charges should not assume that filing Chapter 7 eliminates that exposure.

4. Are Casino Markers Dischargeable?

An ordinary casino marker obligation may be dischargeable in Chapter 7.

However, a casino may contend that the marker was obtained through fraud under § 523(a)(2).

For example, the casino may allege that the debtor obtained credit through materially false representations or knowingly used an instrument without intending to honor it.

The creditor must establish the applicable statutory elements.

A debtor's subsequent inability to pay does not necessarily prove fraudulent intent at the time the credit was obtained.

The debtor's financial circumstances and conduct when the marker was issued may be important.

5. Gambling With Credit Cards

A debtor may use credit cards to obtain cash advances or fund gambling transactions.

Ordinary credit card balances generally are dischargeable.

But recent charges may give rise to fraud allegations.

Section 523(a)(2)(A) addresses debts obtained through false pretenses, false representations, or actual fraud.

The creditor may argue that the debtor incurred charges without a genuine intention to repay.

The debtor may respond that repayment was intended but later became impossible.

The circumstances surrounding the transactions matter.

6. Recent Cash Advances

Section 523(a)(2)(C) establishes rebuttable presumptions of nondischargeability for certain cash advances obtained shortly before bankruptcy.

The applicable dollar thresholds are periodically adjusted.

A debtor who obtains substantial cash advances shortly before filing and uses the proceeds for gambling may face heightened dischargeability risk.

However, the presumption applies only when the statutory requirements are satisfied.

The debtor may present evidence rebutting the presumption.

The precise dates, amounts, and nature of the advances must be examined.

7. Gambling Losses and Fraudulent Intent

Fraud requires more than proof that the debtor made a financially irresponsible decision.

A debtor may genuinely intend to repay a loan while expecting future income or gambling winnings.

That expectation may be unrealistic, but unrealistic optimism does not automatically establish actual fraud.

Conversely, a debtor who knowingly misrepresents material facts to obtain credit may create nondischargeability exposure.

Courts examine the debtor's intent and surrounding circumstances.

The analysis should distinguish poor judgment from legally actionable fraud.

8. Sports Betting Debts

Sports betting may involve direct wagers, credit cards, bank transfers, or loans obtained from third parties.

A licensed sportsbook may require funds to be deposited before wagering.

In that situation, the debtor may owe the bank or credit card issuer rather than the sportsbook.

Other arrangements may involve credit or unpaid account balances.

The identity of the creditor and legal basis of the obligation must be established.

A gambling loss does not automatically create a dischargeable debt if no legally enforceable obligation remains.

9. Online Gambling Accounts

Online gambling platforms may maintain customer balances, deposits, and withdrawal rights.

A debtor who files bankruptcy must disclose qualifying financial interests in such accounts.

The account may contain funds that constitute property of the bankruptcy estate.

The debtor should not omit the account merely because it is associated with gambling.

Outstanding obligations to the platform, bank, or other lender require separate analysis.

10. Gambling Debts Owed to Friends or Family

A debtor may borrow money from relatives or friends to continue gambling or repay prior gambling losses.

A genuine unsecured loan may be dischargeable.

However, payments to relatives shortly before bankruptcy may create preference issues under § 547.

The one-year insider preference period may apply.

The debtor must disclose both the loan and qualifying repayments.

The fact that the creditor is a family member does not automatically make the obligation nondischargeable.

11. Gambling Debts and the Means Test

The means test under § 707(b) generally applies to individual debtors whose debts are primarily consumer debts.

Section 101(8) defines consumer debt as debt incurred primarily for personal, family, or household purposes.

Gambling-related obligations may be consumer debts depending on their purpose and circumstances.

A debtor should not assume that gambling debt is automatically nonconsumer debt because it involved an attempt to win money.

The classification requires examination of the transaction's purpose.

12. Can Gambling Losses Be Deducted as Living Expenses?

The means test permits specified deductions and expenses under the Bankruptcy Code.

Gambling losses generally should not be assumed to qualify as necessary household expenses.

A debtor who regularly spends substantial amounts gambling may face questions concerning the reasonableness of expenses and the debtor's financial conduct.

The debtor should report actual financial information accurately.

A budget should not characterize gambling expenditures as essential living expenses without a valid legal basis.

13. Gambling and Dismissal for Abuse

Section 707(b) permits dismissal or conversion of certain Chapter 7 cases involving primarily consumer debts when the statutory requirements for abuse are satisfied.

Even when the debtor passes the mechanical means test, § 707(b)(3) permits consideration of bad faith and the totality of financial circumstances.

Substantial gambling shortly before bankruptcy may be relevant.

However, gambling losses do not automatically establish abuse.

The debtor's income, debts, financial condition, and overall conduct must be considered.

14. Gambling and Denial of Discharge

Section 727 addresses circumstances in which a debtor may be denied the entire Chapter 7 discharge.

Gambling itself is not an independent ground for denial.

However, a debtor who conceals gambling accounts, destroys financial records, makes false statements, or fails to explain substantial losses may face discharge objections.

For example, a debtor who withdrew $100,000 shortly before filing may be required to explain what happened to the funds.

The debtor should preserve records of gambling transactions and losses.

15. Unexplained Loss of Assets

Section 727(a)(5) permits denial of discharge when the debtor fails to explain satisfactorily a loss of assets or deficiency of assets to meet liabilities.

Large gambling losses may prompt trustee questions.

A debtor may need to produce bank records, casino statements, sportsbook transaction histories, or other documentation.

The issue is not necessarily whether the debtor should have gambled.

It is whether the debtor can satisfactorily explain the disposition of substantial assets.

16. Brokerage Margin Debt

Brokerage margin debt arises when an investor borrows against securities or other qualifying collateral through a margin account.

The borrowed funds may be used to purchase securities or for other permitted purposes.

Margin borrowing is not necessarily gambling debt.

Even highly speculative investment activity must be analyzed according to the actual loan agreement, collateral arrangements, and purpose of the borrowing.

The broker may possess contractual and statutory rights to liquidate collateral when margin requirements are not satisfied.

The bankruptcy consequences depend on the secured obligation and applicable law.

17. Margin Calls and Forced Liquidation

A margin call generally occurs when the account's equity falls below required levels.

The brokerage firm may demand additional collateral or repayment.

Depending on the agreement and applicable rules, the firm may liquidate securities without obtaining the customer's prior consent.

A debtor who experiences forced liquidation may incur substantial losses.

The resulting deficiency may become an unsecured obligation.

The debtor should obtain account agreements, transaction histories, margin notices, and liquidation records.

18. Can a Margin Loan Deficiency Be Discharged?

A deficiency remaining after lawful liquidation of collateral may be dischargeable in Chapter 7, subject to applicable exceptions.

For example, an investor may borrow $100,000 on margin, experience a market decline, and remain liable for $35,000 after liquidation.

The deficiency may constitute an unsecured debt.

However, fraud, misrepresentation, or other statutory exceptions may affect dischargeability.

The broker's rights concerning collateral and securities transactions also require separate analysis.

19. Securities Safe Harbor Provisions

The Bankruptcy Code contains special provisions protecting certain securities-related transactions.

Sections 555, 559, and related provisions address specified contractual liquidation, termination, and acceleration rights.

Section 362(b) also contains exceptions relevant to qualifying financial contracts.

These provisions can limit the ordinary operation of the automatic stay.

A debtor should not assume that filing bankruptcy necessarily prevents a brokerage firm from liquidating securities under a qualifying protected arrangement.

The applicability of the safe harbors depends on the transaction and statutory definitions.

20. Investment Losses Versus Gambling Losses

Investment activity and gambling can share economic characteristics, including risk and uncertainty.

But legal classification should not depend solely on whether the debtor's conduct was speculative.

A margin loan used to purchase securities may be incurred for investment or profit-seeking purposes.

A loan used for recreational casino gambling may be incurred primarily for personal purposes.

The distinction can affect consumer-debt classification and means-test applicability.

The debtor's actual purpose and transaction structure matter.

21. Gambling With Business Funds

A business owner may use business money for personal gambling.

The consequences depend on whether the business is a sole proprietorship, LLC, corporation, or other entity.

Misuse of entity funds may create separate claims involving fiduciary duties, conversion, embezzlement, or other misconduct.

Certain obligations arising from such conduct may be nondischargeable under § 523(a)(4) or (6).

The fact that the money was lost gambling does not resolve the legal character of the debt.

22. Gambling and Divorce

Gambling losses may affect marital finances and divorce-related obligations.

A spouse may incur substantial gambling debt without the other spouse's knowledge.

The legal consequences depend on account ownership, contractual liability, marital property law, and divorce orders.

A divorce agreement allocating gambling debts generally does not automatically release either spouse from obligations owed to third-party creditors.

The bankruptcy treatment of reimbursement or indemnification obligations may also implicate § 523(a)(15).

23. Gambling Winnings and Bankruptcy Estate Property

A debtor may have funds in a gambling account or a right to receive winnings when bankruptcy is filed.

Those interests generally must be disclosed.

Winnings acquired after filing may require separate analysis.

In Chapter 7, the relevant question may be whether the winnings arose from prepetition property interests or postpetition activity.

In Chapter 13, § 1306 provides broader treatment of certain postpetition property.

A debtor should not assume that gambling winnings are excluded from the estate merely because they were received after filing.

24. Gambling Records and Trustee Investigation

A Chapter 7 trustee may investigate substantial gambling activity.

The trustee may request bank statements, casino records, sportsbook histories, credit card statements, and other documents.

The debtor must cooperate with lawful requests.

Accurate records may help distinguish genuine gambling losses from unexplained transfers or concealed assets.

A debtor who has lost substantial sums should not assume that an unsupported statement that the money was gambled away will always satisfy § 727(a)(5).

25. Why Gambling Debts Require Careful Prebankruptcy Analysis

Gambling-related debt may be dischargeable, but the surrounding circumstances can create complications.

Counsel should determine the identity of each creditor, the legal basis of the debt, the timing of borrowing, and whether the creditor may assert fraud.

Casino markers require examination of the governing jurisdiction and potential criminal consequences.

Margin loans require analysis of collateral and securities safe harbor provisions.

The debtor's records and recent financial activity may also affect the trustee's investigation.

Conclusion

Gambling debts are not categorically nondischargeable in Chapter 7 bankruptcy.

Ordinary unsecured loans, credit card balances, and certain casino obligations may be discharged when no statutory exception applies.

However, recent cash advances, fraudulent representations, casino marker enforcement, and inadequate financial records can create serious complications.

Brokerage margin debt requires separate analysis because it involves secured lending and potentially protected securities transactions.

The relevant question is not whether the debtor gambled or invested unsuccessfully. It is how the obligation arose, whether the creditor possesses enforceable collateral rights, and whether the debtor's conduct satisfies a statutory exception to discharge.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 101(8) — Consumer debt definition.
- 11 U.S.C. § 523(a)(2) — Fraud and certain recent credit transactions.
- 11 U.S.C. § 523(a)(4), (6) — Fiduciary misconduct and willful and malicious injury.
- 11 U.S.C. § 555 — Contractual rights concerning securities contracts.

- 11 U.S.C. § 559 — Repurchase agreements.
- 11 U.S.C. § 707(b) — Dismissal for abuse.
- 11 U.S.C. § 727 — Denial of discharge.

Selected decisions

- *Grogan v. Garner*, 498 U.S. 279 (1991) — Establishes the burden of proof for dischargeability exceptions.
- *Field v. Mans*, 516 U.S. 59 (1995) — Addresses reliance in fraud-based dischargeability.
- *Husky International Electronics, Inc. v. Ritz*, 578 U.S. 355 (2016) — Addresses actual fraud under § 523(a)(2)(A).
- *In re Rembert*, 141 F.3d 277 (6th Cir. 1998) — Addresses dischargeability of credit card debt incurred through gambling and the debtor's subjective intent to repay.
- *In re Anastas*, 94 F.3d 1280 (9th Cir. 1996) — Addresses credit card debt and fraudulent intent.
- *In re Eashai*, 87 F.3d 1082 (9th Cir. 1996) — Addresses credit card fraud and implied representations.

Day Trading, Options, Futures, and Margin Accounts in Bankruptcy: Trading Losses, Broker Claims, and the Risk of Losing a Discharge

Belsky Bankruptcy Legal Library | Investment Losses, Business Debts, and Dischargeability

By Alan J. Belsky, Attorney at Law

Losing Money Trading Securities Does Not Automatically Prevent Bankruptcy Relief

Individuals who engage in day trading, options trading, futures transactions, or other speculative investment activities can accumulate substantial losses in a relatively short period.

Those losses may exceed the trader's available cash, retirement savings, or other assets. When trading involves borrowed money or margin, the investor may remain personally liable even after the brokerage firm liquidates the account.

A person who has suffered substantial trading losses may believe that bankruptcy is unavailable because the debts arose from speculation rather than ordinary household expenses.

That assumption is generally incorrect.

Federal bankruptcy law does not automatically prohibit discharge of debts arising from unsuccessful securities trading.

However, trading activity can create unusual bankruptcy issues involving secured obligations, securities contracts, tax losses, financial records, and the classification of debts as consumer or nonconsumer obligations.

The trustee may also investigate substantial losses occurring shortly before bankruptcy.

The distinction between unsuccessful trading and legally actionable misconduct is essential.

1. Day Trading Is Not Automatically Gambling for Bankruptcy Purposes

Day trading generally involves buying and selling securities over short periods to profit from price movements.

The activity may involve stocks, exchange-traded funds, options, futures, or other financial instruments.

Although day trading can be highly speculative, bankruptcy law does not automatically classify it as gambling.

The legal treatment depends on the actual transactions, financing arrangements, and purposes for which debts were incurred.

A trader may suffer substantial investment losses without engaging in fraud or other conduct that prevents discharge.

The fact that the activity was risky does not itself establish nondischargeability.

2. Trading Losses Versus Trading Debts

A financial loss is not necessarily a debt.

For example, an investor who purchases $50,000 in stock using personal funds and later sells it for $10,000 has suffered a $40,000 loss.

But the loss itself does not necessarily create an obligation to a creditor.

By contrast, an investor who borrows $50,000 on margin and suffers losses may remain obligated to repay a deficiency.

The bankruptcy analysis concerns the debtor's actual liabilities and property interests.

A debtor should distinguish losses of personal capital from debts owed to brokerage firms, banks, or other creditors.

3. Margin Accounts

A margin account permits an investor to borrow against qualifying securities or other collateral.

The brokerage firm ordinarily holds a security interest in account assets.

The margin agreement may authorize the firm to demand additional collateral, liquidate securities, or take other action when margin requirements are not satisfied.

A debtor should review the actual agreement.

The broker's rights may extend beyond the investor's understanding of the account's ordinary trading features.

4. Margin Calls

A margin call occurs when the account fails to satisfy applicable equity or collateral requirements.

The broker may demand additional funds or securities.

Depending on the agreement and governing rules, the firm may liquidate positions without waiting for the customer to respond.

The investor may experience substantial losses during rapid market movements.

A margin call does not automatically establish that the investor engaged in misconduct.

It ordinarily reflects the account's failure to satisfy margin requirements.

5. Deficiency Balances After Liquidation

A brokerage firm may liquidate account collateral but still claim a remaining deficiency.

Example

An investor borrows $150,000 through a margin account.

A sharp market decline causes the broker to liquidate the securities.

After applying the liquidation proceeds, the broker claims a $45,000 deficiency.

That deficiency may constitute an unsecured personal obligation.

In an individual Chapter 7 case, it may be dischargeable unless an applicable exception exists.

The broker's contractual rights and calculation of the deficiency should be examined.

6. Can a Broker Claim Fraud?

A broker may allege fraud when the investor obtained credit through materially false representations or other qualifying misconduct.

Section 523(a)(2) addresses certain debts obtained through false pretenses, false representations, or actual fraud.

For example, a broker may contend that an investor falsified financial information to obtain margin privileges.

The creditor must establish the applicable statutory elements.

Ordinary trading losses or failure to meet a margin call do not automatically prove fraud.

7. Options Trading

Options contracts may create rights or obligations to buy or sell underlying assets at specified prices.

A purchaser of an option generally risks the premium paid, subject to the particular transaction.

An option writer may face substantially different exposure.

For example, writing uncovered call options may create significant obligations if the underlying security rises sharply.

Assignment, exercise, margin requirements, and forced liquidation may produce liabilities.

The bankruptcy treatment depends on the contracts and resulting obligations.

8. Short Selling

Short selling involves selling borrowed securities with an obligation to return equivalent securities.

A trader may incur substantial losses if the security's price rises.

The broker may require additional margin or close the position.

A resulting deficiency may become a claim against the debtor.

The transaction may also fall within special securities-related provisions of the Bankruptcy Code.

The debtor should preserve records identifying the short position, borrow arrangements, collateral, and liquidation.

9. Futures Contracts

Futures trading involves contractual obligations concerning commodities, financial instruments, or other underlying interests.

Futures positions may be highly leveraged.

Rapid price movements can produce substantial margin requirements and losses.

The Bankruptcy Code contains specialized provisions governing commodity contracts and related transactions.

Section 556 addresses certain contractual liquidation, termination, and acceleration rights.

The debtor should not assume that futures positions receive the same treatment as ordinary unsecured loans.

10. Securities Safe Harbor Provisions

The Bankruptcy Code contains exceptions and protections for specified financial contracts.

Sections 555, 556, and related provisions protect certain contractual rights concerning securities and commodity contracts.

Section 362(b) contains corresponding automatic-stay exceptions.

These provisions can permit qualifying counterparties to liquidate, terminate, or accelerate contracts notwithstanding the bankruptcy filing.

The applicability depends on the statutory definitions and transaction structure.

A debtor should not assume that bankruptcy automatically freezes every trading position.

11. Repurchase Agreements and Other Financial Contracts

Section 559 addresses certain rights concerning repurchase agreements.

Other provisions govern swap agreements, master netting agreements, and related financial transactions.

These rules are particularly important for sophisticated traders and investors using complex products.

The ordinary consumer bankruptcy framework may not fully describe the counterparty's rights.

The relevant contracts and statutory definitions must be examined.

12. Consumer Versus Nonconsumer Debt

Section 101(8) defines consumer debt as debt incurred primarily for personal, family, or household purposes.

The classification matters because § 707(b) generally applies to individual debtors whose debts are primarily consumer debts.

Debts incurred primarily for investment or profit-seeking purposes may qualify as nonconsumer debts.

For example, a margin loan used to purchase securities with the objective of earning investment profits may present a nonconsumer classification argument.

However, the debtor's actual purpose and circumstances control.

A debtor should not assume that every brokerage obligation is automatically nonconsumer debt.

13. Why Nonconsumer Classification Matters

A debtor whose debts are primarily nonconsumer obligations generally is not subject to the ordinary § 707(b) means-test presumption.

This can materially affect Chapter 7 eligibility.

For example, an individual with substantial income may have accumulated most liabilities through failed business ventures and investment borrowing.

If the debts are primarily nonconsumer, the ordinary consumer means-test provisions may not apply.

However, the debtor remains subject to other Bankruptcy Code requirements, including disclosure obligations and potential dismissal for cause under § 707(a).

The classification should be supported by the actual purpose of the debts.

14. Does Frequent Trading Make the Debtor a Business?

Not necessarily.

Federal income tax law distinguishes investors from traders in securities under particular circumstances.

A person may engage in substantial trading activity without qualifying as a trader for federal income tax purposes.

Conversely, qualifying trader status for tax purposes does not automatically determine the consumer or nonconsumer character of every debt.

The tax and bankruptcy inquiries involve different legal standards.

The debtor's trading history, purpose, and financial arrangements should be examined separately.

15. Trader Tax Status

For federal income tax purposes, a taxpayer may qualify as a trader in securities when the activity satisfies applicable legal requirements.

The IRS examines factors such as the frequency, continuity, and regularity of trading and the taxpayer's objective of profiting from short-term market movements.

Trader status may affect the treatment of business expenses.

However, it does not automatically eliminate the limitations governing capital losses.

The debtor should not assume that frequent trading alone establishes a deductible trade or business.

16. The Mark-to-Market Election

Internal Revenue Code § 475(f) permits qualifying traders to make a mark-to-market election under specified circumstances.

When validly made, the election can materially affect the tax treatment of securities gains and losses.

The election is subject to timing and procedural requirements.

A taxpayer generally cannot retroactively obtain the desired treatment merely because substantial losses occurred.

The bankruptcy consequences may also involve tax attributes and the ownership of tax claims.

A debtor with significant trading losses should consult qualified tax counsel or an accountant concerning the applicable election and reporting requirements.

17. Capital Loss Limitations

For taxpayers who do not qualify for different treatment, securities trading losses generally are subject to capital gain and loss rules.

Under Internal Revenue Code § 1211(b), individuals generally may deduct capital losses against capital gains plus a limited amount of ordinary income each year.

Unused capital losses may be carried forward under applicable rules.

A debtor who lost $200,000 trading securities should not assume that the entire loss can be deducted immediately against wages or other ordinary income.

The tax consequences require separate analysis.

18. Wash Sale Rules

Internal Revenue Code § 1091 generally disallows certain losses when substantially identical securities are acquired within the statutory period surrounding a loss sale.

These are commonly called wash sales.

Frequent traders may generate significant wash-sale adjustments.

The resulting taxable gain or loss may differ substantially from the economic gain or loss shown on a brokerage account summary.

The debtor should preserve detailed transaction records and tax statements.

Wash-sale issues may materially affect anticipated tax liabilities or refunds.

19. Trading Losses Shortly Before Bankruptcy

A debtor who loses substantial money trading shortly before filing may face trustee questions.

The trustee may investigate the source of funds, transfers, account balances, and disposition of assets.

The fact that the debtor lost money through trading does not automatically establish misconduct.

However, the debtor must provide accurate information and preserve sufficient records.

Large unexplained losses may create problems under § 727.

20. Failure to Explain Loss of Assets

Section 727(a)(5) permits denial of discharge when the debtor fails to explain satisfactorily a loss of assets or deficiency of assets to meet liabilities.

For example, a debtor may have possessed $300,000 in investments six months before bankruptcy but report only $5,000 in remaining assets.

The trustee may request an explanation.

Brokerage statements, trade confirmations, margin liquidation records, and tax documents may establish what occurred.

A debtor should not assume that a general statement that the market went down will always be sufficient.

21. Failure to Maintain Records

Section 727(a)(3) addresses inadequate financial records under specified circumstances.

A debtor engaged in substantial trading may reasonably be expected to maintain records sufficient to explain financial transactions.

Electronic brokerage statements ordinarily provide detailed histories.

Failure to preserve or obtain those records can complicate the case.

The debtor's sophistication, trading volume, and circumstances may affect the analysis.

22. Transfers Between Brokerage Accounts

A debtor may transfer cash or securities between brokerage accounts shortly before bankruptcy.

Such transfers generally must be disclosed when required.

The trustee may investigate whether the assets remain owned by the debtor or were transferred to another person.

Transfers to relatives or other parties may raise avoidance issues.

Moving assets between accounts does not necessarily change their bankruptcy character.

The debtor should preserve transfer records.

23. Trading With Retirement Funds

A debtor may conduct securities trading within an IRA or other retirement account.

Qualifying retirement accounts may receive substantial bankruptcy protection.

However, withdrawals, prohibited transactions, or other conduct may affect the account's tax status and legal protection.

A debtor should not assume that all trading-related losses or liabilities inside retirement accounts receive identical treatment.

The account structure and applicable retirement laws matter.

24. Trading After Filing Chapter 7

In Chapter 7, the debtor generally cannot freely trade assets belonging to the bankruptcy estate.

The trustee may control qualifying prepetition securities and brokerage accounts.

Postpetition earnings from the debtor's personal services ordinarily receive different treatment under § 541(a)(6).

However, proceeds or appreciation of estate property may remain estate property.

The debtor should not trade or liquidate estate assets without appropriate authority.

25. Trading During Chapter 13

Chapter 13 generally includes certain postpetition earnings and property under § 1306.

A debtor who engages in significant trading during a Chapter 13 plan may create issues concerning disposable income, plan feasibility, and estate property.

Large trading losses may impair the debtor's ability to make plan payments.

Trading gains may affect the debtor's financial circumstances and potentially the treatment of creditors.

The debtor should disclose material changes and comply with applicable court orders.

26. Broker Claims and Account Agreements

A brokerage firm's claim may include margin principal, interest, liquidation charges, fees, and other contractual amounts.

The debtor should obtain the governing agreements and transaction records.

The enforceability and amount of the claim may depend on contract law, securities regulation, and applicable bankruptcy provisions.

The broker's account statement should not automatically be accepted as resolving every legal issue.

A debtor may have defenses concerning the calculation or enforcement of the obligation.

27. When Day Trading May Support a Chapter 7 Filing

An individual may incur substantial nonconsumer obligations through failed trading activity.

If those obligations are dischargeable and the debtor possesses limited nonexempt property, Chapter 7 may provide meaningful relief.

The debtor may also fall outside the ordinary consumer means-test presumption if debts are primarily nonconsumer.

However, the debtor must disclose trading accounts, explain losses, preserve records, and identify any secured or nondischargeable obligations.

The appropriate bankruptcy strategy depends on the complete financial picture.

Conclusion

Day trading, options, futures, and margin borrowing can produce substantial financial losses, but those losses do not automatically prevent bankruptcy relief.

The legal consequences depend on the nature of the obligations, collateral arrangements, securities contracts, and debtor's conduct.

Margin deficiencies may be dischargeable, while qualifying securities and commodity counterparties may possess special liquidation rights.

Trading-related debts may also be nonconsumer obligations, potentially affecting Chapter 7 means testing.

The debtor's financial records are particularly important when substantial assets have been lost shortly before filing.

Unsuccessful trading is not itself bankruptcy fraud. The greater risks arise when the debtor cannot account for substantial losses, conceals assets, misrepresents financial information, or improperly uses property belonging to the bankruptcy estate.

Related Bankruptcy Cases and Authorities

Federal bankruptcy statutes

- 11 U.S.C. § 101(8) — Consumer debt definition.
- 11 U.S.C. § 362(b) — Automatic-stay exceptions for specified financial contracts.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 555 — Securities contract protections.
- 11 U.S.C. § 556 — Commodity contract protections.
- 11 U.S.C. § 559 — Repurchase agreement protections.
- 11 U.S.C. § 707(b) — Consumer-debt abuse provisions.
- 11 U.S.C. § 727 — Denial of discharge.

Federal tax statutes

- 26 U.S.C. § 475 — Mark-to-market accounting.
- 26 U.S.C. § 1091 — Wash-sale rules.
- 26 U.S.C. § 1211 — Capital loss limitations.

Selected decisions

- *Grogan v. Garner*, 498 U.S. 279 (1991) — Addresses the burden of proof for nondischargeability.
- *In re Bane*, 720 F.3d 465 (4th Cir. 2013) — Addresses fraudulent transfers and denial of discharge.
- *In re Stewart*, 175 F.3d 796 (10th Cir. 1999) — Addresses consumer versus nonconsumer debt classification.
- *In re Booth*, 858 F.2d 1051 (5th Cir. 1988) — Discusses debt incurred with a profit motive and consumer debt classification.
- Cox v. Lansdowne (In re Cox), 904 F.2d 1399 (9th Cir. 1990) — Addresses failure to maintain financial records and justification under § 727(a)(3), including the relevance of a debtor’s reliance on a spouse; it is not a § 727(a)(5) loss-of-assets holding.
- *In re Chalik*, 748 F.2d 616 (11th Cir. 1984) — Addresses materiality of false oaths and omissions.

Bankruptcy and Civil Lawsuits: What Happens to Pending Cases, Appeals, Counterclaims, and Insurance-Only Claims?

Belsky Bankruptcy Legal Library | Civil Litigation and the Automatic Stay

By Alan J. Belsky, Attorney at Law

Bankruptcy Can Stop a Lawsuit Without Necessarily Ending the Dispute

When a party to a civil lawsuit files bankruptcy, the consequences can be immediate and substantial.

Under 11 U.S.C. § 362, a qualifying bankruptcy filing ordinarily triggers an automatic stay that prohibits many actions against the debtor and property of the bankruptcy estate.

But the stay does not apply identically to every lawsuit.

A case in which the debtor is being sued may be stayed, while a lawsuit brought by the debtor may continue under different rules. Counterclaims, appeals, multiple defendants, and insurance coverage can complicate the analysis.

In some circumstances, a plaintiff may obtain limited relief from the automatic stay to establish liability against the debtor solely for purposes of recovering available insurance proceeds.

The bankruptcy discharge may also affect whether litigation can continue after the bankruptcy case concludes.

Understanding these distinctions is essential for debtors, creditors, and attorneys involved in pending civil litigation.

1. The Automatic Stay and Pending Lawsuits

Section 362(a)(1) generally stays commencement or continuation of judicial, administrative, or other proceedings against the debtor that were or could have been commenced before bankruptcy, or that seek recovery of prepetition claims.

The stay ordinarily arises automatically when the petition is filed.

A plaintiff does not necessarily need to receive formal notice before the stay becomes legally effective.

However, notice can affect remedies for violations.

The stay is subject to statutory exceptions and limitations.

2. Lawsuits Against the Debtor

A civil lawsuit seeking damages from the debtor for a prepetition claim generally is stayed.

For example, a creditor may have filed a breach-of-contract action seeking $75,000.

If the defendant files Chapter 7, the plaintiff ordinarily must stop prosecuting the action while the stay applies, unless relief or an exception permits continuation.

The lawsuit is not necessarily dismissed merely because bankruptcy was filed.

The stay generally suspends further proceedings.

3. Lawsuits Filed by the Debtor

The automatic stay ordinarily does not prohibit a debtor from prosecuting a lawsuit that the debtor initiated.

However, the claim may become property of the bankruptcy estate.

In Chapter 7, the trustee may acquire authority to control a prepetition cause of action.

For example, a debtor who filed a personal injury lawsuit before bankruptcy may lose exclusive control over settlement and litigation decisions.

The issue is not simply whether the stay applies.

The ownership and administration of the claim must also be considered.

4. Counterclaims Against the Debtor

Counterclaims can complicate the analysis.

A debtor may have initiated a lawsuit, but the defendant may assert counterclaims seeking affirmative relief against the debtor.

Those counterclaims may be subject to the automatic stay.

The debtor's affirmative claim and the defendant's counterclaim may therefore receive different treatment.

Courts may need to determine whether particular defenses, recoupment arguments, or requests for affirmative relief are stayed.

The label attached to a pleading does not necessarily control.

5. Defensive Claims and Recoupment

A defendant may assert defenses to reduce or defeat the debtor's claim.

Such defenses may be treated differently from affirmative claims seeking recovery from the debtor.

Recoupment generally concerns adjustment of obligations arising from the same transaction.

Setoff ordinarily involves mutual obligations arising from separate transactions.

The distinction can affect the automatic stay.

A defendant should not assume that every defensive assertion is prohibited merely because the plaintiff filed bankruptcy.

Nor should a defendant use a nominal defense to pursue an otherwise stayed affirmative recovery.

6. Lawsuits Involving Multiple Defendants

A civil action may involve several defendants, only one of whom files bankruptcy.

The automatic stay generally protects the debtor, not every nonfiling codefendant.

For example, a personal injury lawsuit may name a driver, employer, and vehicle owner.

If the driver files Chapter 7, the lawsuit may continue against the employer or owner, subject to applicable law.

However, unusual circumstances may justify broader relief.

The effect on nondebtors depends on the nature of the claims and the relevant court orders.

7. The Fourth Circuit's *A.H. Robins* Decision

In *A.H. Robins Co. v. Piccinin*, 788 F.2d 994 (4th Cir. 1986), the Fourth Circuit recognized that unusual circumstances may justify extending bankruptcy-related protection to certain nondebtor parties.

The decision involved litigation associated with the Dalkon Shield.

The court discussed circumstances in which there is such an identity between the debtor and a nondebtor that a judgment against the nondebtor would effectively operate as a judgment against the debtor.

The decision does not establish a general rule that bankruptcy automatically stays litigation against all codefendants.

The exception is limited and fact-specific.

8. Pending Appeals

A bankruptcy filing may affect an appeal arising from litigation against the debtor.

The stay's application generally depends on the nature of the underlying proceeding rather than simply identifying which party filed the appeal.

For example, a debtor may appeal an adverse money judgment.

Although the debtor is the appellant, the appeal may still be treated as a continuation of a proceeding against the debtor.

Conversely, an appeal arising from a lawsuit originally brought by the debtor may receive different treatment.

The procedural posture and underlying claim must be examined.

9. Does the Stay Apply to Federal and State Courts?

Yes.

The automatic stay is federal law and generally applies to covered proceedings in state and federal courts.

A Maryland circuit court, district court, or federal district court ordinarily must respect the stay when it applies.

The debtor should provide notice of the bankruptcy filing.

However, the bankruptcy court ordinarily determines questions concerning relief from the stay.

A state-court litigant should not assume that the state court can independently disregard the stay because the underlying lawsuit was filed there.

10. Criminal and Governmental Regulatory Proceedings

Section 362(b)(1) generally excepts criminal proceedings from the automatic stay.

Section 362(b)(4) excepts certain governmental police and regulatory proceedings.

These exceptions may permit actions involving criminal enforcement, public safety, licensing, or regulatory compliance to continue.

However, the governmental regulatory exception generally does not authorize enforcement of a money judgment merely because the creditor is a government agency.

The purpose and nature of the proceeding matter.

11. Insurance-Only Litigation

A plaintiff may have a claim against a debtor whose liability is covered by insurance.

The debtor may receive a bankruptcy discharge, but the insurer may remain contractually obligated to provide coverage.

Section 524(e) provides that discharge of the debtor does not affect the liability of another entity for the same debt.

In appropriate circumstances, a plaintiff may seek to continue litigation against the debtor nominally for the limited purpose of establishing liability and recovering available insurance proceeds.

The plaintiff generally should not assume that the automatic stay can be disregarded merely because insurance exists.

12. Motions for Limited Relief From Stay

Section 362(d) permits a party in interest to request relief from the automatic stay.

A plaintiff may seek an order permitting continuation of a pending lawsuit solely to determine liability and damages within available insurance coverage.

The proposed relief may expressly prohibit collection against the debtor personally or against estate property.

The bankruptcy court may consider whether continuation would prejudice the debtor or estate and whether the litigation can proceed without interfering with bankruptcy administration.

The court may impose appropriate conditions.

13. Why Insurance Coverage Matters

A liability insurance policy may provide defense and indemnity benefits.

The policy itself may constitute property of the bankruptcy estate in certain circumstances.

The treatment of policy proceeds can depend on the nature of the coverage, the insured parties, and the claims.

For example, a policy covering multiple insureds or claims may present allocation concerns.

The plaintiff should not assume that every dollar of insurance proceeds is necessarily available outside bankruptcy administration.

14. Can a Plaintiff Obtain a Judgment Against the Debtor After Discharge?

In appropriate circumstances, litigation may continue nominally against the discharged debtor to establish liability for purposes of recovering from an insurer or another legally responsible party.

However, the plaintiff must avoid prohibited collection of the discharged personal obligation.

The procedural requirements depend on applicable law and court orders.

A plaintiff may need relief from the stay while the stay remains effective.

After discharge, § 524 governs the injunction against personal collection.

The distinction between establishing liability and enforcing personal liability is critical.

15. The Effect of Discharge on Pending Litigation

A Chapter 7 discharge generally eliminates personal liability for qualifying prepetition debts.

The discharge injunction may prohibit further prosecution of a lawsuit to collect the discharged debt personally.

However, claims against nondebtors, surviving liens, and certain insurance-related proceedings may remain viable.

A creditor should determine whether the underlying debt was discharged and whether continued litigation serves a legally permissible purpose.

16. What If the Debt Is Nondischargeable?

Some debts survive bankruptcy under § 523.

For example, qualifying debts arising from fraud, willful and malicious injury, domestic support, or certain other statutory categories may remain enforceable.

A creditor may seek a dischargeability determination when required.

The existence of a pending state-court judgment does not necessarily resolve the bankruptcy issue.

The applicable statutory exception and procedural deadlines must be examined.

17. The Effect of Bankruptcy on Statutes of Limitations

Bankruptcy may affect limitation periods.

Section 108(c) addresses certain deadlines for commencing or continuing civil actions against the debtor when applicable nonbankruptcy law fixes a period for doing so.

The statute provides a limited extension under specified circumstances.

However, § 108(c) does not automatically suspend every statute of limitations for the entire duration of the bankruptcy.

The interaction with state-law tolling provisions must be considered.

A plaintiff should not assume that a bankruptcy filing indefinitely preserves an otherwise expiring claim.

18. What If the Plaintiff's Limitations Period Is About to Expire?

A plaintiff whose claim is approaching the limitations deadline should evaluate § 108(c) promptly.

The automatic stay may prevent filing or continuing certain proceedings against the debtor.

But the plaintiff must determine the applicable extension and any state-law tolling.

The statute's thirty-day provision can be particularly important.

The plaintiff should not rely on an informal assumption that limitations stops running automatically.

19. Claims Against Nonfiling Defendants

When only one defendant files bankruptcy, the plaintiff may be able to continue pursuing other defendants.

For example, a plaintiff may sue a corporation and its individual officer.

If the officer files bankruptcy, the action against the corporation may continue unless an applicable order or unusual circumstance provides otherwise.

The plaintiff should consider whether proceeding against the nondebtor will affect estate property, insurance coverage, or indemnification rights.

The stay's scope must be evaluated carefully.

20. Third-Party Claims and Indemnification

A defendant may possess contractual or equitable indemnification rights against a debtor.

The bankruptcy filing may affect prosecution of those claims.

The indemnification obligation may constitute a contingent prepetition claim.

The creditor may need to file a proof of claim or seek appropriate relief.

The existence of a contingent obligation does not necessarily eliminate the automatic stay.

21. Discovery Directed to the Debtor

Discovery involving a debtor can raise difficult questions.

A nondebtor defendant may wish to obtain testimony or documents from the debtor in litigation that continues against other parties.

Whether the discovery violates the automatic stay depends on the purpose and effect of the request.

Discovery directed solely to obtain evidence from a debtor as a nonparty may present different issues from discovery designed to advance a stayed claim against the debtor.

The court may need to address the permissible scope.

22. What If a Judgment Is Entered in Violation of the Stay?

A judgment entered in violation of the automatic stay may be subject to challenge.

Maryland bankruptcy decisions have treated acts violating the stay as void, subject to the bankruptcy court's power to annul the stay under § 362(d). The void-versus-voidable characterization has divided courts and should not be presented as a categorical published Fourth Circuit holding. In either event, parties should seek a determination of the stay's effect and any requested annulment rather than treat the judgment as enforceable by assumption.

The parties should not assume that a state-court judgment entered during the stay is enforceable merely because no immediate objection was raised.

However, the actual existence and scope of the stay must be established.

23. Annulment of the Automatic Stay

Section 362(d) permits the bankruptcy court to grant relief from the stay, including annulment.

Annulment may operate retroactively in appropriate circumstances.

Courts consider the relevant facts and equitable considerations.

A party who acted without knowledge of the bankruptcy may seek annulment, but lack of notice does not automatically entitle the party to relief.

The remedy is discretionary and fact-specific.

24. Why Litigation Counsel Must Be Notified Promptly

A debtor involved in civil litigation should identify every pending case when consulting bankruptcy counsel.

The bankruptcy attorney should obtain the pleadings, docket information, and relevant orders.

Litigation counsel should receive prompt notice of the bankruptcy filing.

The parties may need to file notices of bankruptcy in pending courts and evaluate the scope of the stay.

Failure to coordinate can result in improper litigation activity, missed deadlines, or unauthorized settlements.

25. Why Bankruptcy Does Not Necessarily End the Lawsuit

Bankruptcy may suspend litigation, discharge personal liability, or transfer control of a claim to the trustee.

But it does not necessarily resolve every underlying dispute.

Claims against nonfiling parties may continue.

Insurance-related litigation may remain viable.

Certain nondischargeable obligations may still be litigated.

The appropriate procedural path depends on the claim, parties, insurance, and bankruptcy relief obtained.

Conclusion

The automatic stay can substantially affect civil litigation, but its application depends on the nature of the proceeding.

Lawsuits against the debtor generally receive different treatment from lawsuits brought by the debtor.

Counterclaims, appeals, multiple defendants, and insurance coverage create additional issues.

In appropriate circumstances, plaintiffs may obtain limited relief from the stay to establish liability and recover available insurance proceeds without pursuing the debtor personally.

Bankruptcy should not be treated as automatically terminating every pending lawsuit. The parties must determine which claims are stayed, who controls them, and what relief remains available.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 362 — Automatic stay and relief from stay.
- 11 U.S.C. § 108(c) — Certain limitations-period extensions.
- 11 U.S.C. § 323 — Trustee as estate representative.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 524(e) — Effect of discharge on liability of other entities.

Selected decisions

- *A.H. Robins Co. v. Piccinin*, 788 F.2d 994 (4th Cir. 1986) — Addresses unusual circumstances supporting protection of nondebtor parties.
- *Williford v. Armstrong World Industries, Inc.*, 715 F.2d 124 (4th Cir. 1983) — Discusses the limited circumstances in which nondebtor litigation may be stayed.
- In re Midway Airlines Corp., 283 B.R. 846 (E.D.N.C. 2002) — Addresses the automatic stay and the governmental police-power exception in an unpaid-wage proceeding; it is not an Illinois bankruptcy decision about insurance-only litigation.

- *In re Jet Florida Systems, Inc.*, 883 F.2d 970 (11th Cir. 1989) — Addresses nominal litigation against a discharged debtor to establish insurance liability.
- *In re Edgeworth*, 993 F.2d 51 (5th Cir. 1993) — Addresses insurance proceeds and the effect of discharge on claims against an insurer.
- *In re Gruntz*, 202 F.3d 1074 (9th Cir. 2000) (en banc) — Addresses the relationship between bankruptcy jurisdiction and state-court proceedings.
- *In re Schwartz*, 954 F.2d 569 (9th Cir. 1992) — Addresses actions taken in violation of the automatic stay.

Bankruptcy and Medical Bills: Hospital Charges, Health Insurance Reimbursement, Medical Liens, and Why Healthcare Debt Is Usually Dischargeable

Belsky Bankruptcy Legal Library | Medical Debt, Insurance, and Discharge

By Alan J. Belsky, Attorney at Law

Medical Debt Is Usually Dischargeable, but Not Every Healthcare-Related Obligation Disappears

A serious illness, unexpected hospitalization, surgical procedure, or prolonged course of treatment can produce medical bills that exceed a patient's ability to pay.

Even individuals with health insurance may face substantial deductibles, coinsurance, uncovered services, out-of-network charges, or disputed claims.

Medical debt is one of the common reasons individuals consider bankruptcy.

Fortunately, ordinary hospital, physician, ambulance, and other healthcare bills generally are unsecured obligations that can be discharged in Chapter 7.

But healthcare-related financial obligations are not all legally identical.

A provider may possess a lien or other statutory right. A health insurer may assert reimbursement from a personal injury settlement. Medicare or Medicaid may have recovery rights governed by federal or state law.

A debtor may also have medical debts arising from alleged fraud or other circumstances that require separate analysis.

Understanding the distinction between ordinary medical bills and enforceable reimbursement or lien rights is essential.

1. Ordinary Medical Bills Are Generally Dischargeable

Most medical bills arise from treatment provided to a patient.

The provider may bill the patient directly or seek payment from insurance.

If the patient remains personally liable for an unpaid balance, the obligation ordinarily is an unsecured debt.

Chapter 7 generally discharges qualifying unsecured medical debt.

For example, a debtor may owe $45,000 for hospitalization and surgical treatment.

If the obligation does not fall within a statutory exception, Chapter 7 may eliminate the debtor's personal liability.

The fact that the debt arose from necessary medical care does not make it nondischargeable.

2. Hospital Judgments

A hospital or medical provider may sue a patient and obtain a judgment.

The judgment ordinarily does not transform an otherwise dischargeable medical bill into a nondischargeable debt.

A qualifying medical judgment may be discharged in Chapter 7.

However, a valid judgment lien that attached to property before bankruptcy may survive unless avoided or otherwise extinguished.

The debtor should distinguish the judgment debt from any lien securing it.

Maryland also restricts medical-debt judgment liens against a debtor's primary residence under Real Property § 14-203.1 and Courts and Judicial Proceedings § 11-402. That protection concerns the creation or enforcement of the specified real-property judgment lien; it should be distinguished from a separately valid hospital lien on a personal injury recovery.

3. Medical Collection Agencies

Medical providers may refer unpaid accounts to collection agencies or sell accounts to debt purchasers.

The bankruptcy treatment generally depends on the underlying obligation.

A medical debt does not become nondischargeable merely because a collection agency acquires it.

The debtor should list the appropriate creditor and collection agency information as required by the bankruptcy forms.

Accurate notice can help prevent postpetition collection activity.

4. Emergency Room and Ambulance Bills

Emergency treatment can produce separate bills from hospitals, emergency physicians, radiologists, anesthesiologists, and ambulance providers.

These charges may be owed to different entities.

The debtor should identify each creditor.

Ordinary unpaid charges generally may be discharged.

However, governmental ambulance charges or other assessments may require separate analysis if they include fines, penalties, or statutory liens.

5. Medical Debt and the Means Test

Medical expenses can affect bankruptcy planning in several ways.

Existing medical debt ordinarily is included among the debtor's liabilities.

Ongoing medical expenses may also affect allowable deductions and the debtor's actual ability to pay.

Under § 707(b)(2), certain health-related expenses may be considered in the means-test calculation, subject to statutory requirements.

The debtor should distinguish past medical debt from anticipated future medical expenses.

The means test does not simply permit deduction of every medical bill the debtor has incurred.

6. Ongoing Medical Expenses

A debtor with chronic medical needs may incur substantial recurring expenses for prescriptions, treatment, equipment, or care.

These expenses may be relevant to Schedule J and the means test.

The debtor should document the amounts and determine whether insurance covers any portion.

Expenses should be reasonable and accurately reported.

The fact that the debtor has substantial medical expenses does not automatically establish eligibility for Chapter 7, but it may materially affect the analysis.

7. Health Insurance Deductibles and Coinsurance

A patient may remain liable for deductibles, copayments, and coinsurance under a health insurance plan.

These obligations generally are treated as ordinary medical debts when owed to providers.

However, the debtor should determine whether the amounts were properly billed.

Insurance adjustments, contractual discounts, and statutory protections may reduce or eliminate the patient's liability.

Bankruptcy should not be used to pay or discharge an amount that was never legally owed.

8. Surprise Medical Bills

Federal and Maryland law restrict certain surprise medical billing practices.

The federal No Surprises Act provides protections involving specified emergency services, certain nonemergency services at participating facilities, and air ambulance services.

The law may limit patient responsibility for qualifying out-of-network charges.

A debtor should examine whether a disputed medical bill violates applicable billing protections.

The existence of a collection demand does not establish that the full amount is legally enforceable.

9. Medical Bills Owed to Government Hospitals

A patient may owe money to a governmental hospital or medical facility.

The fact that the provider is governmental does not automatically make the debt nondischargeable.

An ordinary charge for treatment may be compensatory rather than punitive.

However, specific federal or state statutes may create different rights.

The debtor should identify the legal basis of the obligation.

10. Medical Liens

A medical lien is different from an ordinary unsecured medical bill.

A lien may give a provider or other claimant rights against specified property or settlement proceeds.

The validity and enforceability of a lien depend on the governing statute, agreement, and applicable law.

A debtor should not assume that discharge of personal liability automatically eliminates every lien.

The lien must be analyzed separately.

11. Maryland Hospital Liens

Maryland law provides statutory provisions concerning hospital liens in qualifying circumstances.

The applicability and scope of those provisions depend on the nature of the treatment and recovery.

A hospital may assert rights against proceeds of a personal injury claim under applicable law.

The debtor should determine whether the lien was properly established and whether it remains enforceable.

The bankruptcy treatment may differ from the treatment of an ordinary unsecured hospital bill.

Commercial Law § 16-601 provides a lien on 50% of a qualifying accident recovery for a hospital's reasonable and necessary treatment charges, subject to the statutory charge limitation and the priority of the attorney's lien for obtaining damages. It does not cover an accident within the Maryland Workers' Compensation Act. Section 16-602 requires the specified filing and mailed notices before payment of recovery funds. The statute does not give every healthcare provider an automatic lien on every patient asset.

12. Personal Injury Settlements

A debtor may have a personal injury claim arising from an automobile accident or other event.

Medical providers, insurers, and government programs may assert claims against settlement proceeds.

The personal injury claim itself may become property of the bankruptcy estate if it arose before filing.

Maryland provides substantial exemption protection for qualifying personal injury compensation.

However, exemption of the debtor's interest does not necessarily eliminate valid third-party reimbursement or lien rights.

The debtor should coordinate bankruptcy counsel and personal injury counsel before settlement.

13. Medicare Conditional Payments

Medicare may pay medical expenses conditionally when another party is responsible under applicable law.

The Medicare Secondary Payer provisions permit recovery in qualifying circumstances.

A personal injury settlement may trigger reimbursement obligations.

The bankruptcy treatment depends on the nature of Medicare's rights and the relevant statutory provisions.

A debtor should not assume that Chapter 7 automatically eliminates every Medicare reimbursement claim.

The claim should be analyzed before settlement proceeds are distributed.

14. Medicaid Recovery Rights

Medicaid may possess statutory recovery rights concerning certain third-party payments.

Federal and Maryland law govern the scope of those rights.

The Supreme Court has addressed limitations on Medicaid recovery from personal injury settlements.

The debtor should determine whether Medicaid has a valid claim against the settlement and what portion of the recovery may be subject to reimbursement.

Bankruptcy discharge does not automatically resolve every Medicaid lien or assignment issue.

15. ERISA Health Plan Reimbursement

Employer-sponsored health plans may contain reimbursement or subrogation provisions.

The enforceability of those provisions depends on the plan, ERISA, and applicable law.

Self-funded ERISA plans may receive different treatment from insured plans.

A plan may seek reimbursement from identifiable settlement funds.

The debtor should not assume that a bankruptcy discharge necessarily eliminates every equitable lien or reimbursement right asserted under ERISA.

16. Private Health Insurance Subrogation

Private health insurers may assert reimbursement rights when a third party caused the injury.

The validity of those rights depends on the policy, applicable Maryland law, and other governing provisions.

Some claims may be contractual.

Others may involve equitable or statutory rights.

The debtor should identify the actual basis for reimbursement.

A general statement that the insurer has a lien is not sufficient to establish enforceability.

17. Medical Credit Cards and Financing Agreements

Patients sometimes finance treatment through medical credit cards or installment loans.

These obligations may be owed to a lender rather than the healthcare provider.

Ordinary unsecured medical financing generally may be dischargeable.

However, the debtor should review the agreement for security interests, deferred-interest terms, or other provisions.

The fact that financing was used for medical care does not automatically make it legally identical to a hospital bill.

18. Medical Debt Obtained Through Fraud

Section 523(a)(2) excepts certain debts obtained through false pretenses, false representations, or actual fraud.

A medical provider may allege that a patient obtained services through fraudulent conduct.

However, inability to pay medical bills does not itself establish fraud.

The creditor must prove the applicable statutory elements.

Ordinary treatment received in good faith generally does not become nondischargeable merely because the patient later files bankruptcy.

19. Medical Debt in Chapter 13

Chapter 13 permits qualifying debtors to address unsecured medical obligations through a repayment plan.

Medical creditors generally receive treatment according to the plan and applicable priority rules.

A debtor may pay only a portion of ordinary unsecured medical debt, depending on disposable income, liquidation value, and other requirements.

Remaining dischargeable balances generally may be discharged upon successful completion of the plan.

Chapter 13 may be preferable when the debtor needs to retain nonexempt property or cure secured arrears.

20. Future Medical Bills

A bankruptcy discharge generally addresses qualifying prepetition obligations.

It does not automatically eliminate debts incurred for new treatment after filing.

A debtor who expects substantial future medical expenses should consider whether the filing date is appropriate.

The legal characterization of claims arising from ongoing treatment can sometimes be complicated.

The debtor should not assume that every medical bill received after filing necessarily represents a postpetition debt.

The underlying transaction and applicable law matter.

21. Medical Debt and Credit Reporting

Medical debt reporting is subject to federal law and consumer reporting practices.

Some medical collections may be excluded from consumer credit reports under applicable reporting policies.

However, the existence or absence of a credit reporting entry does not determine whether the debt is legally enforceable.

A bankruptcy discharge generally eliminates qualifying personal liability regardless of whether the medical debt appears on a credit report.

The debtor should review reports for inaccuracies.

22. Maryland Medical Debt Collection Protections

Maryland law imposes certain requirements on hospital billing, financial assistance, and collection practices.

The applicability depends on the provider and statutory provisions.

A patient may qualify for financial assistance or other protections before bankruptcy.

The debtor should examine whether the provider complied with applicable requirements.

Bankruptcy may be unnecessary for a particular bill if the amount can be reduced or eliminated under hospital financial assistance rules.

23. Why Medical Bills Should Be Reviewed Before Filing

A debtor may have dozens of medical accounts involving hospitals, physicians, laboratories, and collection agencies.

Some balances may be duplicated or incorrectly billed.

Insurance may have paid claims that remain listed as outstanding.

The debtor should obtain available statements and identify the actual creditors.

Potential liens and reimbursement claims should be distinguished from ordinary unsecured balances.

This review can materially affect the debtor's bankruptcy schedules and financial planning.

Conclusion

Ordinary medical bills generally are dischargeable in Chapter 7 bankruptcy.

Hospital judgments, collection agency accounts, and medical financing obligations may also be discharged when no statutory exception applies.

But medical liens, Medicare and Medicaid recovery rights, ERISA reimbursement claims, and other legally enforceable interests may require separate analysis.

The existence of a personal injury settlement can make these issues particularly important.

A debtor should not assume that every healthcare-related claim is an ordinary unsecured debt—or that a bankruptcy discharge automatically eliminates every lien or reimbursement right associated with medical treatment.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 522 — Exemptions.
- 42 U.S.C. § 1395y(b) — Medicare Secondary Payer provisions.
- 42 U.S.C. § 1396a(a)(25) — Medicaid third-party liability.
- 29 U.S.C. § 1132(a)(3) — ERISA equitable relief.

Maryland law

- Maryland Health-General Article — Hospital financial assistance and billing provisions.
- Maryland Courts and Judicial Proceedings § 11-504 — Exemptions.

Selected decisions

- *Arkansas Department of Health & Human Services v. Ahlborn*, 547 U.S. 268 (2006) — Addresses Medicaid recovery from personal injury settlements.
- *Gallardo v. Marstiller*, 596 U.S. 420 (2022) — Addresses Medicaid recovery rights involving settlement allocations.
- *Sereboff v. Mid Atlantic Medical Services, Inc.*, 547 U.S. 356 (2006) — Addresses enforcement of ERISA reimbursement provisions against identifiable settlement funds.
- *Montanile v. Board of Trustees of the National Elevator Industry Health Benefit Plan*, 577 U.S. 136 (2016) — Addresses limitations on ERISA equitable reimbursement when settlement funds have been dissipated.
- *In re Butcher*, 125 F.3d 238 (4th Cir. 1997) — Addresses Maryland's personal injury exemption.

Student Loans in Bankruptcy: Undue Hardship, Parent PLUS Loans, Private Loans, and the Possibility of Discharge

Belsky Bankruptcy Legal Library | Student Loan Debt and Dischargeability

By Alan J. Belsky, Attorney at Law

Student Loans Are Difficult to Discharge, but They Are Not Immune From Bankruptcy

One of the most persistent misconceptions about bankruptcy is that student loans can never be discharged.

That is incorrect.

Section 523(a)(8) of the Bankruptcy Code excepts certain educational debts from discharge unless requiring repayment would impose an undue hardship on the debtor and the debtor's dependents.

The statute does not make every debt associated with education nondischargeable. Nor does it prohibit a bankruptcy court from discharging qualifying student loans when undue hardship is established.

For many years, student loan discharge litigation was regarded as particularly difficult, expensive, and unpredictable.

In 2022, the United States Department of Justice and Department of Education introduced a coordinated process intended to simplify the handling of federal student loan undue-hardship proceedings.

That process did not change the statute or eliminate the requirement for judicial relief. It did, however, create a more structured method for evaluating a debtor's financial circumstances and determining whether the government should stipulate to relevant facts or recommend discharge.

For Maryland debtors, the analysis must also account for Fourth Circuit precedent, including the demanding undue-hardship standard established in *Educational Credit Management Corp. v. Frushour*, 433 F.3d 393 (4th Cir. 2005).

1. What Does § 523(a)(8) Actually Say?

Section 523(a)(8) generally excepts three categories of educational obligations from discharge unless undue hardship is established.

The categories include certain educational benefit overpayments and loans made, insured, or guaranteed by governmental units or qualifying nonprofit institutions; obligations to repay funds received as educational benefits, scholarships, or stipends; and certain qualified education loans as defined by federal tax law.

These categories are not identical.

A debt may fall outside § 523(a)(8) even though the borrower used the proceeds to pay educational expenses.

Conversely, a qualifying educational loan may remain nondischargeable even when it was made by a private lender.

The creditor must establish that the obligation falls within the applicable statutory category.

If it does, the debtor ordinarily must establish undue hardship to obtain discharge.

2. Federal Student Loans

Federal Direct Loans and other qualifying federally backed educational loans ordinarily fall within § 523(a)(8).

These loans generally survive an ordinary Chapter 7 discharge unless the debtor obtains an undue-hardship determination.

A debtor should not assume that listing the loans in the bankruptcy schedules is sufficient to discharge them.

Nor does the entry of a general discharge order necessarily establish that the student loans were eliminated.

A separate adversary proceeding ordinarily is required to obtain an undue-hardship determination.

3. Parent PLUS Loans

Parent PLUS loans are federal educational loans incurred by qualifying parents to finance a child's education.

The parent borrower is generally personally responsible for repayment.

The student does not ordinarily become personally liable merely because the loan financed the student's education.

A Parent PLUS loan generally falls within § 523(a)(8).

The parent may seek an undue-hardship discharge in bankruptcy, but must satisfy the applicable legal requirements.

The fact that the parent is retired, disabled, or living on fixed income may be relevant, but does not automatically establish undue hardship.

4. Parent PLUS Loans and Divorce

Parent PLUS loans can create complicated obligations following divorce.

A marital settlement agreement may require former spouses to share repayment of a loan legally owed to only one parent.

That agreement ordinarily does not release the named borrower from liability to the federal government.

It may, however, create a separate obligation between the former spouses.

The dischargeability of that divorce-related obligation must be distinguished from the dischargeability of the Parent PLUS loan itself.

For example, § 523(a)(15) may affect a reimbursement obligation owed to a former spouse in Chapter 7, even though the underlying federal loan remains governed by § 523(a)(8).

5. Private Student Loans

Private educational loans require careful classification.

Some qualify as nondischargeable educational loans under § 523(a)(8)(B).

Others may fall outside the statute.

A private lender cannot establish nondischargeability merely by labeling an obligation a student loan.

The legal inquiry may involve whether the loan was incurred solely to pay qualified higher education expenses, whether the educational institution was eligible under applicable federal law, and whether other statutory requirements were satisfied.

The loan documents, school records, and disbursement history may be important.

A private loan may also fall within § 523(a)(8)(A)(i) if made under a program funded in whole or in part by a governmental unit or nonprofit institution. Failure to meet the qualified-education-loan definition in subsection (B) therefore does not, by itself, establish dischargeability; every potentially applicable statutory category must be checked.

6. Loans Exceeding Qualified Educational Expenses

A private loan may exceed the borrower's qualifying educational expenses.

That circumstance may affect whether the loan satisfies the statutory definition of a qualified education loan.

However, the analysis is not necessarily resolved simply by comparing the loan amount with tuition.

Qualified higher education expenses may include specified costs of attendance beyond tuition.

The relevant tax-law definitions and statutory requirements must be applied.

A debtor should not assume that every private educational loan is nondischargeable or that every loan exceeding tuition is dischargeable.

7. Bar Examination Loans and Other Educational Financing

Some lenders offer loans to finance bar examination preparation, professional licensing expenses, relocation, or other costs associated with entering a profession.

These obligations may not necessarily satisfy the definition of a qualified education loan.

The analysis depends on the purpose of the loan, the expenses financed, and the applicable statutory category.

For example, a loan used solely to pay living expenses after graduation while studying for a licensing examination may present different issues from a qualifying loan used for educational expenses during enrollment.

The creditor must establish the applicable basis for nondischargeability.

8. The Undue-Hardship Exception

Section 523(a)(8) permits discharge when excepting the educational debt from discharge would impose an undue hardship on the debtor and the debtor's dependents.

Congress did not provide a detailed statutory definition of undue hardship.

Courts therefore developed standards for evaluating the debtor's circumstances.

The Fourth Circuit generally applies the three-part test originating in *Brunner v. New York State Higher Education Services Corp.*, 831 F.2d 395 (2d Cir. 1987).

The debtor must establish all three elements.

9. The First *Brunner* Requirement: Minimal Standard of Living

The debtor must establish that, based on current income and expenses, repayment would prevent maintenance of a minimal standard of living for the debtor and dependents.

This does not mean that the debtor must be completely destitute.

However, courts examine whether the debtor can meet basic living expenses while making required payments.

Relevant expenses may include housing, food, utilities, transportation, medical care, and other reasonable necessities.

The court may scrutinize expenses considered excessive or insufficiently supported.

The debtor should provide a realistic budget rather than relying solely on generalized assertions of financial hardship.

10. The Second *Brunner* Requirement: Persistence of Financial Hardship

The debtor must establish additional circumstances indicating that the inability to repay is likely to persist for a significant portion of the repayment period.

This requirement can be particularly difficult.

Courts may examine age, employment history, earning capacity, education, disability, medical limitations, and other circumstances.

A temporary reduction in income may not be sufficient.

But a debtor whose earning capacity is permanently or substantially limited may present stronger evidence.

The analysis should be supported by objective facts when available.

11. The Third *Brunner* Requirement: Good-Faith Efforts to Repay

The debtor must demonstrate good-faith efforts to repay the loans.

Courts may consider payment history, employment efforts, budgeting, communications with the loan servicer, and attempts to obtain available repayment relief.

The analysis is not necessarily limited to the total amount paid.

A debtor with very limited resources may have been unable to make substantial payments despite genuine efforts.

The court must evaluate the debtor's circumstances.

However, voluntary decisions that unnecessarily reduce income or increase expenses may affect the good-faith analysis.

12. The Fourth Circuit's Decision in *Frushour*

In *Educational Credit Management Corp. v. Frushour*, 433 F.3d 393 (4th Cir. 2005), the Fourth Circuit applied the *Brunner* standard and emphasized the demanding nature of undue-hardship relief.

The court rejected discharge under the circumstances presented.

The decision remains an important authority for Maryland bankruptcy proceedings.

A debtor seeking discharge should not assume that financial difficulty alone satisfies the test.

The evidence must address present hardship, likely persistence, and good-faith repayment efforts.

The Department of Justice's later administrative guidance does not overrule *Frushour* or replace the governing judicial standard.

13. The Department of Justice's Streamlined Student Loan Discharge Process

In November 2022, the Department of Justice and Department of Education announced a coordinated process for handling undue-hardship cases involving federal student loans.

The process is designed to improve consistency, reduce unnecessary litigation, and permit government attorneys to recommend discharge when the evidence supports the statutory standard.

A debtor generally provides financial information through an attestation addressing income, expenses, assets, repayment history, and circumstances affecting future ability to repay.

Government attorneys evaluate that information under the applicable guidance.

The process can lead to stipulations and a recommended discharge, but it does not guarantee that the government will agree.

The bankruptcy court retains responsibility for entering the appropriate judgment.

14. The Attestation Process

The attestation is intended to provide a standardized presentation of the debtor's financial circumstances.

Information may include household composition, income, necessary living expenses, assets, employment history, and factors affecting future earning capacity.

The debtor may also provide information concerning repayment efforts and available loan programs.

The supporting documentation should be accurate and consistent with the bankruptcy schedules.

A debtor should not exaggerate expenses, omit income, or assume that the attestation substitutes for truthful testimony and disclosure.

The government may request additional information when necessary.

15. Is a Trial Always Necessary?

No.

An adversary proceeding may be resolved through stipulations, agreement, or other appropriate procedures when the parties establish a sufficient basis for relief.

The streamlined federal process may reduce the need for extensive discovery and contested trial proceedings.

However, a debtor should not assume that filing an attestation automatically produces discharge.

If the government contests the claim, the debtor may need to prove undue hardship through ordinary litigation.

The bankruptcy court ultimately determines the relief available.

16. How an Adversary Proceeding Begins

Federal Rule of Bankruptcy Procedure 7001 requires an adversary proceeding for a determination of dischargeability.

The debtor ordinarily files a complaint in the bankruptcy court naming the appropriate defendant or defendants.

The complaint should identify the loans, their legal character, and the factual basis for undue hardship.

Service must comply with Rule 7004 and other applicable requirements.

In federal student loan cases, counsel should determine the appropriate governmental parties and service procedures.

The filing of the bankruptcy petition alone does not commence the adversary proceeding.

17. When Should the Adversary Proceeding Be Filed?

An undue-hardship complaint may be filed during the bankruptcy case.

Unlike certain creditor complaints under § 523(c), the ordinary sixty-day deadline under Rule 4007(c) does not govern a debtor's undue-hardship determination under § 523(a)(8).

Rule 4007(b) generally permits complaints concerning debts outside § 523(c) to be filed at any time.

A closed bankruptcy case may be reopened when appropriate to obtain a dischargeability determination.

The debtor should nevertheless consider timing, available evidence, and the practical benefits of prompt action.

18. Can a Closed Chapter 7 Case Be Reopened?

Yes.

Under § 350(b), a bankruptcy court may reopen a case to provide relief to the debtor or for other cause.

A debtor who previously received a Chapter 7 discharge but did not pursue student loan relief may seek to reopen the case and commence an appropriate adversary proceeding.

Reopening does not itself discharge the student loans.

The debtor must establish the statutory basis for relief.

The availability of evidence concerning the debtor's current and anticipated financial circumstances may affect the litigation.

19. What If the Debtor Is Retired?

Retirement can be important in an undue-hardship analysis.

A debtor who has reached retirement age may have limited prospects for increasing income.

However, retirement does not automatically establish undue hardship.

The court may examine the debtor's financial resources, employment prospects, expenses, assets, and repayment obligations.

A debtor who voluntarily retired while retaining substantial earning capacity may present different circumstances from one whose age or health materially limits employment.

The inquiry remains individualized.

20. Disability and Medical Limitations

A debtor with a significant disability or chronic medical condition may have evidence supporting persistent inability to repay.

Medical records, disability determinations, employment history, and functional limitations may be relevant.

But a disability determination under another federal program does not automatically satisfy the *Brunner* test.

The debtor's actual financial circumstances and future earning capacity must be evaluated.

Federal student loan administrative discharge programs based on total and permanent disability may also provide relief outside bankruptcy.

Those programs should be considered separately.

21. Income-Driven Repayment Plans

Federal student loan borrowers may have access to income-driven repayment arrangements, subject to current program requirements.

The availability and terms of such plans have changed over time and may be affected by litigation or regulatory developments.

Under the *Brunner* good-faith analysis, courts may consider the debtor's efforts to investigate or participate in available repayment programs.

However, the availability of a reduced-payment plan does not necessarily establish that repayment would impose no undue hardship.

A debtor may face circumstances in which even reduced payments are unaffordable or the financial burden remains significant.

The current program rules should be verified rather than relying on outdated repayment-plan descriptions.

22. Does a Zero-Dollar Payment Defeat Undue Hardship?

Not automatically.

A borrower may qualify for a zero-dollar monthly payment under an applicable income-driven repayment arrangement.

That fact may be relevant to the undue-hardship analysis, but it does not necessarily resolve the question.

The court may consider the debtor's overall circumstances, anticipated repayment obligations, duration of hardship, and good-faith efforts.

The result depends on controlling law and the facts.

23. Partial Discharge and Other Relief

Courts have considered whether relief may be granted concerning only part of an educational obligation or through other appropriate mechanisms.

The availability of partial discharge or modification depends on governing law and the statutory framework.

A debtor should not assume that the only possible outcomes are complete discharge of every loan or denial of all relief.

However, any proposed partial relief must be supported by applicable precedent and the court's authority.

The Fourth Circuit's treatment of partial discharge requires particular attention.

Any partial discharge must rest on the undue-hardship requirement and applicable judicial authority; general equitable power is not a substitute for § 523(a)(8). DOJ guidance permits a government recommendation of partial relief in appropriate cases, but the recommendation neither binds the court nor displaces Fourth Circuit precedent.

24. Chapter 7 Versus Chapter 13

Student loan obligations generally receive similar undue-hardship treatment under § 523(a)(8) in both chapters.

Chapter 7 ordinarily permits prompt discharge of other qualifying unsecured debts.

Chapter 13 may permit repayment through a plan, but the student loan balance may remain after plan completion unless discharged through an undue-hardship determination or other applicable relief.

Interest and repayment-program consequences can affect the remaining balance.

The debtor should not assume that completing a Chapter 13 plan automatically eliminates student loans.

25. Student Loan Payments During Chapter 13

A Chapter 13 plan may provide for treatment of student loan claims under applicable provisions.

However, separate classification and payment of student loans can raise unfair-discrimination and confirmation issues.

The debtor generally cannot simply prefer student loan creditors over other unsecured creditors without satisfying the Bankruptcy Code.

The treatment of long-term obligations may also implicate § 1322(b)(5).

Plan drafting requires careful consideration of the debtor's objectives and applicable case law.

26. Student Loan Consolidation and Refinancing

Federal consolidation and private refinancing can change the legal and practical characteristics of educational debt.

A debtor should consider whether refinancing sacrifices federal repayment protections, administrative discharge options, or other benefits.

The bankruptcy classification of a refinanced obligation depends on the governing documents and applicable statutory provisions.

The debtor should not assume that replacing a federal student loan with a private loan automatically makes it dischargeable.

The transaction's legal character must be examined.

27. Student Loans and Tax Consequences

Student loan forgiveness or discharge may have federal or state tax consequences depending on the applicable law and tax year.

Certain exclusions from cancellation-of-debt income may apply.

The tax treatment of an administrative loan discharge may differ from other forms of forgiveness.

The debtor should obtain current tax advice rather than assuming that every forgiven student loan creates taxable income or that every discharge is tax-free.

A qualifying discharge granted in a Title 11 case is excluded from federal cancellation-of-debt income under § 108(a)(1)(A), subject to the statute's requirements and tax-attribute rules. That bankruptcy exclusion is separate from temporary or program-specific exclusions governing administrative student loan forgiveness.

28. Why the Student Loan Documents Matter

A debtor seeking discharge should obtain a complete loan history.

Relevant documents may include promissory notes, disbursement records, school enrollment information, repayment histories, consolidation documents, and current balances.

For private loans, the educational institution's eligibility and the purpose of the loan may be critical.

For federal loans, the debtor should identify the precise loan programs and servicers.

The attorney should not rely solely on a credit report description.

29. Why Student Loan Discharge Should Be Evaluated During Bankruptcy Planning

A debtor may have substantial student loan obligations and comparatively little other debt.

If the loans are nondischargeable and undue hardship cannot be established, Chapter 7 may provide limited relief.

Conversely, a debtor with substantial ordinary unsecured debt may benefit from Chapter 7 even when student loans survive.

A debtor with a potentially strong undue-hardship claim should consider whether to pursue an adversary proceeding.

The availability of the Department of Justice's streamlined federal process makes that evaluation particularly important.

Conclusion

Student loans are not categorically immune from bankruptcy discharge.

Section 523(a)(8) protects qualifying educational obligations unless repayment would impose undue hardship.

The Fourth Circuit applies the demanding *Brunner* standard, but the Department of Justice's coordinated federal student loan review process may simplify the presentation and resolution of appropriate cases.

Private educational loans also require careful classification because not every loan associated with education falls within § 523(a)(8).

Parent PLUS loans, retirement, disability, repayment history, and future earning capacity can materially affect the analysis.

A debtor with substantial student loan debt should not assume that discharge is impossible without first examining the loan's legal classification and the debtor's actual ability to repay.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 523(a)(8) — Educational debt exceptions and undue hardship.
- 11 U.S.C. § 350(b) — Reopening bankruptcy cases.
- 11 U.S.C. § 1322 — Chapter 13 plan provisions.
- 11 U.S.C. § 1328 — Chapter 13 discharge.
- Federal Rule of Bankruptcy Procedure 4007 — Dischargeability proceedings.

Federal statutes

- Federal Rule of Bankruptcy Procedure 7001 — Adversary proceedings.
- Federal Rule of Bankruptcy Procedure 7004 — Service of summons and complaint.

Federal administrative guidance

- U.S. Department of Justice — Student Loan Bankruptcy Discharge Guidance — Department of Justice and Department of Education process for evaluating federal student loan undue-hardship cases.
- U.S. Department of Education — Federal Student Aid — Federal loan information, repayment programs, and administrative discharge options.

Selected decisions

- *Brunner v. New York State Higher Education Services Corp.*, 831 F.2d 395 (2d Cir. 1987) — Establishes the three-part undue-hardship test.
- *Educational Credit Management Corp. v. Frushour*, 433 F.3d 393 (4th Cir. 2005) — Applies the *Brunner* test in the Fourth Circuit and addresses the debtor's burden of establishing undue hardship.
- *In re Mosko*, 515 F.3d 319 (4th Cir. 2008) — Addresses undue hardship and the good-faith repayment requirement.
- *In re Ekenasi*, 325 F.3d 541 (4th Cir. 2003) — Addresses undue hardship and the debtor's future financial circumstances.
- *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010) — Addresses student loan discharge provisions in a confirmed Chapter 13 plan and the consequences of failure to object.
- *McDaniel v. Navient Solutions, LLC*, 973 F.3d 1083 (10th Cir. 2020) — Addresses the scope of § 523(a)(8)(A)(ii) concerning certain private educational obligations.
- *Homaidan v. Sallie Mae, Inc.*, 3 F.4th 595 (2d Cir. 2021) — Addresses private educational loans and the statutory meaning of educational benefits.
- *In re Crocker*, 941 F.3d 206 (5th Cir. 2019) — Addresses the distinction between educational loans and obligations covered by § 523(a)(8)(A)(ii).

Bankruptcy and Tax Debts: Which Income Taxes Can Be Discharged, Which Survive, and Why Filing Dates Matter

Belsky Bankruptcy Legal Library | Tax Dischargeability and Bankruptcy Planning

By Alan J. Belsky, Attorney at Law

Some Income Taxes Can Be Discharged in Bankruptcy, but Timing Is Critical

A person who owes substantial federal or Maryland income taxes may assume that bankruptcy cannot eliminate the obligation.

That assumption is incorrect.

Certain older income tax debts can be discharged in Chapter 7 bankruptcy when the statutory requirements are satisfied.

However, tax dischargeability is governed by detailed rules involving the original return due date, the date the return was filed, the date the tax was assessed, and whether any events suspended the applicable periods.

A debtor who files bankruptcy even a few days too early may remain liable for a tax obligation that could have been discharged through a later filing.

Conversely, waiting may permit the IRS or Maryland Comptroller to continue collection, obtain liens, or take other enforcement action.

The appropriate filing date must therefore be determined from verified tax records rather than estimates.

1. Income Taxes Are Not Categorically Nondischargeable

Section 523(a)(1) identifies tax obligations excepted from discharge.

The statute incorporates priority-tax provisions under § 507(a)(8).

Certain older income taxes may fall outside those provisions and become dischargeable.

But not every tax is treated alike.

Income taxes, payroll withholding taxes, sales taxes, property taxes, and tax penalties may be governed by different rules.

The analysis must identify the particular tax, tax period, and legal basis for the obligation.

2. The Three-Year Rule

Under § 507(a)(8)(A)(i), certain income taxes receive priority treatment when the return was last due, including extensions, within three years before the bankruptcy petition.

Older income taxes may fall outside this priority period.

Example

A taxpayer owes federal income tax for 2022.

Assume the return was due April 18, 2023, and no extension or tolling applies.

The ordinary three-year period generally would expire in April 2026.

A bankruptcy filed before expiration may leave the tax nondischargeable.

A later filing may satisfy the three-year requirement, assuming the other statutory conditions are met.

The precise deadline should be calculated using the legally applicable due date and any extensions or suspension periods.

3. Extensions Change the Three-Year Calculation

The three-year period is measured from the date the return was last due, including extensions.

For example, a taxpayer may obtain a valid extension to October.

The later due date may control the three-year calculation.

A debtor should not automatically use April 15 as the relevant date.

The attorney should verify the actual filing deadline applicable to the tax year.

4. The Two-Year Rule

Section 523(a)(1)(B)(ii) generally excepts from discharge certain taxes for which a required return was filed after its due date and within two years before the bankruptcy petition.

This provision can prevent discharge even when the tax year is old.

Example

A debtor files a delinquent 2019 income tax return in January 2025.

The debtor files Chapter 7 in December 2026.

Although the tax year is several years old, the return was filed less than two years before bankruptcy.

The tax may remain nondischargeable.

The debtor generally must satisfy the applicable two-year requirement in addition to the other dischargeability conditions.

5. The 240-Day Assessment Rule

Section 507(a)(8)(A)(ii) generally gives priority treatment to income taxes assessed within 240 days before bankruptcy, subject to statutory adjustments.

The assessment date may differ substantially from the tax return filing date.

For example, the IRS may assess additional tax after an audit.

That assessment can affect dischargeability.

A debtor should not assume that an old tax year is dischargeable merely because the return was filed several years earlier.

The actual assessment history must be examined.

6. The Three Rules Must Be Satisfied Together

For an ordinary income tax debt to be dischargeable, the debtor generally must satisfy the applicable three-year, two-year, and 240-day requirements.

The analysis is cumulative.

A tax may satisfy the three-year rule but fail the two-year rule.

It may satisfy both but remain within the 240-day assessment period.

Fraud, willful tax evasion, unfiled returns, and other statutory provisions may independently prevent discharge.

A complete analysis therefore requires more than calculating the age of the tax year.

Section 507(a)(8)(A)(iii) separately gives priority to certain income taxes not assessed before filing but still assessable afterward. Satisfying the usual three-year, two-year, and 240-day shorthand therefore does not establish dischargeability without checking this additional category and its statutory exceptions.

7. Why Filing a Few Days Too Early Can Be Costly

Consider a debtor who owes $65,000 in otherwise potentially dischargeable income taxes.

The applicable 240-day assessment period will expire in ten days.

If the debtor files Chapter 7 immediately, the taxes may remain nondischargeable.

If the debtor waits until the relevant period expires, the taxes may become dischargeable, assuming all other requirements are satisfied.

However, waiting may expose the debtor to garnishment, levy, or other collection activity.

The attorney must weigh the value of the potential discharge against the risks of delay.

8. Late-Filed Returns

Late-filed returns create difficult dischargeability questions.

The Bankruptcy Code contains a definition of return in the hanging paragraph following § 523(a).

The provision refers to applicable nonbankruptcy law, including filing requirements.

Courts have disagreed concerning the treatment of returns filed after the statutory deadline.

Some decisions apply strict interpretations that may prevent discharge of taxes associated with late-filed returns.

Other decisions distinguish different types of late filings and circumstances.

The debtor should not assume that waiting two years after filing a delinquent return necessarily makes the tax dischargeable.

9. The Fourth Circuit's Decision in *Moroney*

In *In re Moroney*, 352 F.3d 902 (4th Cir. 2003), the Fourth Circuit addressed the dischargeability of taxes associated with returns filed after the IRS had prepared substitute assessments.

The court concluded that the debtor's filings did not constitute returns for the relevant bankruptcy dischargeability purpose under the circumstances presented.

The decision predates the 2005 statutory amendments.

Its continuing significance must therefore be considered alongside the current statutory definition of return and subsequent case law.

For Maryland debtors, late-filed returns require particularly careful analysis.

10. Substitute Returns Prepared by the IRS

When a taxpayer fails to file, the IRS may prepare a substitute for return or otherwise determine and assess tax.

A substitute return does not necessarily satisfy the debtor's filing obligations for bankruptcy dischargeability purposes.

A later return submitted by the taxpayer may also present complications.

The statutory definition of return expressly addresses certain returns prepared under Internal Revenue Code § 6020(a) and excludes those prepared under § 6020(b).

The distinction matters.

The debtor should obtain the IRS account transcript and determine exactly what documents were filed and when.

11. Fraudulent Returns

Section 523(a)(1)(C) excepts taxes from discharge when the debtor made a fraudulent return or willfully attempted in any manner to evade or defeat the tax.

The provision can apply regardless of the ordinary aging rules.

For example, a debtor who intentionally concealed substantial income may face nondischargeability even when the tax year is old.

The government must establish the applicable statutory requirements.

An ordinary mistake or inability to pay does not automatically establish fraud or willful evasion.

12. Willful Tax Evasion

Willful evasion can involve conduct beyond filing a fraudulent return.

Courts may examine affirmative acts intended to evade payment or collection.

Examples may include concealment of assets, misleading financial representations, or other conduct satisfying the statutory standard.

The distinction between inability to pay and deliberate evasion is important.

A taxpayer who lacks sufficient resources to pay a tax debt has not necessarily willfully evaded it.

The Fourth Circuit's applicable precedent must be considered.

13. IRS Tax Liens

Discharge of personal liability does not necessarily eliminate a valid federal tax lien.

Under federal tax law, a lien may arise when the statutory requirements are satisfied.

A tax lien may attach to property interests owned by the taxpayer.

Bankruptcy may discharge the debtor's personal obligation while leaving the lien enforceable against qualifying property.

The debtor should determine whether a lien exists and what property it encumbers.

The lien's treatment is separate from dischargeability of the underlying tax.

14. Maryland Tax Liens

The Maryland Comptroller may possess statutory collection and lien rights concerning unpaid state taxes.

The effect depends on Maryland tax law and the nature of the obligation.

A debtor should determine whether a Maryland tax lien has attached to property.

Discharge of personal liability does not necessarily eliminate a valid prepetition lien.

The relevant state records should be examined.

15. Trust Fund Taxes

Certain taxes collected or withheld from others receive special treatment.

Examples include employee income tax withholding and the employee portion of payroll taxes.

Section 507(a)(8)(C) addresses taxes required to be collected or withheld and for which the debtor is liable.

These obligations generally are not discharged merely because they are old.

Business owners and responsible persons may face personal liability under applicable tax laws.

The debtor should distinguish trust fund taxes from ordinary income taxes.

16. Sales Taxes

Sales and use taxes may receive different treatment depending on the governing law and legal character of the tax.

Some obligations may qualify as trust fund taxes.

Others may be analyzed under different provisions of § 507(a)(8).

The debtor should not assume that every sales tax debt follows the ordinary three-year, two-year, and 240-day income tax rules.

The applicable state statute and nature of the obligation must be examined.

17. Property Taxes

Property taxes may receive different treatment from income taxes.

Section 507(a)(8)(B) addresses certain property taxes.

Valid tax liens may survive bankruptcy.

The debtor should distinguish personal liability from the government's rights against real estate.

A Chapter 7 discharge does not necessarily eliminate a property tax lien or prevent enforcement against the property.

18. Tax Penalties

Tax penalties may be dischargeable or nondischargeable depending on the statutory basis and circumstances.

Section 523(a)(7) contains provisions concerning certain governmental fines and penalties.

The relationship between the penalty and underlying tax can matter.

A debtor should obtain an itemized accounting separating principal tax, interest, penalties, and collection charges.

The entire balance should not automatically be treated as one indivisible obligation.

19. Interest on Tax Debts

Interest generally follows the dischargeability treatment of the underlying tax obligation, subject to applicable law.

If the underlying tax is nondischargeable, associated interest may also survive.

If the tax is discharged, associated prepetition interest ordinarily may be discharged as well.

However, valid liens and postpetition interest issues may require separate analysis.

The debtor should obtain a complete account transcript.

20. Tolling and Suspension of the Time Periods

The three-year and 240-day periods may be suspended or extended under specified circumstances.

Events affecting the calculation may include prior bankruptcy cases, offers in compromise, collection due process proceedings, and other statutory suspension periods.

The relevant provisions include § 507(a)(8) and applicable tax law.

A debtor should not calculate dischargeability simply by counting calendar days from the original tax return due date.

The history of the tax account matters.

21. Prior Bankruptcy Filings

A previous bankruptcy may affect the timing of tax dischargeability.

The automatic stay may have prevented tax collection during the earlier case.

The Bankruptcy Code contains provisions extending or suspending relevant tax priority periods.

A debtor who previously filed Chapter 13 and later seeks Chapter 7 relief should review the prior case dates.

The earlier filing may cause taxes to remain nondischargeable longer than expected.

22. Offers in Compromise

An offer in compromise may affect tax collection and certain statutory periods.

The Bankruptcy Code contains provisions concerning suspension of the 240-day assessment period in connection with offers in compromise.

The debtor should obtain records showing when the offer was submitted, pending, rejected, withdrawn, or otherwise resolved.

The precise dates can materially affect the dischargeability calculation.

23. IRS Account Transcripts

IRS account transcripts are essential to a reliable federal income tax dischargeability analysis.

They can identify return filing dates, assessments, payments, penalties, and certain account events.

However, one transcript may not always contain every fact necessary to calculate the statutory periods.

Counsel may need additional records concerning extensions, collection proceedings, prior bankruptcy cases, or offers in compromise.

The debtor's recollection alone should not be used to determine the filing date.

24. Maryland Comptroller Records

Maryland income tax obligations require separate analysis.

The attorney should obtain relevant Maryland Comptroller account records and identify the applicable return dates, assessments, and collection history.

Federal and state assessment dates may differ.

A federal tax debt may be dischargeable while the corresponding Maryland tax debt remains nondischargeable, or vice versa.

The two obligations should not automatically be treated as having identical dischargeability dates.

25. Chapter 7 Versus Chapter 13 for Tax Debts

Chapter 7 may discharge qualifying older income taxes relatively quickly.

However, nondischargeable taxes generally remain enforceable.

Chapter 13 may permit payment of qualifying priority tax claims through a repayment plan.

Certain tax liens may also receive treatment under the plan, subject to applicable law.

A debtor with substantial recent tax obligations may benefit from Chapter 13 even when Chapter 7 is available.

The appropriate chapter depends on the tax classifications, liens, income, and other debts.

26. Tax Refund Offsets

The IRS or Maryland Comptroller may assert rights to apply tax refunds against outstanding obligations.

Bankruptcy may affect those rights.

Section 553 generally preserves qualifying setoff rights, subject to statutory limitations.

The debtor should not assume that a tax refund will be paid directly merely because a return reflects an overpayment.

The relevant tax periods and obligations must be examined.

27. What If the IRS Continues Collecting After Discharge?

The IRS may continue collecting taxes that were not discharged, subject to applicable law.

It may also enforce certain surviving tax liens.

However, collection of a discharged personal tax obligation may violate the discharge injunction.

The debtor should determine whether the particular tax was discharged and whether the collection activity concerns personal liability or a surviving lien.

The discharge order alone may not identify each tax obligation's status.

28. Why Tax Dischargeability Should Be Determined Before Filing

Tax dischargeability is one of the clearest examples of why bankruptcy timing matters.

A debtor may have substantial unsecured debt and qualify for Chapter 7 but receive limited benefit if a large tax obligation survives.

Waiting a short period may sometimes change the result.

In other cases, waiting may be dangerous because of collection activity or asset exposure.

The attorney should calculate the applicable dates from verified records and evaluate the entire financial picture.

Conclusion

Certain older federal and Maryland income taxes can be discharged in Chapter 7 bankruptcy.

But the three-year, two-year, and 240-day rules must be considered together, along with return filing requirements, assessments, fraud, evasion, and statutory suspension periods.

Late-filed returns and substitute assessments can create particularly difficult questions.

Tax liens may survive even when personal liability is discharged.

Trust fund taxes, property taxes, and other obligations may be governed by different rules.

A debtor with substantial tax debt should not select a bankruptcy filing date until the relevant returns, assessments, and tolling events have been verified. Filing even a few days too early can have serious financial consequences.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 507(a)(8) — Priority treatment of specified tax claims.
- 11 U.S.C. § 523(a)(1) — Tax exceptions to discharge.
- 11 U.S.C. § 523(a)(7) — Certain tax penalties.
- 11 U.S.C. § 553 — Setoff.
- 11 U.S.C. § 1322 — Chapter 13 plan treatment.
- 26 U.S.C. § 6020 — Returns prepared by the IRS.
- 26 U.S.C. § 6321 — Federal tax liens.

Maryland law

- Maryland Tax-General Article — State tax administration, assessments, and collection.
- Maryland Comptroller — State tax account information.

Selected decisions

- *In re Moroney*, 352 F.3d 902 (4th Cir. 2003) — Addresses late-filed returns following substitute assessments.
- *United States v. Noland*, 517 U.S. 535 (1996) — Addresses bankruptcy treatment of certain tax penalties.
- *Young v. United States*, 535 U.S. 43 (2002) — Addresses equitable tolling of the three-year tax priority period under the former statutory framework.
- *United States v. Sotelo*, 436 U.S. 268 (1978) — Addresses trust fund tax liability.
- *United States v. Galletti*, 541 U.S. 114 (2004) — Addresses federal tax assessments and partnership-related liabilities.
- *In re McCoy*, 666 F.3d 924 (5th Cir. 2012) — Addresses late-filed state income tax returns under the post-2005 statutory definition.
- *In re Mallo*, 774 F.3d 1313 (10th Cir. 2014) — Addresses late-filed returns and dischargeability.
- *In re Hindenlang*, 164 F.3d 1029 (6th Cir. 1999) — Addresses late-filed returns after substitute assessment procedures.

Bankruptcy and Tax Liens: Why Discharging Income Taxes May Not Remove IRS or Maryland Liens Against Your Property

Belsky Bankruptcy Legal Library | Tax Liens, Exemptions, and Secured Claims

By Alan J. Belsky, Attorney at Law

Discharging a Tax Debt Does Not Necessarily Eliminate the Government's Lien

A debtor may successfully discharge an old federal or Maryland income tax debt in Chapter 7 bankruptcy, only to discover that a tax lien still encumbers the debtor's home, vehicle, or other property.

The distinction can be surprising.

Bankruptcy generally permits discharge of qualifying personal obligations, but valid liens ordinarily survive unless avoided, satisfied, released, or otherwise affected by applicable law.

Tax liens receive particular treatment because federal and state tax statutes may create liens securing unpaid obligations.

A debtor who discharges personal liability may therefore remain unable to sell or refinance property without addressing a surviving lien.

The scope of the lien depends on when it arose, what property it attached to, whether the debtor owned the property when bankruptcy was filed, and the applicable tax and bankruptcy provisions.

Understanding the distinction between discharge and lien survival is essential.

1. Personal Liability Versus In Rem Liability

Personal liability is the debtor's obligation to pay a debt.

In rem liability concerns a creditor's enforceable interest in particular property.

A Chapter 7 discharge may eliminate personal liability for qualifying income taxes.

But a valid tax lien may remain enforceable against property to which it attached.

For example, a debtor may discharge a $50,000 income tax obligation but remain subject to a federal tax lien against real estate owned before filing.

The government may be prohibited from collecting the discharged tax personally while retaining certain rights against the encumbered property.

2. How Federal Tax Liens Arise

Under 26 U.S.C. § 6321, a federal tax lien generally arises when a person liable for tax neglects or refuses to pay after demand.

The lien may attach to the taxpayer's property and rights to property.

Section 6322 addresses the period during which the lien continues.

Federal tax liens can be broad.

They may attach to real estate, personal property, financial accounts, and other qualifying interests.

The precise attachment and priority questions depend on federal law and the taxpayer's property rights under applicable nonbankruptcy law.

3. Assessment, Demand, and Lien Attachment

A federal tax lien generally arises through statutory operation after assessment, demand, and failure to pay, subject to the governing provisions.

The lien's existence does not necessarily depend on the IRS recording a notice.

The notice serves important purposes concerning priority and enforceability against specified third parties.

A debtor should distinguish the statutory lien from the public notice of the lien.

The absence of a recorded notice does not automatically establish that no federal tax lien exists.

4. Notice of Federal Tax Lien

The IRS may file a Notice of Federal Tax Lien in appropriate public records.

The notice alerts third parties to the government's asserted lien.

It can affect real estate transactions, financing, and priority disputes.

A debtor should obtain the actual notice and determine the tax periods, assessments, and amounts involved.

The notice may cover several tax years with different dischargeability characteristics.

The debtor should not assume that the entire lien is eliminated merely because one tax year becomes dischargeable.

5. Maryland Tax Liens

Maryland law provides mechanisms for establishing and enforcing state tax liens.

The Comptroller may assert liens for qualifying unpaid taxes.

The effect depends on the relevant provisions of the Maryland Tax-General Article and applicable collection procedures.

A Maryland tax lien may affect real estate or other property interests.

The debtor should identify the particular lien, its statutory basis, and the property to which it attached.

Federal and Maryland liens must be analyzed separately.

6. Why Tax Liens Survive Chapter 7

Bankruptcy discharge generally eliminates qualifying personal liability.

But the Supreme Court has long recognized that valid liens ordinarily pass through bankruptcy unaffected unless the Bankruptcy Code provides otherwise.

In *Johnson v. Home State Bank*, 501 U.S. 78 (1991), the Court discussed the distinction between personal liability and a surviving mortgage lien.

The principle is relevant to tax liens.

A debtor may be personally discharged while the government retains an enforceable lien against property.

7. Example: Discharged Taxes Secured by a Home

Assume a debtor owes $70,000 in old federal income taxes.

The taxes satisfy the applicable dischargeability requirements.

Before bankruptcy, the IRS acquired a valid tax lien against the debtor's residence.

The debtor files Chapter 7 and receives a discharge.

The personal tax liability may be discharged.

However, the lien may continue encumbering the residence.

The debtor may need to resolve the lien before selling or refinancing.

The discharge alone does not necessarily clear title.

8. Tax Liens and Exempt Property

Exemption and lien survival are distinct.

Section 522(c)(2)(B) provides that exempt property may remain liable for certain debts secured by properly filed tax liens, subject to the statutory language.

A debtor may therefore claim a homestead exemption and still have property encumbered by a qualifying tax lien.

Maryland's increased residential exemption does not automatically eliminate valid federal or state tax liens.

The exemption protects the debtor's interest against specified creditor remedies, but tax lien treatment requires separate analysis.

9. Can a Tax Lien Be Avoided Under § 522(f)?

Section 522(f) permits avoidance of qualifying judicial liens that impair exemptions.

However, a statutory tax lien is generally not a judicial lien merely because it is enforceable through legal proceedings.

The Bankruptcy Code distinguishes judicial liens from statutory liens.

A debtor ordinarily cannot use § 522(f)(1)(A) to avoid a valid federal tax lien simply because it impairs a homestead exemption.

The lien's legal character must be established.

10. What Property Does the Tax Lien Reach?

A federal tax lien generally attaches to the taxpayer's property and rights to property under applicable law.

The scope can include real estate, personal property, bank accounts, and other interests.

However, bankruptcy can affect the government's ability to enforce the lien against property acquired after filing.

The debtor's prepetition property interests and postpetition acquisitions must be distinguished.

The precise treatment depends on the discharge, applicable lien law, and statutory provisions.

11. After-Acquired Property

A debtor may acquire new property after receiving a Chapter 7 discharge.

A federal tax lien securing discharged personal liability generally does not automatically attach to all new property acquired after bankruptcy merely because the tax debt once existed.

However, the analysis can be complicated when the new property represents proceeds or substitutions of prepetition collateral.

The government's surviving lien rights must be distinguished from prohibited personal collection.

The debtor should not assume that every asset acquired after filing is encumbered by the old tax lien.

12. Tax Liens and Bank Accounts

A federal tax lien may attach to qualifying bank account interests existing before bankruptcy.

The government may assert rights against those funds, subject to applicable law.

But postpetition deposits and newly acquired funds may require separate analysis.

A debtor should distinguish prepetition account balances, estate property, exempt property, and postpetition earnings.

The existence of a tax lien does not eliminate the need to identify the specific property interest involved.

13. Retirement Accounts and Tax Liens

Retirement accounts may receive substantial bankruptcy exemption protection.

However, federal tax liens can present special issues.

The IRS may possess collection rights against certain retirement interests notwithstanding ordinary exemption protections.

The scope of those rights depends on the account, federal tax law, and applicable restrictions.

A debtor should not assume that a retirement account protected from ordinary unsecured creditors is necessarily immune from federal tax lien enforcement.

14. Tenancy by the Entirety

Maryland tenancy-by-the-entirety property generally is protected against creditors holding claims against only one spouse.

However, federal tax liens can present different issues.

In *United States v. Craft*, 535 U.S. 274 (2002), the Supreme Court held that a federal tax lien could attach to a taxpayer spouse's rights in entireties property under the circumstances presented.

The decision illustrates that federal tax lien law may reach interests protected against ordinary individual creditors under state law.

A married Maryland debtor should not assume that entireties ownership automatically defeats an IRS lien.

15. Jointly Owned Property

When a debtor owns property jointly with another person, a tax lien may attach to the debtor's interest.

The government's rights depend on the ownership structure and applicable law.

A nondebtor co-owner's interest may receive separate protection.

However, federal tax law provides mechanisms for enforcing liens against certain jointly owned property.

The debtor should not assume that joint ownership automatically prevents collection.

16. Tax Lien Priority

Tax liens may compete with mortgages, judgment liens, and other security interests.

Priority depends on applicable federal and state law, including filing and perfection requirements.

For example, a mortgage recorded before a federal tax lien notice may possess priority under applicable rules.

But priority disputes can be complex.

The debtor should obtain title records and lien documents before evaluating the effect of bankruptcy.

17. What If the Property Has No Equity?

A debtor may own real estate worth less than the mortgage balance.

A junior tax lien may have little or no present collateral value.

However, the absence of current equity does not necessarily eliminate the lien in Chapter 7.

The Supreme Court's decision in *Dewsnup v. Timm*, 502 U.S. 410 (1992), limits the use of § 506(d) to strip down certain liens in Chapter 7.

The debtor should not assume that an underwater tax lien disappears automatically.

18. Tax Liens in Chapter 13

Chapter 13 may provide additional options for addressing secured tax claims through a repayment plan.

The treatment depends on lien validity, collateral value, priority, and applicable statutory provisions.

The debtor may be required to pay the allowed secured claim according to the plan.

Certain tax obligations also receive priority treatment.

The interaction between secured status, dischargeability, and plan confirmation must be examined.

19. Valuing the Government's Secured Claim

Section 506(a) addresses the determination of secured claims based on the value of the creditor's interest in estate property.

In Chapter 13, valuation may affect plan treatment of certain tax liens.

However, statutory exceptions and lien rights must be considered.

The debtor should not assume that every tax lien can be reduced to zero merely because the property has little equity.

The applicable chapter and statutory provisions matter.

20. Tax Liens and Property Sales

A debtor who wishes to sell real estate encumbered by a tax lien may need to obtain a release, discharge of property, payoff, or other appropriate resolution.

The IRS provides administrative procedures concerning discharge of property from federal tax liens under applicable provisions.

A sale may be possible even when the lien exceeds the available equity, depending on the government's agreement and legal requirements.

The debtor should address the lien before entering a transaction that requires clear title.

21. IRS Lien Withdrawal Versus Release

A lien release and a withdrawal of a Notice of Federal Tax Lien are different legal actions.

A release generally concerns the lien's legal effectiveness after satisfaction or other qualifying circumstances.

Withdrawal concerns the filed notice and its treatment under applicable federal law.

The debtor should determine which form of relief is appropriate.

A bankruptcy discharge does not automatically require the IRS to withdraw every previously filed notice.

22. Tax Liens and the Automatic Stay

The automatic stay generally restricts specified collection and lien-enforcement activities after bankruptcy filing.

However, tax authorities possess certain statutory exceptions.

For example, § 362(b)(9) permits specified tax-related actions notwithstanding the stay.

The government may be permitted to assess taxes or take other specified administrative steps.

Enforcement against estate property may remain restricted.

The debtor should distinguish tax assessment, notice, lien filing, and collection.

23. Tax Liens After Discharge

After discharge, the government may retain in rem rights against property subject to a surviving lien.

However, it ordinarily cannot collect discharged personal liability through prohibited methods.

A tax collection notice may require examination to determine whether it concerns a surviving lien or an attempt to collect personally.

The debtor should preserve communications and obtain clarification when necessary.

24. Why Tax Lien Searches Matter Before Filing

A debtor with substantial tax obligations should determine whether federal or Maryland tax liens exist before filing bankruptcy.

The review should identify tax periods, assessment dates, lien notices, filing locations, property ownership, and lien priorities.

The debtor should also determine whether the underlying taxes are dischargeable.

A bankruptcy filing may eliminate personal liability while leaving substantial secured claims unresolved.

That possibility can materially affect whether Chapter 7 or Chapter 13 is preferable.

Conclusion

A bankruptcy discharge may eliminate qualifying federal or Maryland income tax obligations without extinguishing valid tax liens.

The distinction between personal liability and in rem enforcement is fundamental.

Federal tax liens can attach to a broad range of property interests, including certain interests in jointly owned or entireties property.

Exemptions do not necessarily defeat tax liens.

Chapter 13 may provide additional mechanisms for addressing secured tax claims, while Chapter 7 generally leaves valid liens intact unless another legal basis permits relief.

A debtor should not assume that discharging an old tax debt clears the lien securing it. Tax liens must be identified, valued, and addressed separately from the dischargeability of the underlying tax.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 506 — Secured claim valuation.
- 11 U.S.C. § 522(c)(2)(B) — Tax liens and exempt property.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 524 — Discharge injunction.
- 11 U.S.C. § 1322 — Chapter 13 plan provisions.
- 26 U.S.C. § 6321 — Federal tax lien.
- 26 U.S.C. § 6322 — Duration of federal tax lien.
- 26 U.S.C. § 6323 — Notice and priority.
- 26 U.S.C. § 6325 — Release and discharge of liens.

Maryland law

- Maryland Tax-General Article — State tax lien and collection provisions.
- Maryland Courts and Judicial Proceedings § 11-504 — Exemptions.

Selected decisions

- *Johnson v. Home State Bank*, 501 U.S. 78 (1991) — Addresses survival of liens following discharge of personal liability.
- *United States v. Craft*, 535 U.S. 274 (2002) — Addresses federal tax liens and tenancy-by-the-entirety interests.
- *Dewsnup v. Timm*, 502 U.S. 410 (1992) — Limits lien stripdown under § 506(d) in Chapter 7.
- *Bank of America, N.A. v. Caulkett*, 575 U.S. 790 (2015) — Addresses wholly underwater junior liens in Chapter 7.
- *United States v. Rodgers*, 461 U.S. 677 (1983) — Addresses federal tax lien enforcement against jointly owned property.
- *United States v. National Bank of Commerce*, 472 U.S. 713 (1985) — Addresses federal tax levy rights involving joint bank accounts.

When Your Debts Exceed Chapter 13 Limits: Individual Chapter 11, Subchapter V, and Alternatives to Liquidation

Belsky Bankruptcy Legal Library | Bankruptcy Eligibility, Debt Limits, and Reorganization

By Alan J. Belsky, Attorney at Law

Too Much Debt for Chapter 13 Does Not Necessarily Mean Chapter 7 Is the Only Option

An individual may earn substantial income, own a home or business, and have the financial ability to repay creditors over time, yet be ineligible for Chapter 13 because the amount of debt exceeds the statutory limits.

This problem frequently arises with business owners who personally guaranteed commercial loans, individuals with substantial real estate debt, and people facing large judgments or tax obligations.

Chapter 13 was designed to provide individuals with regular income an opportunity to repay creditors while retaining property. But Congress imposed debt limits that restrict eligibility.

When those limits are exceeded, Chapter 11 may offer an alternative.

Chapter 11 is commonly associated with large corporate reorganizations, but individuals may also obtain relief under Chapter 11. In appropriate circumstances, qualifying business debtors may elect Subchapter V, a specialized procedure intended to make reorganization more efficient and less expensive.

The choice requires careful analysis. Chapter 11 involves greater expense and procedural complexity than Chapter 13, and Subchapter V has eligibility restrictions of its own.

The important distinction is between being ineligible for Chapter 13 and being ineligible to reorganize at all.

1. Chapter 13 Has Statutory Debt Limits

Under 11 U.S.C. § 109(e), Chapter 13 is generally available to qualifying individuals with regular income whose noncontingent, liquidated debts fall below specified limits.

For cases commenced on or after April 1, 2025, under the currently verified statutory framework, those limits are:

Type of debt	Chapter 13 limit
Noncontingent, liquidated unsecured debts	Less than $526,700
Noncontingent, liquidated secured debts	Less than $1,580,125

The limits are separate. A debtor must satisfy both.

The amounts were established through the April 2025 adjustments under § 104.

A significant proposed change

Congress has advanced the Bankruptcy Threshold Adjustment Act of 2026, which would replace the separate Chapter 13 limits with a combined $2,750,000 limit and increase the Subchapter V ceiling to $7.5 million.

The official bill-status record reviewed for this audit, updated October 15, 2026, shows Senate passage and an enrolled bill, with the latest action described as a message on Senate action sent to the House on October 14. It does not identify an enacted public law. Accordingly, this article uses the separate limits established by the April 2025 adjustment. Before applying these figures to a future petition, check for enactment and the new law's effective-date provisions; enrolled legislation alone is not sufficient.

2. The Limits Are Measured When the Petition Is Filed

Chapter 13 eligibility ordinarily is determined by reference to qualifying debts owed on the petition date.

A later increase or decrease in debt does not necessarily change the initial eligibility determination.

However, the amount and legal character of debts must be established accurately.

The debtor's schedules, loan documents, judgments, and other records may be relevant.

Counsel should not assume that every amount appearing on a credit report must be included without examining whether the debt is contingent, liquidated, secured, or unsecured.

3. What Is a Liquidated Debt?

A liquidated debt generally is one whose amount is readily ascertainable by agreement or calculation.

A debt need not be reduced to judgment to be liquidated.

For example, an unpaid $200,000 promissory note with an ascertainable balance ordinarily presents a liquidated obligation.

A disputed personal injury claim requiring a determination of liability and damages may present a different question.

The distinction concerns the ascertainability of the amount, not merely whether the debtor admits liability.

4. Disputed Debts May Still Count

A debtor may dispute a creditor's claim without making the debt unliquidated.

For example, a debtor may dispute liability on a commercial guarantee whose outstanding balance can be determined from the loan records.

The dispute does not necessarily remove the obligation from the Chapter 13 calculation.

Courts distinguish disputed debts from contingent or unliquidated debts.

A debtor should not classify a debt as unliquidated merely because litigation concerning liability remains pending.

5. Contingent Debts

A contingent debt generally depends on a future event that must occur before the debtor's payment obligation becomes fixed.

A guarantee may be contingent or noncontingent depending on its terms and the events that have occurred.

For example, a guarantee conditioned on the principal borrower's default may become noncontingent when the required default occurs.

Some guarantees impose immediate or unconditional obligations.

The actual documents must be examined.

A debtor should not assume that every personal guarantee is excluded from the debt-limit calculation.

6. Secured Versus Unsecured Debt

Under the existing Chapter 13 framework, secured and unsecured debts have separate limits.

The classification can require more than examining the creditor's label.

Section 506(a) addresses the secured status of allowed claims by reference to collateral value.

An undersecured obligation may contain both secured and unsecured components for relevant bankruptcy purposes.

Courts have addressed how such claims affect § 109(e) eligibility.

The debtor should obtain reasonable collateral valuations before relying on the scheduled debt classification.

7. Example: A Homeowner With a Large Mortgage

Assume a debtor has:

Obligation	Amount
First mortgage	$1,250,000
Vehicle loan	$45,000
Credit cards	$90,000
Medical debt	$25,000

Assuming the secured obligations are fully secured and the other debts are qualifying unsecured obligations, the debtor has $1,295,000 in secured debt and $115,000 in unsecured debt.

Both amounts fall below the currently verified separate Chapter 13 limits.

The debtor may satisfy the debt-limit requirement, subject to the other eligibility conditions.

The fact that total debt exceeds $1.4 million does not itself make Chapter 13 unavailable under the existing separate-limit system.

8. Example: A Business Owner With Personal Guarantees

Assume an individual owns an LLC and personally guarantees several business obligations.

The debtor owes $150,000 in ordinary unsecured consumer debt and has $900,000 in presently enforceable, unsecured personal guarantees.

If the guarantees are noncontingent and liquidated, qualifying unsecured debt totals $1,050,000.

That exceeds the currently verified Chapter 13 unsecured limit.

Even if the debtor has regular income sufficient to fund a repayment plan, Chapter 13 may be unavailable.

Traditional Chapter 11 may offer an alternative, and Subchapter V should be evaluated if the debtor satisfies its business-debt requirements.

9. Joint Debts and Married Debtors

Jointly owed obligations require careful treatment.

A married couple may owe substantial mortgage debt and jointly guaranteed commercial obligations.

The calculation depends on whether one spouse or both spouses file, the nature of their liability, and the applicable statutory provisions.

Joint filing does not necessarily permit the debt limits to be doubled.

Likewise, a nonfiling spouse's separate obligations are not automatically debts of the filing spouse.

The relevant legal liability must be established.

10. Chapter 7 Has No General Maximum Debt Limit

Chapter 7 does not impose a general ceiling on the amount of debt an individual may owe.

A debtor with several million dollars in qualifying obligations may be eligible for Chapter 7.

However, eligibility is not the same as suitability.

Chapter 7 involves potential liquidation of nonexempt property.

An individual who owns valuable business interests, investment property, or substantial nonexempt home equity may prefer reorganization.

The debtor's income and the consumer or nonconsumer nature of the debts may also affect Chapter 7 analysis.

11. Chapter 11 Is Available to Individuals

Chapter 11 is not limited to corporations.

An individual may file Chapter 11 when eligible under the Bankruptcy Code.

Unlike Chapter 13, traditional Chapter 11 has no general maximum debt limit.

An individual Chapter 11 debtor may seek to reorganize obligations while retaining property, subject to statutory requirements.

However, the process can involve significant legal expense, reporting obligations, creditor negotiations, and court proceedings.

Chapter 11 should not be selected merely because it is available.

The debtor must have a realistic reorganization objective.

12. How Individual Chapter 11 Differs From Chapter 13

Chapter 13 generally provides a relatively standardized repayment process administered by a standing trustee.

Chapter 11 involves a more complex reorganization framework.

The debtor may remain in possession of property and exercise many powers associated with estate administration.

Creditors may have voting rights concerning the proposed plan.

Disclosure statements, claim classifications, confirmation standards, and continuing reporting obligations may apply.

For individuals, additional provisions govern postpetition earnings and discharge.

The greater flexibility of Chapter 11 comes with greater complexity.

13. The Absolute-Priority Rule in Traditional Chapter 11

One of the most significant obstacles to confirming a traditional Chapter 11 plan is the absolute-priority rule.

Under § 1129(b)(2)(B), when an impaired class of unsecured creditors rejects the plan, a junior claimant or interest holder generally cannot retain property on account of that junior interest unless the statutory requirements are satisfied.

The application to individual Chapter 11 debtors is complicated by § 1115, which expands the estate to include specified postpetition property and earnings.

Courts have disagreed about the interaction between §§ 1115 and 1129(b).

The Fourth Circuit's decision in *In re Maharaj*, 681 F.3d 558 (4th Cir. 2012), adopts the narrower interpretation, under which the absolute-priority rule continues to apply to an individual debtor's prepetition property.

This is an important reason traditional Chapter 11 may be difficult for an individual seeking to retain substantial assets over the objection of unsecured creditors.

14. The Individual Chapter 11 Disposable-Income Requirement

Under § 1129(a)(15), when an allowed unsecured creditor objects to an individual debtor's plan, confirmation generally requires either payment of the claim in full or distribution of value at least equal to the debtor's projected disposable income over the statutory period.

That period generally is five years or the longer period provided by the plan.

The provision incorporates the definition of disposable income under § 1325(b)(2).

An individual Chapter 11 debtor should not assume that the absence of Chapter 13 eligibility permits retention of all future earnings without a repayment commitment.

15. What Is Subchapter V?

Subchapter V was enacted through the Small Business Reorganization Act of 2019.

It provides a specialized Chapter 11 procedure for qualifying small business debtors.

The objective is to reduce expense and procedural complexity while preserving a realistic opportunity to reorganize.

Subchapter V retains significant creditor protections but modifies some of the confirmation requirements that can make traditional Chapter 11 difficult.

It can be particularly valuable to an individual whose debts arise primarily from business operations or personal guarantees.

16. The Subchapter V Debt Threshold

The currently verified Subchapter V ceiling is $3,424,000 in qualifying aggregate noncontingent, liquidated secured and unsecured debt.

The statute excludes specified insider and affiliate debts from the calculation and imposes additional requirements.

At least 50% of the qualifying debt must arise from the debtor's commercial or business activities.

A debtor engaged primarily in owning or operating a single piece of real property is subject to a specific exclusion.

The United States Trustee Program confirms the $3,424,000 threshold following expiration of the temporary $7.5 million limit in June 2024.

The proposed 2026 legislation would restore the higher limit, but its enactment must be verified before relying on it.

17. Individuals May Qualify for Subchapter V

Subchapter V is not restricted to corporations or LLCs.

An individual engaged in qualifying commercial or business activities may be eligible.

For example, an individual who operated a business and personally guaranteed substantial commercial obligations may qualify even though the business itself has ceased operations, depending on the facts and governing law.

The debtor must satisfy the statutory debt and business-activity requirements.

A person whose obligations are almost entirely ordinary consumer debts does not become eligible merely because Chapter 13 is unavailable.

18. Subchapter V and the Absolute-Priority Rule

Subchapter V offers a significant advantage over traditional Chapter 11.

Under § 1191(b), a qualifying plan may be confirmed without acceptance by impaired creditor classes if the applicable statutory requirements are satisfied.

The traditional absolute-priority rule does not apply in the same manner to a nonconsensual Subchapter V plan.

Instead, the debtor generally must satisfy the specialized fair-and-equitable requirements, including a commitment of projected disposable income or equivalent value over the applicable three-to-five-year period.

This can permit a qualifying business owner to retain ownership while reorganizing debt, even without unanimous creditor support.

19. The Subchapter V Trustee

A trustee is appointed in a Subchapter V case.

The trustee's role differs from that of an ordinary Chapter 7 liquidation trustee.

The Subchapter V trustee generally assists with developing a consensual plan, monitors relevant matters, and performs statutory duties.

The debtor ordinarily remains in possession and continues operating the business unless circumstances justify a different result.

The trustee's role can vary depending on whether the plan is confirmed consensually or through § 1191(b).

20. The Ninety-Day Plan Deadline

Subchapter V imposes an accelerated plan-filing requirement.

Under § 1189(b), the debtor generally must file a plan within ninety days after the order for relief.

The court may extend that period when the need for an extension is attributable to circumstances for which the debtor should not justly be held accountable.

Only the debtor may file a Subchapter V plan.

These provisions make early preparation particularly important.

21. Disclosure Statements and Creditor Voting

Traditional Chapter 11 generally requires a disclosure statement containing adequate information for creditors to evaluate the proposed plan.

Subchapter V ordinarily does not require a separate disclosure statement unless the court orders otherwise for cause.

The Subchapter V plan must contain specified information, including a business history, liquidation analysis, and projections.

Creditors retain important participation and objection rights.

However, Subchapter V's streamlined procedures may reduce the cost and delay associated with traditional Chapter 11.

22. Treatment of the Debtor's Home

A business owner's home may secure both personal and commercial obligations.

Traditional Chapter 11 and Chapter 13 impose restrictions on modifying certain claims secured solely by the debtor's principal residence.

Subchapter V contains a special provision under § 1190(3) permitting modification of certain home-secured claims when the loan proceeds were used primarily in connection with the debtor's small business rather than primarily to acquire the residence.

This can be particularly important when an individual pledged a home to finance business operations.

The statutory requirements are specific and should not be assumed satisfied merely because the debtor owns a business.

23. Chapter 11 Is More Expensive and Demanding

Chapter 11 generally requires substantially more attorney time and financial reporting than an ordinary Chapter 13 case.

The debtor may need to prepare cash-flow projections, monthly operating reports, creditor classifications, a liquidation analysis, and a detailed plan.

Professional employment and compensation may require court approval.

Traditional Chapter 11 also involves United States Trustee quarterly fees.

Subchapter V eliminates those quarterly fees but does not eliminate professional expenses or all reporting obligations.

A debtor should consider whether the anticipated benefit justifies the cost.

24. What If Reorganization Is Not Feasible?

A debtor may exceed Chapter 13 limits but lack sufficient income or assets to support a Chapter 11 plan.

Chapter 11 is not a guarantee that property can be retained.

The debtor must establish feasibility and satisfy confirmation requirements.

If the business or personal financial circumstances cannot support a realistic plan, Chapter 7, negotiated settlements, voluntary asset sales, or other alternatives may be preferable.

Filing Chapter 11 solely to postpone inevitable liquidation can impose substantial additional expense.

25. Comparing the Available Chapters

Issue	Chapter 7	Chapter 13	Traditional Chapter 11	Subchapter V
General maximum debt	None	Separate statutory limits	None	Business-debt limit
Repayment plan	Ordinarily none	Required	Required for reorganization	Required
Nonexempt property	May be liquidated	Generally retained through plan	Retention depends on confirmation	More flexible retention rules
Business activity required	No	No	No	Yes, qualifying activity
Absolute-priority rule	Not applicable to liquidation	Not applicable in the Chapter 11 sense	Generally applicable	Modified for qualifying nonconsensual plans
Administrative burden	Usually lower	Moderate	Generally high	Streamlined relative to traditional Chapter 11
Typical debtor	Individual seeking liquidation relief	Individual with regular income	Individual or business needing complex reorganization	Qualifying small business debtor

26. Why Debt Classification Should Be Completed Before Filing

A debtor who appears ineligible for Chapter 13 may qualify after proper analysis of contingent, unliquidated, or disputed obligations.

Conversely, a debtor may appear eligible until substantial guarantees or unsecured portions of secured debts are correctly classified.

The attorney should examine the actual obligations before recommending Chapter 11.

Debt-limit analysis should include the petition-date balances, enforceability of guarantees, collateral values, and relevant statutory exclusions.

The decision should not rest solely on totals generated by a credit report or bankruptcy preparation software.

Conclusion

Exceeding Chapter 13 debt limits does not necessarily leave an individual with only Chapter 7 liquidation as an option.

Traditional Chapter 11 permits individuals to reorganize without a general maximum debt limit, although it involves significant procedural and financial burdens.

Subchapter V offers a potentially more efficient alternative for qualifying individuals and businesses whose obligations arise substantially from commercial activities.

The distinction is particularly important for business owners with large personal guarantees, valuable assets, and continuing income.

Before concluding that a debtor has too much debt to reorganize, counsel should determine which obligations count toward the applicable limits and whether traditional Chapter 11 or Subchapter V offers a feasible alternative.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 109(e) — Chapter 13 eligibility and debt limits.
- 11 U.S.C. § 101(51D) — Small business debtor definition.
- 11 U.S.C. § 506(a) — Secured claim valuation.
- 11 U.S.C. § 1115 — Individual Chapter 11 estate property.
- 11 U.S.C. § 1129 — Chapter 11 plan confirmation.
- 11 U.S.C. § 1182 — Subchapter V eligibility definitions.
- 11 U.S.C. § 1189 — Subchapter V plan filing.
- 11 U.S.C. § 1190 — Contents of a Subchapter V plan.
- 11 U.S.C. § 1191 — Subchapter V plan confirmation.

Selected decisions

- *In re Maharaj*, 681 F.3d 558 (4th Cir. 2012) — Holds that the absolute-priority rule continues to apply to individual Chapter 11 debtors' prepetition property.
- *In re Knight*, 55 F.3d 231 (7th Cir. 1995) — Addresses the meaning of noncontingent and liquidated debt for Chapter 13 eligibility.
- *In re Mazzeo*, 131 F.3d 295 (2d Cir. 1997) — Discusses contingent and liquidated obligations under § 109(e).
- *In re Scovis*, 249 F.3d 975 (9th Cir. 2001) — Addresses debt-limit calculations and secured-claim classification.
- *In re Cleary Packaging, LLC*, 36 F.4th 509 (4th Cir. 2022) — Addresses the scope of discharge exceptions under Subchapter V.

Administrative authorities

- United States Courts — Chapter 11 Bankruptcy Basics
- United States Trustee Program — Subchapter V

Bankruptcy and Repossessed Vehicles: What Happens When the Lender Takes Your Car Before or After You File?

Belsky Bankruptcy Legal Library | Vehicle Loans, Repossession, and Bankruptcy Protection

By Alan J. Belsky, Attorney at Law

Bankruptcy May Stop Repossession, but Getting a Vehicle Back Is More Complicated

For many debtors, losing a vehicle means losing the ability to work, attend medical appointments, transport children, or meet essential daily obligations.

A borrower who falls behind on automobile payments may face repossession, sometimes with little warning.

Filing bankruptcy can provide substantial protection, but the result depends on whether the vehicle has already been repossessed, whether the lender has sold it, and which chapter the debtor files.

Chapter 7 generally provides temporary protection through the automatic stay but ordinarily requires the debtor to address the secured debt through surrender, redemption, reaffirmation, or another legally permissible arrangement.

Chapter 13 may provide additional options for curing arrears and modifying certain secured claims through a repayment plan.

However, bankruptcy does not automatically restore possession of a vehicle already repossessed.

The distinction between preventing repossession and recovering a repossessed vehicle is fundamental.

1. How Automobile Repossession Works in Maryland

Maryland law permits secured creditors to repossess collateral following default when the applicable statutory and contractual requirements are satisfied.

Motor vehicle repossessions involving consumer credit may be governed by Maryland Commercial Law Article provisions, including Title 12, Subtitle 10, and relevant provisions of the Uniform Commercial Code.

The creditor's rights depend on the financing agreement and applicable law.

A secured creditor may be permitted to repossess without first obtaining a court judgment, provided the repossession complies with statutory requirements and does not involve a breach of the peace.

Notice and post-repossession procedures may also apply.

A debtor should not assume that every repossession is lawful merely because payments were missed.

2. Default Under the Automobile Loan

The loan agreement ordinarily defines events of default.

Failure to make required payments is a common basis.

Other contractual defaults may involve insurance requirements, unauthorized transfers, or other obligations.

However, Maryland consumer credit law may impose additional protections or restrictions.

The lender must comply with the governing contract and applicable statutes.

The debtor should obtain the complete financing agreement and payment history.

3. The Automatic Stay

Under 11 U.S.C. § 362(a), a qualifying bankruptcy filing ordinarily stays many actions to obtain possession of property of the bankruptcy estate or enforce prepetition liens.

If the debtor still possesses the vehicle when bankruptcy is filed, the lender generally may not repossess it while the stay applies without relief or an exception.

The stay arises automatically upon filing, subject to statutory limitations.

The debtor should promptly notify the lender and repossession agent.

However, the stay does not permanently eliminate the lender's security interest.

4. What If the Vehicle Has Not Yet Been Repossessed?

A debtor who files before repossession may preserve possession temporarily.

But the debtor must address the secured obligation.

In Chapter 7, the lender may seek relief from the stay if payments are not being made or adequate protection is lacking.

The debtor may consider reaffirmation, redemption, surrender, or another lawful arrangement.

In Chapter 13, the vehicle loan may receive treatment through a repayment plan.

The appropriate strategy depends on the vehicle's value, loan balance, payment history, and the debtor's income.

5. What If the Vehicle Was Repossessed Before Filing?

This situation is more complicated.

The debtor may retain certain ownership or redemption rights under Maryland law even after repossession.

Those rights may become property of the bankruptcy estate.

However, filing bankruptcy does not automatically require the lender to return the vehicle immediately.

The debtor must determine whether the vehicle has been sold, whether redemption rights remain, and what relief is available under bankruptcy law.

6. The Supreme Court's Decision in *Fulton*

In *City of Chicago v. Fulton*, 592 U.S. 154 (2021), the Supreme Court held that mere retention of property seized before bankruptcy does not itself violate § 362(a)(3).

The decision rejected the proposition that passive retention alone constitutes an act to exercise control over estate property under that subsection.

However, the Court did not resolve every turnover issue under § 542 or every possible automatic-stay theory.

A debtor seeking return of a repossessed vehicle may need to pursue affirmative relief.

The lender's rights and the debtor's remaining property interest must be established.

7. Turnover Under § 542

Section 542(a) generally addresses turnover of qualifying estate property held by an entity other than the trustee.

A debtor may seek turnover of a vehicle when the statutory requirements are satisfied.

However, turnover is not automatic merely because bankruptcy was filed.

The creditor may raise questions concerning ownership, adequate protection, or other applicable defenses.

The procedural requirements must be followed.

In Chapter 7, the trustee's rights may also be relevant.

8. The Importance of State-Law Ownership Rights

Federal bankruptcy law generally looks to state law to determine the debtor's property interests.

If the debtor retains ownership or redemption rights after repossession, those rights may enter the bankruptcy estate.

But if the lender completed a legally effective disposition before filing, the debtor's remaining rights may be limited.

Maryland repossession and sale procedures therefore matter.

A debtor should not assume that the vehicle can be recovered simply because the lender has not yet delivered title to a purchaser.

9. Redemption Before Sale

Maryland law may provide a debtor with rights to redeem repossessed collateral before disposition, subject to applicable requirements.

The amount required may include the secured obligation and permitted expenses.

Consumer credit statutes may provide additional protections.

The debtor should obtain the lender's redemption statement and determine the deadline.

Bankruptcy may affect the enforcement of the creditor's rights, but it does not automatically eliminate the need to satisfy applicable redemption requirements.

10. Redemption in Chapter 7

Section 722 permits an individual Chapter 7 debtor to redeem certain tangible personal property intended primarily for personal, family, or household use from a lien securing a dischargeable consumer debt.

The property must also be exempted under § 522 or abandoned under § 554. Section 722 does not authorize redemption of any vehicle merely because it is used personally.

Redemption generally requires payment of the allowed secured claim in full at the time of redemption.

For example, a debtor may owe $24,000 on a vehicle worth $12,000.

If § 722 applies, the debtor may be able to redeem the vehicle by paying the applicable secured value rather than the full loan balance.

However, redemption generally requires a lump-sum payment or other financing arrangement.

The debtor must satisfy the statutory requirements.

11. Reaffirmation Agreements

A reaffirmation agreement permits a debtor to remain personally liable on a qualifying debt despite discharge.

Under § 524(c), the agreement must satisfy statutory requirements.

A debtor may reaffirm an automobile loan to retain the vehicle.

However, reaffirmation can create significant risk.

If the debtor later defaults and the vehicle is repossessed, the lender may pursue a deficiency under applicable law.

The debtor should consider the vehicle's value, loan balance, interest rate, and affordability before reaffirming.

12. What If the Debtor Does Not Reaffirm?

The consequences depend on the loan, applicable statutory provisions, and creditor's rights.

Sections 521(a)(2), 521(a)(6), and 362(h) impose requirements concerning certain secured personal property.

Failure to comply may cause the stay to terminate concerning the property and may affect estate treatment.

The debtor should not assume that continuing monthly payments alone always guarantees the right to retain the vehicle without reaffirmation.

The applicable agreement and law must be examined.

13. Chapter 13 and Vehicle Loans

Chapter 13 may permit a debtor to retain a vehicle while paying the secured claim through a repayment plan.

The plan may address arrears and ongoing obligations.

Depending on the circumstances, the debtor may be able to modify the secured claim's treatment.

However, statutory restrictions apply to certain recently acquired vehicles and other collateral.

The debtor must propose a feasible plan satisfying confirmation requirements.

14. The 910-Day Rule

Section 1325(a) contains special provisions concerning certain purchase-money security interests in motor vehicles acquired for the debtor's personal use within 910 days before bankruptcy.

When the statutory requirements apply, the debtor generally cannot reduce the secured claim to the vehicle's current value through ordinary bifurcation under § 506(a).

The debtor may need to pay the qualifying claim according to the applicable plan requirements.

The precise treatment of interest and other amounts depends on governing law.

The debtor should determine the acquisition date and loan purpose before proposing a cramdown.

15. Vehicle Cramdown

When the 910-day restriction does not apply, Chapter 13 may permit modification of an undersecured vehicle claim.

For example, a debtor may owe $30,000 on a vehicle worth $16,000.

A qualifying plan may treat $16,000 as secured and the remaining balance as unsecured, subject to applicable requirements.

The secured portion generally must receive the required plan treatment, including appropriate interest when applicable.

The unsecured portion receives treatment with other unsecured claims.

Cramdown is not available in every case.

16. Interest Rates in Chapter 13

When a Chapter 13 plan pays a secured claim over time, the creditor may be entitled to interest sufficient to satisfy the present-value requirement.

In *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004), the Supreme Court addressed the appropriate interest-rate approach in Chapter 13 cramdown.

The plurality endorsed a formula approach beginning with a national prime rate and adjusting for risk.

The applicable rate depends on governing precedent and case circumstances.

A debtor should not assume that the original contract rate necessarily controls every modified secured claim.

17. Deficiency Balances After Repossession

A deficiency arises when the lender's net proceeds from collateral disposition are insufficient to satisfy the enforceable debt.

Maryland law imposes requirements concerning repossession, notice, sale, and deficiency claims.

The lender's compliance may affect its ability to recover a deficiency.

A debtor should obtain the sale accounting and relevant notices.

An ordinary unsecured deficiency may be dischargeable in Chapter 7.

18. What If the Lender Sold the Vehicle Before Bankruptcy?

When the lender completes a legally effective disposition before filing, the debtor may no longer possess the same ownership or redemption rights.

The debtor may still have claims concerning improper repossession or sale procedures.

The lender may assert a deficiency.

The bankruptcy treatment depends on the debtor's remaining rights and obligations.

A debtor should not assume that Chapter 13 can always recover a vehicle already sold before filing.

19. Wrongful Repossession

A lender or repossession agent may violate Maryland law during repossession.

Potential issues include breach of the peace, failure to comply with statutory procedures, or improper disposition of collateral.

The debtor may possess claims or defenses arising from the conduct.

If those claims existed before bankruptcy, they may become property of the bankruptcy estate.

The debtor should disclose them.

20. Repossession After Bankruptcy Filing

A lender that repossesses a vehicle while the automatic stay applies may violate § 362.

The debtor may seek relief.

Under § 362(k), an individual injured by a willful stay violation may recover actual damages, including attorney's fees and costs, and punitive damages in appropriate circumstances.

However, the debtor must establish that the stay applied and that the statutory requirements were satisfied.

Repeat filings, stay-relief orders, and other exceptions may affect the result.

21. What If the Debtor Is Behind on Insurance?

Automobile lenders commonly require collision and comprehensive insurance.

Failure to maintain required coverage may constitute a contractual default.

In bankruptcy, lack of insurance may also affect adequate protection.

A lender may seek stay relief when collateral is uninsured.

The debtor should maintain required coverage whenever possible.

Bankruptcy does not automatically eliminate lawful insurance requirements.

22. Vehicles Owned by a Business

A vehicle may be titled to an LLC or corporation rather than the individual debtor.

The debtor's personal bankruptcy does not automatically make every entity-owned vehicle property of the individual's estate.

However, the debtor's ownership interest in the business may become estate property.

Personal guarantees and security agreements may create additional obligations.

The legal ownership and financing documents must be examined.

23. Cosigners

A parent, spouse, or other individual may have cosigned the automobile loan.

The filing debtor's Chapter 7 discharge generally does not eliminate the cosigner's liability.

The lender may pursue the cosigner under applicable law.

Chapter 13 provides a limited codebtor stay for certain consumer debts under § 1301.

The debtor should consider the effect on nonfiling family members before surrendering or modifying treatment of the vehicle.

24. Why Timing Matters

A debtor who files before repossession may have more options than one who files after the vehicle is sold.

The availability of redemption, turnover, reaffirmation, or Chapter 13 treatment depends on the relevant facts.

A last-minute filing may stop repossession but fail to provide a sustainable solution.

The debtor should evaluate whether ongoing payments are affordable and whether retaining the vehicle is financially sensible.

Conclusion

Bankruptcy can provide substantial protection against automobile repossession, but it does not automatically eliminate secured vehicle loans or require immediate return of previously repossessed collateral.

Chapter 7 may permit surrender, redemption, reaffirmation, or other lawful arrangements.

Chapter 13 may provide additional options for curing arrears and modifying certain secured claims.

Maryland repossession law determines important ownership, redemption, and deficiency rights.

The Supreme Court's decision in *Fulton* also makes clear that passive retention of previously seized property does not itself violate § 362(a)(3).

The earlier a debtor evaluates bankruptcy before repossession or sale, the greater the opportunity to preserve meaningful options for retaining transportation.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 362 — Automatic stay.
- 11 U.S.C. § 542 — Turnover.
- 11 U.S.C. § 722 — Redemption.
- 11 U.S.C. § 524(c) — Reaffirmation.
- 11 U.S.C. § 521 — Statement of intention and secured personal property.
- 11 U.S.C. § 1325 — Chapter 13 secured claim treatment.
- 11 U.S.C. § 1301 — Codebtor stay.

Maryland law

- Maryland Commercial Law, Title 12, Subtitle 10 — Credit Grantor Closed End Credit Provisions, where validly elected; distinguish the separate Retail Installment Sales Act and the agreement's governing law.
- Maryland Commercial Law, Title 9 — Secured transactions.
- Maryland Courts and Judicial Proceedings § 11-504 — Exemptions.

Selected decisions

- *City of Chicago v. Fulton*, 592 U.S. 154 (2021) — Addresses retention of property seized before bankruptcy.
- *United States v. Whiting Pools, Inc.*, 462 U.S. 198 (1983) — Addresses turnover of seized property and estate interests.
- *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004) — Addresses interest rates on modified secured claims in Chapter 13.
- *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997) — Addresses collateral valuation when a Chapter 13 debtor retains secured property.
- *In re Price*, 562 F.3d 618 (4th Cir. 2009) — Addresses vehicle loan treatment under the 910-day provision.

Bankruptcy and Credit Reports: Correcting Errors After Discharge, Disputed Balances, Reinserted Debts, and Credit Reporting Violations

Belsky Bankruptcy Legal Library | Credit Reporting and Life After Bankruptcy

By Alan J. Belsky, Attorney at Law

Bankruptcy Discharge Eliminates Qualifying Debts, but It Does Not Erase Credit History

A Chapter 7 discharge ordinarily eliminates the debtor's personal liability for qualifying prepetition obligations.

But the discharge does not automatically remove the bankruptcy filing, prior delinquencies, or discharged accounts from consumer credit reports.

Credit reporting agencies may continue reporting accurate historical information for the periods permitted by federal law.

Problems arise when discharged debts are reported as currently collectible, account balances are inaccurate, debts reappear, or creditors fail to investigate legitimate disputes.

The Fair Credit Reporting Act provides procedures for challenging inaccurate or incomplete information.

In some circumstances, a creditor's reporting conduct may also implicate the bankruptcy discharge injunction.

However, these are distinct legal theories with different requirements.

A debtor should understand what accurate postbankruptcy reporting looks like and how to challenge errors effectively.

1. What Does the Fair Credit Reporting Act Require?

The Fair Credit Reporting Act, 15 U.S.C. § 1681 et seq., regulates consumer reporting agencies and entities that furnish information to them.

The statute establishes requirements concerning accuracy, permissible reporting periods, reinvestigation of disputes, and certain consumer remedies.

The law does not require every negative account to disappear after bankruptcy.

It requires compliance with applicable reporting standards.

A debtor should distinguish accurate adverse information from information that is materially inaccurate or misleading.

2. How Long Can Bankruptcy Be Reported?

Under 15 U.S.C. § 1681c(a)(1), bankruptcy information generally may be reported for up to ten years from the relevant bankruptcy order or adjudication.

For an ordinary voluntary bankruptcy, the filing date generally serves as the starting point.

Major credit reporting agencies have traditionally removed Chapter 13 bankruptcies after approximately seven years under their reporting policies.

The shorter Chapter 13 period is generally a reporting practice rather than a separate statutory maximum.

The bankruptcy's appearance on a credit report does not mean that the debtor remains legally obligated on discharged debts.

3. Discharged Accounts May Remain Visible

A credit card or loan discharged in bankruptcy may remain on the credit report during the applicable reporting period.

The account may show historical delinquencies and an indication that it was included in bankruptcy.

The discharge does not erase the fact that the account existed or that payments were missed before filing.

However, the account should not be reported in a materially misleading manner concerning the debtor's continuing personal liability.

The debtor should examine both the account status and reported balance.

4. Reporting a Balance After Discharge

A discharged unsecured debt ordinarily should not be reported as though the debtor remains personally obligated to pay an enforceable balance.

For example, a debtor may discharge a $15,000 credit card account.

If the creditor continues reporting a currently due $15,000 personal balance after discharge, the reporting may be inaccurate or misleading.

However, the legal analysis depends on the entire report and circumstances.

Historical balances and charge-off information may be reported differently from current collectible balances.

The debtor should obtain the complete account entry before asserting a violation.

5. Secured Debts Require Different Treatment

A mortgage or automobile lien may survive Chapter 7 discharge even when personal liability is eliminated.

The creditor may retain rights against collateral.

Credit reporting of secured accounts can therefore present more complicated questions.

The report should not falsely suggest personal liability that was discharged.

But the existence of a surviving lien may be relevant to how the account is described.

The debtor should distinguish personal liability from in rem enforcement rights.

6. What If the Creditor Reports New Delinquencies After Discharge?

A creditor may continue reporting historical prepetition delinquencies accurately.

However, reporting new delinquencies as though the debtor remains personally obligated to make payments on a discharged unsecured debt may raise concerns.

The debtor should determine whether the reported delinquency concerns a discharged personal obligation, a reaffirmed debt, or another enforceable obligation.

The relevant dates and account status matter.

Not every post-discharge reporting entry automatically establishes a violation.

7. Reaffirmed Debts

A valid reaffirmation agreement may preserve personal liability for a debt that otherwise would be discharged.

The account may therefore receive different reporting treatment.

The debtor should obtain the reaffirmation agreement and confirm that it satisfied § 524(c).

A creditor should not assume that the debtor reaffirmed merely because payments continued after bankruptcy.

The enforceability of the agreement must be established.

8. What Is Reinsertion?

Reinsertion occurs when information previously deleted from a consumer report is added again.

Section 1681i(a)(5)(B) imposes requirements concerning reinsertion of information deleted through the reinvestigation process.

The consumer reporting agency generally must receive the required certification of completeness and accuracy and provide the prescribed notice.

A debtor should preserve earlier credit reports showing deletion and later reports showing reinsertion.

The mere reappearance of an account does not automatically establish unlawful reinsertion unless the statutory requirements apply.

9. Disputing Errors With Credit Reporting Agencies

Section 1681i provides procedures for disputing the completeness or accuracy of information in a consumer report.

A debtor may submit a dispute identifying the account and explaining the alleged error.

Supporting documentation may include the bankruptcy petition, schedules, discharge order, and account statements.

The reporting agency generally must conduct a reasonable reinvestigation within the applicable statutory period.

The debtor should preserve the dispute and response.

10. Why a Written Dispute Is Important

A written dispute can create a clear record of the information challenged and the documents provided.

Although disputes may be submitted through online systems, the debtor should consider whether the process permits a complete explanation and preservation of supporting materials.

The dispute should identify the specific inaccurate information.

For example, the debtor may state that the account was discharged on a particular date and that the report incorrectly shows a current balance due.

A generalized request to remove all negative information may be less useful than a precise factual dispute.

11. Disputes With Furnishers

Entities that furnish information to consumer reporting agencies have duties under § 1681s-2.

The statute distinguishes certain accuracy-related obligations from duties triggered after the furnisher receives notice of a dispute from a consumer reporting agency.

Private enforcement rights differ between these provisions.

In many cases, a consumer's claim against a furnisher under § 1681s-2(b) depends on the furnisher receiving the required notice through the reporting agency.

A direct complaint to the creditor may be useful, but it does not necessarily trigger the same private statutory remedies.

12. The Duty to Investigate

After receiving the required notice, a furnisher generally must investigate the disputed information, review relevant materials, and report the results as required by § 1681s-2(b).

The investigation must satisfy the applicable legal standard.

A creditor should not simply verify inaccurate information without meaningful review.

However, the scope of the required investigation depends on the nature of the dispute and information provided.

The debtor must establish the relevant statutory elements when pursuing a claim.

13. The Fourth Circuit's Decision in *Saunders*

In *Saunders v. Branch Banking & Trust Co.*, 526 F.3d 142 (4th Cir. 2008), the Fourth Circuit addressed materially misleading credit reporting and furnisher obligations under the FCRA.

The court recognized that technically accurate information may nevertheless be misleading when it creates a materially inaccurate impression.

The decision is important for Maryland consumers.

A creditor cannot necessarily defend every disputed entry merely by pointing to one literally accurate component.

The report must be evaluated in context.

14. The Fourth Circuit's Decision in *Johnson*

In *Johnson v. MBNA America Bank, NA*, 357 F.3d 426 (4th Cir. 2004), the Fourth Circuit addressed a furnisher's investigation duties after receiving notice of a consumer dispute.

The decision emphasizes the requirement of a reasonable investigation under the circumstances.

The adequacy of an investigation may depend on the nature of the disputed information and the records available to the furnisher.

The debtor should preserve evidence showing what information was provided and how the furnisher responded.

15. What Damages Are Available Under the FCRA?

The FCRA provides remedies for qualifying negligent and willful noncompliance.

Under § 1681o, negligent noncompliance may support recovery of actual damages and attorney's fees and costs when statutory requirements are satisfied.

Under § 1681n, willful noncompliance may permit statutory damages in specified circumstances, punitive damages, and attorney's fees and costs.

The debtor must establish the applicable elements.

An inaccurate entry does not automatically entitle the consumer to a particular damages amount.

For a damages action in federal court, the consumer must also establish concrete injury and Article III standing. TransUnion LLC v. Ramirez, 594 U.S. 413 (2021), rejects an assumption that a statutory violation alone establishes standing; dissemination of inaccurate information and other concrete harms must be analyzed under the particular claim.

16. Emotional Distress and Credit Reporting

In appropriate circumstances, actual damages under the FCRA may include proven emotional distress.

However, the debtor must establish a sufficient evidentiary basis.

Generalized frustration or annoyance may not establish compensable injury.

Relevant evidence may include testimony, communications, medical records when appropriate, and circumstances demonstrating the effect of the inaccurate reporting.

The required proof depends on governing law.

17. Credit Denials and Financial Losses

A debtor may suffer financial harm because of inaccurate credit reporting.

Examples may include denial of a loan, increased interest rates, or other measurable losses.

The debtor should preserve adverse action notices, lender communications, credit reports, and financial records.

Causation is important.

A debtor who recently filed bankruptcy may face legitimate credit restrictions independent of the disputed entry.

The claimant must distinguish harm caused by inaccurate reporting from consequences attributable to accurate bankruptcy information.

18. Credit Reporting and the Discharge Injunction

Section 524(a)(2) generally prohibits attempts to collect discharged debts as personal liabilities.

A creditor's reporting conduct may, in some circumstances, be part of an effort to coerce payment of a discharged debt.

However, inaccurate reporting alone does not automatically establish contempt of the discharge injunction.

The debtor must establish that the creditor's conduct violated the injunction under the applicable standard.

The distinction between an FCRA claim and a bankruptcy contempt proceeding matters.

19. The *Taggart* Standard

In *Taggart v. Lorenzen*, 587 U.S. 554 (2019), the Supreme Court held that civil contempt for violating the discharge injunction may be appropriate when there is no fair ground of doubt that the order prohibited the creditor's conduct.

The standard is objective.

A creditor may avoid contempt when there is an objectively reasonable basis for uncertainty concerning the injunction's application.

The debtor should not assume that every disputed credit entry satisfies this standard.

The reporting conduct and surrounding circumstances must be examined.

20. When Credit Reporting Becomes Collection Pressure

A creditor may report a discharged balance while simultaneously demanding payment or offering to remove negative information if the debtor pays.

Such conduct may provide evidence concerning the purpose of the reporting.

The legal analysis depends on the communications and applicable law.

A debtor should preserve collection letters, emails, account statements, and credit reports.

The combination of inaccurate reporting and collection demands may present a different case from an isolated reporting error.

21. What If the Debt Was Not Discharged?

Some debts survive bankruptcy under § 523.

Examples include certain taxes, domestic support obligations, qualifying student loans, and debts arising from specified misconduct.

A creditor may accurately report an enforceable balance when the debt was not discharged, subject to applicable reporting requirements.

The debtor should determine the obligation's dischargeability before asserting that the balance must be zero.

22. What If the Bankruptcy Case Was Dismissed?

A dismissed bankruptcy case generally differs from one in which the debtor received a discharge.

If the case was dismissed without discharge, the debtor may remain personally liable for the underlying debts.

The credit reporting treatment may therefore differ.

A debtor should not assume that filing bankruptcy, without receiving a discharge, requires creditors to report balances as eliminated.

The actual court orders control.

23. How to Review Credit Reports After Discharge

A debtor should obtain reports from the major consumer reporting agencies and examine the bankruptcy entry and individual accounts.

The review should identify inaccurate balances, improper current delinquencies, duplicate accounts, and other material errors.

The debtor should also verify that accounts actually discharged are reported consistently with the discharge.

The review should distinguish accurate historical information from inaccurate current obligations.

24. Why Credit Repair Companies May Not Be Necessary

A debtor generally can dispute inaccurate credit information directly without paying a credit repair company.

The FCRA provides consumer dispute procedures.

A company cannot lawfully guarantee removal of accurate adverse information merely because the consumer dislikes it.

The debtor should be cautious about expensive services promising immediate deletion of bankruptcy records.

Accurate reporting may remain for the legally permitted period.

25. When Litigation May Be Appropriate

A debtor who has submitted a documented dispute and received an inadequate response may have grounds to consider legal action.

The attorney should review the reports, dispute history, investigation responses, damages, and applicable limitations periods.

Potential claims may arise under the FCRA or, in appropriate circumstances, the discharge injunction.

The remedies and procedural requirements differ.

The debtor should not assume that every error warrants litigation, but persistent material inaccuracies should not be ignored.

Conclusion

A Chapter 7 discharge generally eliminates qualifying personal liabilities, but it does not erase accurate credit history.

Credit reporting agencies and furnishers must comply with the Fair Credit Reporting Act.

Discharged debts should not be reported in a materially misleading manner concerning continuing personal liability.

Consumers may dispute inaccuracies and pursue statutory remedies when the legal requirements are satisfied.

The discharge injunction may provide additional protection when reporting is used as a prohibited collection device.

The objective is not to remove every negative account from the credit report. It is to ensure that the report accurately reflects the debtor's legal and financial position after bankruptcy.

Related Bankruptcy Cases and Authorities

Federal statutes

- 15 U.S.C. § 1681c — Reporting periods.
- 15 U.S.C. § 1681i — Reinvestigation of disputed information.
- 15 U.S.C. § 1681s-2 — Furnisher obligations.
- 15 U.S.C. § 1681n — Willful noncompliance.
- 15 U.S.C. § 1681o — Negligent noncompliance.
- 11 U.S.C. § 524 — Discharge injunction.

Selected decisions

- *Saunders v. Branch Banking & Trust Co.*, 526 F.3d 142 (4th Cir. 2008) — Addresses materially misleading reporting and furnisher obligations.
- *Johnson v. MBNA America Bank, NA*, 357 F.3d 426 (4th Cir. 2004) — Addresses reasonable investigation duties under the FCRA.

- *Dreher v. Experian Information Solutions, Inc.*, 856 F.3d 337 (4th Cir. 2017) — Addresses concrete injury and standing under the FCRA.
- *Spokeo, Inc. v. Robins*, 578 U.S. 330 (2016) — Addresses Article III standing for statutory reporting violations.
- *TransUnion LLC v. Ramirez*, 594 U.S. 413 (2021) — Addresses standing and concrete harm in FCRA litigation.
- *Taggart v. Lorenzen*, 587 U.S. 554 (2019) — Establishes the contempt standard for discharge-injunction violations.

Bankruptcy and Debt Collectors: The Fair Debt Collection Practices Act, Maryland Collection Law, and Remedies for Abusive Collection

Belsky Bankruptcy Legal Library | Debt Collection, Consumer Protection, and Bankruptcy

By Alan J. Belsky, Attorney at Law

Bankruptcy Is Not the Only Protection Against Abusive Debt Collection

Individuals struggling with debt often experience repeated telephone calls, threatening letters, collection lawsuits, wage garnishments, and demands for payment from unfamiliar companies.

Some collection activity is lawful.

Creditors generally may pursue legitimate debts through legally authorized procedures. But federal and Maryland law prohibit specified abusive, deceptive, and unfair collection practices.

The Fair Debt Collection Practices Act, or FDCPA, regulates qualifying debt collectors.

Maryland provides additional protections through the Maryland Consumer Debt Collection Act and related consumer protection statutes.

Bankruptcy adds another layer of protection through the automatic stay and discharge injunction.

These laws overlap in some circumstances, but they are not interchangeable.

A debtor may possess consumer protection claims even before filing bankruptcy. Conversely, a creditor's conduct after bankruptcy may violate the automatic stay or discharge injunction without necessarily establishing an FDCPA violation.

Understanding the differences can help debtors identify unlawful conduct and available remedies.

1. The Fair Debt Collection Practices Act

The FDCPA, 15 U.S.C. § 1692 et seq., prohibits specified abusive, deceptive, and unfair practices by qualifying debt collectors.

The statute generally applies to persons who meet its definition of debt collector.

That definition includes certain businesses whose principal purpose is debt collection and persons who regularly collect debts owed to others.

The FDCPA does not automatically apply to every original creditor collecting its own debts.

However, particular entities may qualify depending on their business activities and statutory definitions.

2. Original Creditors Versus Debt Collectors

A bank collecting its own credit card account ordinarily occupies a different position from a third-party collection agency.

The FDCPA generally focuses on qualifying debt collectors.

However, the Supreme Court has addressed circumstances in which entities purchasing defaulted debts may or may not qualify under particular portions of the definition.

In *Henson v. Santander Consumer USA Inc.*, 582 U.S. 79 (2017), the Court held that an entity collecting debts it purchased for its own account was not a debt collector under the regularly-collects-debts-owed-to-another portion of the statutory definition.

The decision did not eliminate the separate principal-purpose definition.

The entity's actual activities must be examined.

3. Harassing Telephone Calls

Section 1692d prohibits specified conduct intended to harass, oppress, or abuse a person in connection with debt collection.

Examples include repeated telephone calls made with the prohibited intent and certain abusive language.

Federal Regulation F also imposes requirements concerning telephone contact frequency and other collection communications.

The circumstances matter.

Not every unwanted call establishes a statutory violation.

The debtor should preserve call logs, voicemail messages, and other evidence.

4. Threats of Arrest

Debt collectors generally may not falsely threaten arrest or criminal prosecution to obtain payment of an ordinary civil debt.

Section 1692e prohibits specified false or misleading representations.

However, some obligations may arise from conduct that independently supports criminal proceedings.

The collector's statements must be evaluated in context.

A creditor cannot transform an ordinary unpaid credit card balance into a criminal offense merely by threatening arrest.

5. False Threats of Lawsuits or Garnishment

A debt collector may violate the FDCPA by threatening legal action that cannot lawfully be taken or is not intended.

For example, a collector may threaten immediate wage garnishment without possessing a judgment or other lawful basis.

The legality depends on the underlying debt and available remedies.

A collector may accurately describe lawful collection consequences.

But false or misleading threats may violate § 1692e.

6. Collecting Amounts Not Legally Owed

Section 1692f(1) prohibits collection of amounts not expressly authorized by the agreement creating the debt or permitted by law.

A collector may improperly add interest, collection fees, or other charges.

The debtor should obtain an itemized statement.

The collector's assertion that a fee is standard does not necessarily establish that it is legally recoverable.

The governing contract and applicable law control.

7. Debt Validation

Section 1692g establishes requirements concerning validation information and disputes.

A qualifying collector generally must provide specified information concerning the debt and the consumer's rights.

A timely written dispute may trigger obligations to cease collection until verification or other required information is provided.

Regulation F contains additional validation-notice provisions.

The debtor should preserve the notice and any dispute correspondence.

8. Time-Barred Debts

A debt may become unenforceable through a lawsuit because the applicable statute of limitations has expired.

That does not necessarily mean the underlying obligation ceases to exist for every purpose.

Federal and Maryland law may restrict collection activity involving time-barred debts.

Regulation F prohibits qualifying debt collectors from bringing or threatening legal action to collect time-barred debts.

Maryland law may provide additional protections.

The debtor should not assume that a collector's demand establishes that a lawsuit would be timely.

9. Maryland Consumer Debt Collection Act

Maryland Commercial Law Article § 14-202 prohibits specified debt collection practices.

The statute applies to collectors as defined by Maryland law and is not necessarily limited to the same entities covered by the FDCPA.

Prohibited conduct includes certain threats, disclosures, communications, and attempts to enforce rights with knowledge that the right does not exist.

The Maryland statute can provide protection when the FDCPA does not apply.

The particular subsection and required elements must be established.

10. The Maryland Supreme Court's Decision in *Chavis*

In *Chavis v. Blibaum & Associates, P.A.*, 476 Md. 534, 264 A.3d 1254 (2021), the Supreme Court of Maryland addressed claims under the Maryland Consumer Debt Collection Act arising from attempts to collect allegedly unauthorized postjudgment interest.

The decision discusses the statute's knowledge requirement and the circumstances in which a collector may attempt to enforce a right that does not exist.

The case is particularly important for Maryland collection litigation.

A debtor should not assume that every legal error establishes an MCDCA violation.

The statutory knowledge requirement must be considered.

11. The Maryland Consumer Protection Act

The Maryland Consumer Protection Act provides additional remedies concerning unfair, abusive, or deceptive trade practices.

Certain violations of the MCDCA may also constitute unfair or deceptive practices under the MCPA.

However, the requirements for a private damages action must be satisfied.

The debtor should distinguish statutory violations from recoverable damages and available remedies.

12. Maryland Collection Lawsuits

A debt collector may file a lawsuit in the District Court of Maryland or another court with jurisdiction.

The collector must establish the legal basis for the claim.

A debtor may have defenses involving ownership of the debt, the amount claimed, limitations, payment, or other matters.

The debtor should not assume that a collection lawsuit is valid merely because it was filed.

Failure to respond may result in default judgment.

13. Debt Buyers

Debt buyers purchase portfolios of accounts from original creditors or other entities.

They may seek collection through letters, telephone calls, or lawsuits.

The buyer must establish the right to enforce the obligation under applicable law.

Account documentation, assignments, and payment histories may be relevant.

A debtor should not assume that an unfamiliar debt buyer has no enforceable claim.

But the collector's assertion of ownership should be supported when legally required.

14. Wage Garnishment

A judgment creditor may seek wage garnishment under Maryland law.

Maryland provides statutory exemptions and procedures affecting garnishment.

A debtor may challenge improper garnishment or assert available exemptions.

Filing bankruptcy ordinarily stays further garnishment on qualifying prepetition unsecured judgments while the automatic stay applies.

Previously garnished wages may raise separate preference recovery questions.

15. Bank Account Garnishment

A creditor may seek attachment of funds in a bank account.

The debtor may have exemption rights concerning wages, Social Security benefits, or other protected funds.

The legality of the attachment depends on the judgment, procedure, and applicable law.

Bankruptcy may affect further enforcement.

However, funds seized before filing may require additional legal action.

16. Collection After Bankruptcy Filing

Section 362 generally prohibits many collection activities after a qualifying bankruptcy petition is filed.

A debt collector that continues prohibited collection after receiving notice may violate the automatic stay.

Section 362(k) provides remedies for willful violations under specified circumstances.

The debtor should preserve evidence of notice and subsequent collection activity.

The fact that the collector is a third-party agency does not eliminate the obligation to comply with bankruptcy law.

17. Collection After Discharge

Section 524 generally prohibits attempts to collect discharged debts as personal liabilities.

A collector may violate the discharge injunction by demanding payment of a discharged obligation.

However, the legal standard for contempt differs from the standard governing willful automatic-stay violations.

In *Taggart v. Lorenzen*, 587 U.S. 554 (2019), the Supreme Court adopted an objective standard requiring no fair ground of doubt that the discharge order prohibited the conduct.

The debtor should determine whether the debt was discharged and whether the communication constitutes prohibited collection.

18. Can the FDCPA Apply After Bankruptcy?

Potentially, yes.

The FDCPA and Bankruptcy Code may address overlapping conduct.

However, the relationship between the statutes depends on the nature of the claim and governing precedent.

The Supreme Court addressed a related issue in *Midland Funding, LLC v. Johnson*, 581 U.S. 224 (2017), holding that filing an accurate proof of claim on a time-barred debt in Chapter 13 did not constitute the FDCPA violation alleged.

The decision does not establish that every collection act occurring in bankruptcy is immune from the FDCPA.

The particular conduct and statutory provisions matter.

19. Proofs of Claim

A creditor may file a proof of claim in bankruptcy.

The claim may be subject to objection under § 502.

The debtor or trustee may dispute the amount, validity, priority, or enforceability of the claim.

The filing of a proof of claim does not necessarily establish that the creditor is entitled to payment.

However, an inaccurate or disputed claim does not automatically establish an FDCPA violation.

20. What Damages Are Available Under the FDCPA?

Under 15 U.S.C. § 1692k, a qualifying plaintiff may recover actual damages and additional statutory damages subject to the statute's limits.

For an individual action, additional statutory damages generally may not exceed $1,000.

Reasonable attorney's fees and costs may also be available in successful actions.

The amount of recovery depends on the applicable statutory factors and evidence.

The debtor should not assume that every violation automatically results in a $1,000 award.

21. Maryland Debt Collection Damages

Maryland Commercial Law § 14-203 provides a civil remedy for violations of the MCDCA.

A collector that violates the statute may be liable for damages proximately caused by the violation, including damages for emotional distress or mental anguish suffered with or without accompanying physical injury.

The debtor must establish the statutory violation and recoverable harm.

Additional remedies may be available under other applicable laws.

22. The FDCPA Limitations Period

Under 15 U.S.C. § 1692k(d), an FDCPA action generally must be brought within one year from the date the violation occurs.

The Supreme Court addressed the limitations period in *Rotkiske v. Klemm*, 589 U.S. 8 (2019).

The Court held that the ordinary statutory period begins when the violation occurs rather than when it is discovered, while leaving appropriate equitable doctrines for separate consideration.

A debtor should not delay investigating potential claims.

23. Does Bankruptcy Eliminate a Debtor's Claims Against Collectors?

A debtor may possess an FDCPA, MCDCA, or other consumer protection claim before filing bankruptcy.

That claim may become property of the bankruptcy estate under § 541.

The debtor must disclose it.

In Chapter 7, the trustee may acquire authority to prosecute or settle the claim, subject to exemptions and other applicable law.

The debtor should not assume that a consumer protection lawsuit can proceed independently of bankruptcy administration.

24. Why Documentation Matters

Debt collection cases often depend on the content and timing of communications.

The debtor should preserve letters, emails, text messages, call logs, voicemail recordings, court papers, and payment records.

The debtor should also retain evidence of disputes and bankruptcy notices.

A clear chronology can help establish whether the collector violated a statute and what damages resulted.

25. When Bankruptcy Is Preferable to Collection Litigation

A debtor may possess valid claims against one or more debt collectors but still face overwhelming lawful debts.

Consumer protection litigation may address misconduct without eliminating the underlying financial problem.

Chapter 7 may provide broader relief by discharging qualifying debts.

Conversely, a debtor with a limited number of disputed obligations may benefit from asserting defenses or consumer protection rights without filing bankruptcy.

The appropriate strategy depends on the entire financial situation.

Conclusion

Federal and Maryland law provide important protections against abusive, deceptive, and unlawful debt collection.

The FDCPA regulates qualifying debt collectors, while the Maryland Consumer Debt Collection Act may reach a broader range of collection conduct.

Bankruptcy provides additional protections through the automatic stay and discharge injunction.

These remedies overlap but have distinct requirements.

A debtor should not assume that every aggressive collection effort is unlawful—or that a collector may enforce any amount it demands. The collector's legal authority, conduct, and compliance with federal and Maryland law must be examined.

Related Bankruptcy Cases and Authorities

Federal statutes and regulations

- 15 U.S.C. § 1692 et seq. — Fair Debt Collection Practices Act.
- 15 U.S.C. § 1692k — FDCPA civil liability.
- 12 C.F.R. Part 1006 — Regulation F.
- 11 U.S.C. § 362 — Automatic stay.
- 11 U.S.C. § 524 — Discharge injunction.
- 11 U.S.C. § 541 — Estate property.

Maryland statutes

- Maryland Commercial Law § 14-202 — Prohibited collection practices.
- Maryland Commercial Law § 14-203 — Civil remedies.
- Maryland Commercial Law § 13-301 — Unfair, abusive, or deceptive trade practices.

Selected decisions

- *Chavis v. Blibaum & Associates, P.A.*, 476 Md. 534, 264 A.3d 1254 (2021) — Addresses the MCDCA's knowledge requirement and attempts to collect unauthorized interest.
- *Henson v. Santander Consumer USA Inc.*, 582 U.S. 79 (2017) — Addresses the FDCPA definition of debt collector.
- *Midland Funding, LLC v. Johnson*, 581 U.S. 224 (2017) — Addresses filing a proof of claim for a time-barred debt.
- *Rotkiske v. Klemm*, 589 U.S. 8 (2019) — Addresses the FDCPA limitations period.
- *Taggart v. Lorenzen*, 587 U.S. 554 (2019) — Addresses contempt for discharge-injunction violations.
- *Heintz v. Jenkins*, 514 U.S. 291 (1995) — Holds that the FDCPA generally applies to attorneys regularly engaged in debt collection litigation.

Bankruptcy and Debt Settlement Companies: Why Negotiated Settlements Sometimes Cost More Than Chapter 7

Belsky Bankruptcy Legal Library | Alternatives to Bankruptcy and Consumer Debt Relief

By Alan J. Belsky, Attorney at Law

Debt Settlement May Reduce What You Owe, but It Can Also Make a Financial Crisis Worse

Advertisements for debt settlement services frequently promise substantial reductions in credit card balances and other unsecured obligations.

A consumer may be told that creditors will accept a fraction of the amount owed if the consumer stops making payments and deposits money into a designated settlement account.

Sometimes negotiated settlements provide meaningful relief.

But the process can involve substantial risks.

Creditors are not required to settle. Interest and fees may continue accumulating. Collection lawsuits may be filed while the consumer saves money for proposed settlements.

A settlement company may also charge fees that materially reduce the consumer's savings.

In some circumstances, forgiven debt can create taxable income.

For a consumer who qualifies for Chapter 7 bankruptcy, the financial comparison may strongly favor bankruptcy.

However, debt settlement can be appropriate when the consumer has limited debt, substantial nonexempt assets, or another reason to avoid bankruptcy.

The decision should be based on the actual cost, risks, and likely outcome of each alternative.

1. What Is Debt Settlement?

Debt settlement generally involves negotiating with a creditor to accept less than the full amount owed in satisfaction of an obligation.

For example, a creditor owed $20,000 may agree to accept $9,000 as full settlement.

The creditor's willingness to settle depends on the account, collection history, debtor's circumstances, and other considerations.

A settlement may be negotiated directly by the consumer, through an attorney, or through a debt settlement company.

The legal consequences depend on the agreement's terms.

2. How Debt Settlement Companies Operate

Some debt settlement companies instruct consumers to stop paying unsecured creditors and instead accumulate funds in a dedicated account.

The company then attempts to negotiate reduced balances.

The strategy assumes creditors eventually will prefer accepting partial payment rather than continuing collection.

However, creditors are not required to participate.

A creditor may sue before sufficient settlement funds accumulate.

The consumer may therefore face judgments, garnishments, or other collection consequences while waiting.

3. Settlement Companies Cannot Guarantee Results

A debt settlement company cannot force a creditor to accept less than the amount legally owed.

The company may advertise average settlement percentages, but those figures may not predict the consumer's outcome.

Some creditors may refuse to negotiate.

Others may demand larger payments than anticipated.

The consumer should be cautious about representations suggesting that all debts will be settled for a guaranteed percentage.

The actual agreements and creditor responses control.

4. Interest and Fees May Continue Accumulating

When a consumer stops paying credit cards, contractual interest, late fees, and other lawful charges may continue accumulating.

A $15,000 balance may increase substantially before settlement occurs.

Even if the creditor eventually accepts a reduced payment, the savings should be measured against the actual balance and total cost.

The consumer should not compare only the original principal with the negotiated payment.

The settlement company's fees must also be considered.

5. Debt Settlement Fees

Debt settlement companies may charge fees based on the amount of debt enrolled or the savings achieved.

Federal law restricts certain advance fees charged by covered debt relief services.

The Telemarketing Sales Rule, 16 C.F.R. Part 310, contains requirements governing qualifying debt relief services.

The application depends on the provider and manner in which services are marketed.

The consumer should obtain a complete written explanation of fees and when they become payable.

6. The Advance-Fee Rule

Under the Telemarketing Sales Rule, covered debt relief services generally may not collect fees before satisfying specified conditions, including obtaining a settlement or other qualifying alteration of the debt and the consumer making at least one payment under the arrangement.

The rule also addresses dedicated accounts and related consumer protections.

The consumer should not assume that every company demanding an upfront payment is operating lawfully.

However, the application of the rule depends on the service and statutory definitions.

7. Maryland Regulation of Debt Settlement Services

Maryland's Debt Settlement Services Act is in Financial Institutions Title 12, Subtitle 10 and generally uses a provider-registration framework, subject to its definitions and exemptions. Debt management services are separately regulated under Title 12, Subtitle 9 and generally require a license. Verify the provider's actual service and required Maryland registration or license rather than treating the two authorizations as interchangeable.

The existence of a website or national advertising campaign does not establish compliance with Maryland law.

The provider's actual services and legal status matter.

8. Creditors May Sue During Settlement Negotiations

Debt settlement negotiations ordinarily do not automatically stop collection lawsuits.

A creditor may file suit while the consumer is accumulating settlement funds.

If the consumer fails to respond, the creditor may obtain a default judgment.

The creditor may then pursue lawful collection remedies.

The consumer should not assume that enrolling in a settlement program prevents litigation.

9. Wage Garnishment

A judgment creditor may seek wage garnishment under Maryland law.

The consumer may have statutory exemption rights.

However, debt settlement enrollment generally does not create an automatic stay comparable to bankruptcy.

A consumer whose wages are being garnished may find it difficult to accumulate the funds needed for settlement.

Chapter 7 may provide more immediate protection when the automatic stay applies.

10. Bank Account Garnishment

A creditor may also seek attachment of funds in a bank account after obtaining the necessary legal authority.

The consumer may have exemption rights.

But a private debt settlement arrangement generally does not prevent lawful collection proceedings.

A consumer should not assume that money saved for settlement is immune from creditor process.

11. Credit Reporting Consequences

Debt settlement can negatively affect credit reports.

Accounts may become delinquent, charged off, or reported as settled for less than the full balance.

The reporting consequences depend on the creditor and applicable law.

Bankruptcy also affects credit reporting, but it provides a different legal outcome.

A consumer should compare the likely consequences rather than assuming that debt settlement necessarily preserves credit better than Chapter 7.

12. Forgiven Debt May Be Taxable

Under Internal Revenue Code § 61(a)(11), cancellation of indebtedness generally may constitute gross income unless an exclusion or exception applies.

For example, a creditor may forgive $25,000 of a credit card balance.

The consumer may receive a Form 1099-C.

The forgiven amount may create taxable income.

However, the Internal Revenue Code provides exclusions, including certain bankruptcy and insolvency exclusions under § 108.

The consumer should not assume that every settlement creates taxable income or that every forgiven amount is automatically tax-free.

13. The Insolvency Exclusion

Section 108(a)(1)(B) excludes qualifying cancellation-of-debt income to the extent the taxpayer was insolvent immediately before the discharge.

Insolvency generally involves liabilities exceeding the fair market value of assets under the statutory definition.

The exclusion requires an appropriate calculation.

A consumer should not assume that having substantial credit card debt automatically establishes insolvency.

Assets and liabilities must be evaluated.

14. Bankruptcy and Cancellation-of-Debt Income

Section 108(a)(1)(A) generally excludes qualifying discharge-of-indebtedness income when the discharge occurs in a Title 11 bankruptcy case and the taxpayer is under the court's jurisdiction.

This can provide an important tax distinction between ordinary negotiated settlements and debts discharged through bankruptcy.

However, tax attributes may be reduced under § 108(b).

The debtor should consider the complete tax consequences.

15. Example: Settlement Versus Chapter 7

Assume a consumer owes $80,000 in unsecured credit card debt.

A settlement company proposes negotiating settlements averaging 45% of the enrolled balances.

If successful, the consumer may need approximately $36,000 to fund settlements, plus applicable fees.

Interest and charges may increase the balances before settlement.

The consumer may also face potential cancellation-of-debt tax consequences.

If the consumer qualifies for Chapter 7 and has fully protected assets, the same debts may be discharged without funding a multiyear settlement program.

The comparison depends on eligibility, assets, and the actual debts involved.

16. When Debt Settlement May Be Preferable

Debt settlement may be appropriate when the consumer has a manageable number of obligations and sufficient funds to resolve them.

For example, a consumer may owe $18,000 to one creditor and have access to a reasonable lump-sum settlement.

The consumer may prefer negotiation over bankruptcy.

Debt settlement may also be considered when bankruptcy would expose valuable nonexempt property to liquidation.

The decision should reflect the consumer's actual circumstances.

17. Settling One Debt Does Not Resolve Others

A consumer may settle one credit card account while remaining liable for several others.

The successful settlement does not automatically protect the consumer from collection by other creditors.

A settlement program may therefore produce uneven results.

The consumer should evaluate whether the proposed settlements provide a comprehensive solution.

Chapter 7 generally addresses qualifying unsecured debts collectively through the bankruptcy process.

18. Preference Risks Before Bankruptcy

A consumer may make substantial payments to selected creditors shortly before filing bankruptcy.

Under § 547, certain transfers may be avoidable as preferences.

Payments to ordinary creditors within ninety days before filing may receive scrutiny.

Payments to insiders may be examined over a longer statutory period.

The applicable monetary threshold and other requirements matter.

A debtor should disclose significant settlement payments made before bankruptcy.

19. Settlements With Family Members

A debtor may repay relatives before filing bankruptcy because of personal obligations or family pressure.

Such payments may create preference exposure.

The trustee may seek recovery from the recipient when the statutory requirements are satisfied.

The debtor should not assume that repayment of a genuine family loan is automatically protected.

The timing and relationship matter.

20. Settlement Agreements Must Be Clear

A negotiated settlement should establish the amount to be paid, payment deadline, and legal effect of payment.

The agreement should address whether the creditor releases the remaining balance and whether any judgment or lien will be satisfied.

A debtor should not rely solely on an oral promise.

The creditor's authority to settle should also be established.

A settlement that fails to resolve a judgment lien may leave significant problems.

21. What If the Consumer Defaults on the Settlement?

Some settlements require installment payments.

The agreement may provide consequences if the consumer misses a payment.

The creditor may claim that the original balance or another amount becomes due.

The enforceability depends on the agreement and applicable law.

A consumer should not assume that a partial payment permanently resolves the debt unless the settlement terms provide that result.

22. Debt Management Plans Are Different

A debt management plan generally involves repayment of debts under negotiated interest rates or payment arrangements.

It does not necessarily involve forgiveness of principal.

Nonprofit credit counseling agencies may offer such plans.

The consumer should distinguish debt management from debt settlement.

The cost, credit consequences, and legal effects differ.

23. Negotiating Directly With Creditors

A consumer may negotiate directly with creditors without hiring a debt settlement company.

Some creditors may consider hardship arrangements, reduced interest, payment plans, or lump-sum settlements.

The consumer should obtain written confirmation of any agreement.

Direct negotiation may avoid settlement company fees.

However, the consumer must still consider tax consequences, credit reporting, and the risk of collection by other creditors.

24. When Bankruptcy Provides a More Complete Solution

Chapter 7 may be particularly attractive when the consumer has substantial unsecured debt, limited nonexempt property, and no realistic ability to fund settlements.

The automatic stay generally provides immediate protection against many collection activities.

The discharge ordinarily eliminates qualifying personal liabilities.

However, Chapter 7 does not eliminate every debt or lien.

The debtor's assets and eligibility must be evaluated.

25. Why the Comparison Should Be Made Before Enrolling

A consumer should compare debt settlement and bankruptcy before committing substantial money to a settlement program.

The analysis should include the amount owed, expected settlement payments, company fees, taxes, collection risks, assets, income, and available bankruptcy exemptions.

A consumer who spends years accumulating settlement funds may discover that Chapter 7 could have provided a faster and less expensive resolution.

Conversely, a consumer with limited debt and substantial nonexempt property may find negotiation preferable.

Conclusion

Debt settlement can provide meaningful relief in appropriate circumstances, but it is not necessarily cheaper or safer than bankruptcy.

Creditors are not required to settle. Interest and fees may accumulate. Collection lawsuits and garnishments may continue.

Forgiven debt may also create taxable income.

Chapter 7 offers a different form of relief by discharging qualifying debts through a federal court proceeding.

Before paying a debt settlement company, a consumer should determine whether Chapter 7 or another bankruptcy option would provide a more complete and economical solution.

Related Bankruptcy Cases and Authorities

Federal statutes and regulations

- 11 U.S.C. § 362 — Automatic stay.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 547 — Preferential transfers.
- 26 U.S.C. § 61(a)(11) — Cancellation-of-debt income.
- 26 U.S.C. § 108 — Exclusions from cancellation-of-debt income.
- 16 C.F.R. Part 310 — Telemarketing Sales Rule.

Maryland law

- Maryland Financial Consumer Protection laws — Applicable regulation of debt settlement and management services.
- Maryland Office of Financial Regulation — Licensing and consumer information.

Selected decisions

- *United States v. Kirby Lumber Co.*, 284 U.S. 1 (1931) — Addresses income arising from discharge of indebtedness.
- *Commissioner v. Tufts*, 461 U.S. 300 (1983) — Addresses tax consequences of liabilities and property dispositions.
- *Grogan v. Garner*, 498 U.S. 279 (1991) — Addresses dischargeability litigation standards.
- *Midland Funding, LLC v. Johnson*, 581 U.S. 224 (2017) — Addresses time-barred claims in bankruptcy.
- *In re Bane*, 720 F.3d 465 (4th Cir. 2013) — Addresses fraudulent transfers and discharge consequences.

Bankruptcy and Divorce in Maryland: Marital Property, Joint Debts, Support Obligations, and the Consequences of Filing Before or After Divorce

Belsky Bankruptcy Legal Library | Divorce, Property Rights, and Dischargeability

By Alan J. Belsky, Attorney at Law

The Timing of Bankruptcy and Divorce Can Change the Outcome of Both Proceedings

Bankruptcy and divorce frequently arise from the same financial difficulties.

A married couple may have substantial credit card debt, a jointly owned home, automobile loans, tax obligations, and disputes over who should pay particular debts after separation.

One spouse may wish to file bankruptcy while the other does not.

The timing of the bankruptcy can materially affect ownership of property, the enforceability of divorce-related obligations, and the protection available against creditors.

Maryland law adds an important consideration: property owned by spouses as tenants by the entirety may receive substantial protection from creditors holding claims against only one spouse.

Divorce ordinarily terminates that form of ownership.

A bankruptcy filed before divorce may therefore produce a substantially different result from one filed afterward.

Domestic support obligations also receive special treatment and generally survive bankruptcy.

A careful analysis requires coordination of bankruptcy law, Maryland domestic relations law, and the parties' contractual obligations.

1. Bankruptcy and Divorce Are Separate Legal Proceedings

A Maryland divorce proceeding determines issues such as marital property, support, and obligations between spouses.

Bankruptcy determines the debtor's estate, creditor rights, exemptions, and dischargeability under federal law.

The proceedings may affect one another, but neither automatically resolves every issue pending in the other.

For example, a divorce decree may require one spouse to pay a joint credit card debt.

That order does not necessarily release the other spouse from liability to the credit card issuer.

Likewise, a bankruptcy discharge may affect personal liability to a creditor without eliminating every obligation arising from the divorce.

2. Filing Bankruptcy Before Divorce

A married individual may file Chapter 7 before the divorce becomes final.

At that time, the debtor may own property jointly with the spouse, including property held as tenants by the entirety.

The debtor's interest generally becomes property of the bankruptcy estate under § 541, subject to applicable exemptions.

The timing of the filing may preserve exemption rights that would not exist after divorce.

However, the debtor must consider joint creditors, pending property division, and the potential effect of subsequent divorce proceedings.

Section 541(a)(5)(B) also brings into the estate certain property interests acquired or becoming available within 180 days after filing through a property settlement with the debtor's spouse or an interlocutory or final divorce decree. Filing before the divorce does not automatically exclude a later property award from the Chapter 7 estate.

Filing before divorce is not automatically preferable.

3. Filing Bankruptcy After Divorce

Once the divorce becomes final, the former spouses' property rights may change.

Property formerly held as tenants by the entirety ordinarily becomes owned in another form unless otherwise transferred or disposed of under applicable law.

For example, real estate may become held as tenants in common.

A debtor who files Chapter 7 after divorce may therefore possess a fractional ownership interest that is subject to different creditor rights and exemptions.

The debtor should not assume that the absence of a new deed means the prior entireties ownership continues.

The legal effect of divorce must be examined.

4. Tenancy by the Entirety in Maryland

Maryland recognizes tenancy by the entirety as a form of ownership available to married spouses.

Qualifying entireties property generally cannot be reached by a creditor holding a claim against only one spouse.

However, creditors holding qualifying joint claims against both spouses may have rights against the property.

Section 522(b)(3)(B) provides bankruptcy exemption protection for certain entireties interests to the extent exempt from process under applicable nonbankruptcy law.

The debtor's ownership interest and the nature of creditor claims must be established.

5. The Fourth Circuit's Decision in *Sumy*

In *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985), the Fourth Circuit addressed tenancy-by-the-entirety property and the rights of joint creditors in bankruptcy.

The decision recognizes the significance of joint obligations when entireties property is involved.

A debtor should not assume that entireties ownership provides unlimited protection merely because only one spouse files bankruptcy.

The existence and amount of joint debts can materially affect the analysis.

6. Divorce Terminates Tenancy by the Entirety

When spouses divorce, tenancy-by-the-entirety ownership ordinarily terminates.

The former spouses may become tenants in common unless a valid agreement, decree, or conveyance establishes a different result.

This can occur even when the land records still reflect the original deed.

The legal consequences of divorce are not necessarily dependent on immediate recording of a new deed.

A debtor considering bankruptcy should determine the present ownership form rather than relying solely on how title was originally acquired.

7. Example: The Same Home Before and After Divorce

Assume spouses own a residence as tenants by the entirety.

The property has $180,000 in equity.

One spouse owes substantial individual credit card debt, while the couple has relatively little joint unsecured debt.

Before divorce, the debtor's entireties exemption may provide substantial protection against individual creditors.

After divorce, the debtor may own an undivided one-half interest as a tenant in common.

That interest may be exposed to Chapter 7 administration to the extent not otherwise exempt.

The difference can be significant.

8. Maryland's Increased Residential Exemption

Maryland increased the bankruptcy residential-property exemption to $125,000 effective June 1, 2026.

The expanded exemption may provide additional protection for qualifying homeowners.

However, it does not make tenancy-by-the-entirety analysis irrelevant.

The two protections arise under different legal principles.

A debtor should determine whether the property qualifies for the residential exemption, the amount of equity, the ownership structure, and the existence of joint creditors.

9. Marital Property Versus Titled Property

Maryland domestic relations law distinguishes marital property from legal title.

Property may be considered marital property for purposes of equitable distribution even when titled in only one spouse's name.

Bankruptcy estate ownership generally depends on the debtor's legal and equitable interests under applicable law.

A spouse's potential claim for monetary relief in divorce may not be identical to a present ownership interest in particular property.

The bankruptcy court may need to determine the nature of the debtor's interest.

10. The Automatic Stay and Divorce Proceedings

Section 362(b)(2) provides exceptions for specified domestic relations proceedings.

Certain actions concerning divorce, support, child custody, and related matters may continue notwithstanding bankruptcy.

However, the exception does not necessarily permit division or transfer of property belonging to the bankruptcy estate without regard to the stay.

The distinction between determining marital status and administering estate property is important.

The parties should not assume that every aspect of a divorce case is automatically stayed or automatically exempt from the stay.

11. Divorce Decrees and Joint Creditors

A divorce decree may require one spouse to pay a joint debt.

For example, the decree may direct the husband to pay a jointly owed automobile loan.

The lender ordinarily retains its contractual rights against both borrowers unless it agrees to release one.

The spouse assigned responsibility may also owe a separate obligation to the other spouse under the divorce decree.

Bankruptcy may affect these obligations differently.

12. Domestic Support Obligations

Section 523(a)(5) generally excepts domestic support obligations from discharge.

Section 101(14A) defines domestic support obligations.

Qualifying child support and alimony ordinarily survive Chapter 7 and Chapter 13.

The legal characterization depends on the substance of the obligation.

A payment labeled property settlement may actually function as support.

Conversely, an obligation labeled alimony may require examination of its actual purpose.

13. Property Settlement Obligations

Section 523(a)(15) addresses certain divorce-related debts owed to a spouse, former spouse, or child that are not domestic support obligations.

In Chapter 7, qualifying obligations under § 523(a)(15) generally are nondischargeable.

The treatment can differ in Chapter 13.

A debtor should not assume that every debt allocated in a divorce agreement is dischargeable merely because it is not alimony or child support.

The identity of the obligee and nature of the obligation matter.

14. Chapter 13 and Divorce-Related Debts

Chapter 13 provides different discharge treatment for certain obligations under § 523(a)(15).

A qualifying non-support divorce-related obligation may be dischargeable upon completion of a Chapter 13 plan, subject to applicable law.

Domestic support obligations remain protected.

This distinction can materially affect chapter selection.

However, Chapter 13 imposes repayment and confirmation requirements.

The debtor should not assume that filing Chapter 13 automatically eliminates every property settlement obligation.

15. Hold-Harmless and Indemnification Agreements

A marital settlement agreement may require one spouse to indemnify the other for a joint debt.

For example, one spouse may agree to pay a credit card and hold the other harmless.

The creditor may still pursue the nonpaying spouse if that spouse remains contractually liable.

The indemnification provision creates a separate obligation between the former spouses.

Its bankruptcy treatment may fall under § 523(a)(15).

The debtor should distinguish the creditor's claim from the former spouse's reimbursement claim.

16. Parent PLUS Loans in Divorce

Parent PLUS loans generally are obligations of the parent borrower.

A divorce agreement may require former spouses to share repayment.

That agreement ordinarily does not make the nonborrower spouse directly liable to the federal government.

However, it may create a separate contractual or divorce-related obligation between the spouses.

The federal student loan may remain nondischargeable under § 523(a)(8), while the interspousal obligation requires separate analysis under § 523(a)(15) or other applicable provisions.

17. Joint Tax Obligations

Spouses who filed joint income tax returns may possess joint and several federal tax liability, subject to applicable relief provisions.

Divorce does not automatically release either spouse from liability to the IRS.

A settlement agreement allocating tax responsibility generally does not bind the government.

One spouse may qualify for innocent spouse or other relief under tax law.

Bankruptcy dischargeability must be determined separately for each spouse and tax period.

18. Divorce-Related Attorney's Fees

A divorce court may award attorney's fees to one spouse.

The bankruptcy treatment depends on the nature and purpose of the award.

Some fee obligations may qualify as domestic support obligations.

Others may fall within § 523(a)(15).

The court should examine the underlying order and circumstances.

The fact that the obligation is described as attorney's fees does not automatically determine dischargeability.

19. Retirement Accounts and Divorce

Retirement accounts and pensions may be divided through divorce-related orders.

A qualified domestic relations order may establish rights in qualifying retirement benefits.

The bankruptcy treatment depends on the plan, order, and debtor's actual property interest.

A debtor should disclose retirement interests and relevant divorce-related rights.

The timing and legal effectiveness of a division order may be important.

20. What If the Divorce Is Pending When Bankruptcy Is Filed?

A pending divorce can complicate bankruptcy estate administration.

The debtor may possess property interests subject to unresolved domestic relations claims.

The bankruptcy trustee may have rights concerning estate property.

The divorce court may retain authority over matters excepted from the automatic stay.

Coordination between bankruptcy and domestic relations counsel is important.

The parties should not assume that filing bankruptcy resolves disputed property division.

21. Transfers Under Marital Settlement Agreements

A debtor may transfer real estate, money, or other assets to a spouse under a marital settlement agreement.

Such transfers may be examined under bankruptcy avoidance provisions.

The trustee may investigate whether the transfer was made for reasonably equivalent value or with actual fraudulent intent.

The fact that a transfer occurred in connection with divorce does not automatically immunize it from bankruptcy scrutiny.

The timing and circumstances matter.

22. Fraudulent Transfers in Divorce

Sections 544 and 548 may permit trustees to challenge qualifying transfers.

For example, a debtor may transfer substantially all valuable property to a spouse shortly before filing while retaining substantial unsecured debt.

The trustee may examine whether the transfer is avoidable.

A bona fide divorce settlement may involve legitimate consideration and property rights.

The analysis requires examination of the actual agreement and surrounding circumstances.

23. Bankruptcy and Family Support Enforcement

Domestic support obligations receive special treatment.

Section 362(b)(2) contains exceptions permitting specified support-related proceedings and collection activities.

Domestic support claims may also receive priority under § 507(a)(1).

A debtor should not assume that filing bankruptcy stops every child support enforcement measure.

The type of proceeding and source of funds matter.

24. What If One Spouse Files and the Other Does Not?

An individual spouse may file bankruptcy without the other spouse joining.

The filing generally affects the debtor's personal liability and estate property.

The nonfiling spouse ordinarily remains liable for separately enforceable joint obligations.

However, entireties property, household income, tax obligations, and divorce-related claims may create additional issues.

The debtor should not assume that an individual filing has no consequences for the nonfiling spouse.

25. Why Timing Should Be Evaluated Before Either Proceeding

A debtor contemplating both bankruptcy and divorce should evaluate the sequence before taking action.

Filing before divorce may preserve certain entireties protections.

Filing after divorce may alter ownership interests and expose property to administration.

Domestic support and property settlement obligations may survive bankruptcy differently.

Transfers made through divorce may also receive trustee scrutiny.

The appropriate sequence depends on the particular assets, debts, ownership interests, and objectives—not a universal rule that bankruptcy should always come before or after divorce.

Conclusion

Bankruptcy and divorce can profoundly affect one another.

Maryland tenancy-by-the-entirety law makes timing particularly important because divorce ordinarily terminates that form of ownership.

Domestic support obligations generally survive bankruptcy, while other divorce-related debts may receive different treatment under Chapters 7 and 13.

Joint creditors retain rights that may not be eliminated by a marital settlement agreement.

Property transfers, retirement interests, and tax obligations also require careful analysis.

A person contemplating both divorce and bankruptcy should coordinate the two proceedings before finalizing property transfers or selecting a bankruptcy filing date.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 101(14A) — Domestic support obligations.
- 11 U.S.C. § 362(b)(2) — Domestic relations exceptions to the automatic stay.
- 11 U.S.C. § 522(b)(3)(B) — Entireties property exemption.
- 11 U.S.C. § 523(a)(5), (15) — Domestic support and divorce-related obligations.
- 11 U.S.C. § 544 — Trustee avoidance powers.
- 11 U.S.C. § 548 — Fraudulent transfers.
- 11 U.S.C. § 1328 — Chapter 13 discharge.

Maryland law

- Maryland Family Law Article — Divorce, marital property, and support.
- Maryland Courts and Judicial Proceedings § 11-504 — Exemptions.

Selected decisions

- *Sumy v. Schlossberg*, 777 F.2d 921 (4th Cir. 1985) — Addresses entireties property and joint creditors.
- *In re Bunker*, 312 F.3d 145 (4th Cir. 2002) — Addresses tenancy-by-the-entirety exemption issues.

- Roberge v. Buis (In re Roberge), 188 B.R. 366 (E.D. Va. 1995), aff'd, 95 F.3d 42 (4th Cir. 1996) (unpublished table decision) — Supports relief from the stay to permit a state court to determine divorce-related property interests; the unpublished affirmance is historical, nonbinding authority.
- Catron v. Catron (In re Catron), 43 F.3d 1465 (4th Cir. 1994) (unpublished table decision) — Applies the pre-2005 support analysis to a marital obligation; historical, nonbinding context rather than a replacement for current § 523(a)(5) and (15).
- *Stern v. Marshall*, 564 U.S. 462 (2011) — Addresses bankruptcy court constitutional authority in a different context.

Chapter 13 Bankruptcy in Maryland: How the Repayment Plan Works, Who Qualifies, and What Happens Over Three to Five Years

Belsky Bankruptcy Legal Library | Chapter 13 Bankruptcy

By Alan J. Belsky, Attorney at Law

Chapter 13 Allows Individuals to Repay Debts While Retaining Their Property

Chapter 13 bankruptcy provides a means for individuals with regular income to reorganize their financial obligations through a court-supervised repayment plan.

Unlike Chapter 7, which generally involves liquidation of nonexempt property and discharge of qualifying debts, Chapter 13 ordinarily permits debtors to retain their property while making payments over three to five years.

Chapter 13 can be particularly valuable for homeowners facing foreclosure, individuals with substantial nonexempt assets, and debtors who need time to cure mortgage arrears or address certain tax obligations.

But Chapter 13 is not simply Chapter 7 with monthly payments.

The debtor must propose a legally sufficient plan, make required payments, comply with trustee and court requirements, and complete the plan before receiving the ordinary Chapter 13 discharge.

The process requires a realistic evaluation of income, expenses, secured debts, priority obligations, and the value of nonexempt property.

A plan that appears affordable on paper may fail if it does not account for the debtor's actual financial circumstances.

1. Who Is Eligible for Chapter 13?

Under 11 U.S.C. § 109(e), Chapter 13 generally is available to qualifying individuals with regular income whose noncontingent, liquidated debts fall below the applicable statutory limits.

The debtor may be employed, self-employed, retired, or receiving another sufficiently regular source of income.

The source of income matters less than whether the debtor can fund a feasible plan.

Chapter 13 is not available to corporations or LLCs.

However, a sole proprietor may qualify because the business and individual are not separate legal entities.

2. Chapter 13 Debt Limits

For cases filed under the currently verified April 2025 debt-limit adjustments, Chapter 13 generally requires:

Debt category	Limit
Noncontingent, liquidated unsecured debt	Less than $526,700
Noncontingent, liquidated secured debt	Less than $1,580,125

These limits are subject to statutory changes and periodic adjustments.

Debt classification can be complicated when the debtor has personal guarantees, disputed claims, undersecured obligations, or substantial judgments.

The debt limits should be calculated before filing.

3. What Is Regular Income?

Section 101(30) defines an individual with regular income as an individual whose income is sufficiently stable and regular to enable payments under a Chapter 13 plan.

A debtor need not necessarily receive a conventional salary.

Qualifying income may include wages, self-employment earnings, pension payments, rental income, or other reliable sources.

The debtor must establish that the proposed plan is feasible.

A speculative expectation of future income ordinarily is not enough.

4. How Chapter 13 Differs From Chapter 7

Chapter 7 generally provides relatively prompt discharge of qualifying debts, subject to liquidation of nonexempt property.

Chapter 13 involves a repayment plan lasting several years.

The debtor ordinarily retains possession of property while satisfying plan obligations.

Chapter 13 may provide mechanisms for curing mortgage arrears, modifying certain secured debts, and paying priority obligations over time.

However, the debtor must commit sufficient income to satisfy statutory confirmation requirements.

The choice depends on the debtor's assets, debts, income, and objectives.

5. The Automatic Stay

Filing Chapter 13 ordinarily triggers the automatic stay under § 362.

The stay generally prohibits many collection activities involving prepetition debts.

It may stop foreclosure, repossession, garnishment, and collection lawsuits while applicable.

However, exceptions and repeat-filing limitations may affect protection.

The stay is not a guarantee that the debtor may retain property regardless of future defaults.

Creditors may seek relief when statutory grounds exist.

6. The Chapter 13 Repayment Plan

The debtor proposes a plan specifying how qualifying creditors will be treated.

The plan may provide for mortgage arrears, vehicle loans, priority taxes, domestic support obligations, and unsecured debts.

The debtor ordinarily makes periodic payments to the Chapter 13 trustee.

The trustee distributes funds according to the confirmed plan and applicable law.

Some ongoing obligations may be paid directly by the debtor rather than through the trustee.

The precise arrangement depends on the plan and local practice.

7. How Long Does the Plan Last?

Chapter 13 plans generally last three to five years.

The applicable commitment period is governed by § 1325(b)(4).

The debtor's current monthly income, household size, and applicable median-income threshold may affect the required period.

Below-median debtors generally have a three-year applicable commitment period, subject to statutory qualifications.

Above-median debtors generally have a five-year period.

A plan ordinarily may not exceed five years.

For below-median debtors, § 1322(d) ordinarily limits the plan to three years unless the court approves a longer period for cause, up to five years. Under § 1325(b)(4)(B), the applicable commitment period may be shorter if all allowed unsecured claims are paid in full over that shorter period. Merely proposing a fixed dollar amount or showing little disposable income does not itself establish a right to end the plan early.

8. What Is Disposable Income?

Disposable income generally concerns income available after deductions permitted by the Bankruptcy Code.

Section 1325(b) governs projected disposable income when the trustee or an unsecured creditor objects to confirmation.

The calculation may differ from the debtor's actual monthly cash flow.

For above-median debtors, certain expense deductions are determined under statutory standards.

For below-median debtors, reasonably necessary expenses remain important.

The debtor should not assume that the amount left in a checking account each month automatically determines the required plan payment.

9. The Means Test in Chapter 13

The means-test forms help determine current monthly income and certain deductions.

The calculation generally uses income received during the six full calendar months preceding filing, subject to statutory rules.

Current monthly income may differ from the debtor's present earnings.

For example, a debtor may have recently lost a high-paying job.

The historical six-month average may exceed current income.

The Supreme Court addressed the use of known or virtually certain changes in income and expenses in *Hamilton v. Lanning*, 560 U.S. 505 (2010).

The debtor's projected disposable income may require adjustments under applicable law.

10. The Best-Interests-of-Creditors Test

Section 1325(a)(4) generally requires unsecured creditors to receive at least as much under the Chapter 13 plan as they would receive in a hypothetical Chapter 7 liquidation.

This is commonly called the liquidation test.

For example, a debtor may have $40,000 in nonexempt property value available for unsecured creditors in Chapter 7.

The Chapter 13 plan generally must provide unsecured creditors with at least the required liquidation value.

The debtor's ability to retain property does not eliminate the obligation to satisfy this test.

11. Secured Creditors

Secured creditors possess liens against property.

Chapter 13 may permit the debtor to cure arrears, maintain payments, or modify certain secured claims.

The treatment depends on the collateral and statutory requirements.

Home mortgages secured solely by the debtor's principal residence receive special protection.

Vehicle loans may be subject to the 910-day rule.

The debtor should not assume that every secured claim can be reduced to collateral value.

12. Mortgage Arrears

Chapter 13 can be particularly useful for homeowners who have fallen behind on mortgage payments.

Section 1322(b)(5) generally permits curing qualifying defaults within a reasonable time while maintaining ongoing payments.

For example, a debtor may owe $30,000 in mortgage arrears.

A feasible plan may provide for repayment over the plan period while the debtor maintains current mortgage payments.

However, the debtor must have sufficient income to fund both obligations.

Chapter 13 does not make an unaffordable mortgage affordable merely by spreading arrears over time.

13. Automobile Loans

Chapter 13 may permit treatment of vehicle loans through the plan.

Depending on the acquisition date and loan characteristics, the debtor may be able to modify the secured claim.

The 910-day provision may restrict cramdown for certain recently acquired vehicles.

The debtor must also provide appropriate treatment of secured creditors under § 1325(a)(5).

A realistic vehicle budget is important to plan feasibility.

14. Priority Debts

Certain debts receive priority under § 507.

Examples include qualifying domestic support obligations and certain taxes.

Chapter 13 generally requires specified treatment of priority claims.

Some priority obligations must be paid in full through the plan unless the holder agrees to different treatment.

The debtor should identify priority debts before filing.

Failure to account for them can make a proposed plan infeasible.

15. Unsecured Creditors

Ordinary unsecured creditors may include credit card companies, medical providers, personal lenders, and other creditors without collateral or priority status.

Chapter 13 does not necessarily require payment of every unsecured debt in full.

The amount paid depends on projected disposable income, liquidation value, and other statutory requirements.

Some plans provide substantial repayment.

Others may provide little or no distribution to general unsecured creditors.

The debtor should not assume that Chapter 13 always requires repayment of 100% of unsecured debt.

16. When Do Plan Payments Begin?

Under § 1326(a)(1), the debtor generally must begin making required payments within thirty days after filing the plan or the order for relief, whichever is earlier, unless the court orders otherwise.

Payments ordinarily begin before plan confirmation.

The debtor should not wait for the confirmation hearing before beginning payments.

Failure to commence payments may lead to dismissal or other consequences.

17. The Meeting of Creditors

Under § 341, the debtor must ordinarily attend a meeting of creditors.

The Chapter 13 trustee conducts the examination.

The trustee may ask about income, expenses, assets, debts, transfers, and the proposed plan.

Creditors may participate.

The debtor should provide requested documents and answer accurately.

The meeting is not the same as the confirmation hearing.

18. The Confirmation Hearing

The bankruptcy court determines whether the proposed plan satisfies the statutory requirements.

The trustee or creditors may object.

Issues may include feasibility, disposable income, secured claim treatment, priority claims, and the liquidation test.

The debtor may need to amend the plan.

Once confirmed, the plan generally binds the debtor and creditors as provided by § 1327.

19. What If the Debtor Cannot Afford the Proposed Payment?

A plan must be feasible.

Section 1325(a)(6) requires the court to determine that the debtor will be able to make all payments under the plan and comply with it.

A debtor should not propose an unrealistic payment merely to obtain temporary relief from foreclosure or repossession.

The budget should account for ordinary living expenses and foreseeable irregular costs.

A plan that cannot be maintained is unlikely to provide lasting relief.

20. Changes in Income During the Plan

A Chapter 13 debtor may experience job loss, illness, retirement, increased income, or other financial changes.

Section 1329 permits modification of a confirmed plan in specified circumstances before completion of payments.

The debtor may seek to adjust payments or other plan provisions.

However, modification is not automatic.

The proposed change must satisfy applicable statutory requirements.

The debtor should promptly notify counsel of material changes.

21. What If the Debtor Misses Payments?

Failure to make required plan payments may lead to a motion to dismiss or convert under § 1307(c).

The trustee may seek relief when payments become delinquent.

The debtor may have an opportunity to cure the default or seek modification.

But repeated or substantial nonpayment can jeopardize the case.

If the case is dismissed, the debtor generally loses the protection of the automatic stay.

Creditors may resume lawful collection.

22. Dismissal Versus Discharge

A Chapter 13 case that is dismissed ordinarily does not produce the same result as successful completion and discharge.

The debtor may remain liable for unpaid obligations.

The automatic stay generally terminates upon dismissal.

Creditors may resume collection, subject to applicable law.

The debtor should not assume that payments made during an unsuccessful Chapter 13 case eliminated every remaining debt.

23. Conversion to Chapter 7

A Chapter 13 debtor may be able to convert the case to Chapter 7 under § 1307, subject to applicable law.

Conversion may be appropriate when the debtor can no longer fund the plan.

However, conversion can expose nonexempt property to Chapter 7 administration.

The debtor's eligibility for Chapter 7 and the consequences of conversion must be examined.

Section 348(f) governs the converted estate, including the different rule for a bad-faith conversion. Harris v. Viegelahn, 575 U.S. 510 (2015), specifically holds that undistributed postpetition wages held by the Chapter 13 trustee must be returned to the debtor following the good-faith conversion addressed there; it does not decide every valuation or conversion-property question.

24. Hardship Discharge

Section 1328(b) permits a hardship discharge in limited circumstances when the debtor cannot complete plan payments because of circumstances for which the debtor should not justly be held accountable.

The debtor must satisfy additional statutory requirements.

The hardship discharge is narrower than the ordinary Chapter 13 discharge.

It does not necessarily eliminate the same categories of debt.

The remedy should be considered when plan completion becomes impossible for reasons beyond the debtor's control.

25. The Chapter 13 Discharge

After completing required plan payments and satisfying applicable statutory conditions, the debtor may receive a discharge under § 1328(a).

The discharge generally eliminates qualifying remaining debts.

Certain obligations survive, including specified domestic support obligations, student loans absent undue hardship, and other statutory exceptions.

The debtor must also satisfy applicable certification and educational requirements.

The discharge ordinarily marks the successful completion of the repayment process.

26. Why Chapter 13 Requires Long-Term Planning

A Chapter 13 plan may last sixty months.

During that period, the debtor must continue paying housing, utilities, food, transportation, insurance, and other necessary expenses.

Unexpected repairs, employment changes, medical expenses, and family obligations can disrupt the budget.

A successful plan should account for realistic financial conditions rather than assuming every month will be identical.

The debtor should understand the commitment before filing.

27. When Chapter 13 May Be Preferable to Chapter 7

Chapter 13 may be preferable when the debtor needs to cure mortgage arrears, retain nonexempt property, address priority taxes, or obtain other relief unavailable through Chapter 7.

It may also be appropriate when the debtor does not qualify for Chapter 7 relief under applicable provisions.

However, Chapter 13 requires sufficient income and long-term compliance.

A debtor who qualifies for Chapter 7 and has fully protected property may obtain more efficient relief through Chapter 7.

The choice should be based on the debtor's actual objectives and circumstances.

Conclusion

Chapter 13 permits qualifying individuals to reorganize debts through a repayment plan lasting generally three to five years.

It can provide powerful tools for retaining property, curing mortgage arrears, and addressing secured and priority obligations.

But the debtor must propose a feasible plan, satisfy confirmation requirements, make payments, and complete the process.

The amount paid to unsecured creditors depends on statutory requirements rather than a universal percentage.

Chapter 13 is most effective when the debtor has stable income, a realistic budget, and a clear reason to pursue repayment rather than Chapter 7 liquidation.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 109(e) — Chapter 13 eligibility.
- 11 U.S.C. § 101(30) — Individual with regular income.
- 11 U.S.C. § 1322 — Contents of Chapter 13 plan.
- 11 U.S.C. § 1325 — Plan confirmation.
- 11 U.S.C. § 1326 — Payments.
- 11 U.S.C. § 1327 — Effect of confirmation.
- 11 U.S.C. § 1328 — Discharge.
- 11 U.S.C. § 1329 — Plan modification.
- 11 U.S.C. § 1307 — Conversion and dismissal.

Selected decisions

- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Addresses projected disposable income.
- *Ransom v. FIA Card Services, N.A.*, 562 U.S. 61 (2011) — Addresses means-test vehicle ownership deductions.
- *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004) — Addresses secured claim interest rates.
- *Harris v. Viegelahn*, 575 U.S. 510 (2015) — Addresses undistributed Chapter 13 funds following conversion to Chapter 7.
- *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010) — Addresses confirmed plan provisions and student loan discharge.
- *Mort Ranta v. Gorman*, 721 F.3d 241 (4th Cir. 2013) — Addresses Social Security income and Chapter 13 confirmation.
- *Johnson v. Zimmer*, 686 F.3d 224 (4th Cir. 2012) — Addresses household size and the economic-unit approach.

Calculating Chapter 13 Plan Payments in Maryland: Disposable Income, Means-Test Deductions, and the Liquidation Test

Belsky Bankruptcy Legal Library | Chapter 13 Repayment Plans

By Alan J. Belsky, Attorney at Law

How Much Will You Have to Pay Each Month in Chapter 13?

One of the first questions a prospective Chapter 13 debtor asks is how much the monthly payment will be.

The answer is not simply the amount remaining after subtracting household expenses from take-home pay.

Chapter 13 payments are determined through several interacting requirements of the Bankruptcy Code. These include projected disposable income, the value of nonexempt property, the treatment of secured debts, priority claims, and the administrative costs of the plan.

A debtor may have relatively little disposable income but still be required to make substantial payments because of mortgage arrears, priority taxes, or valuable nonexempt property.

Conversely, a debtor with substantial unsecured debt may be able to confirm a plan that pays general unsecured creditors only a small percentage of their claims.

The purpose of the calculation is to determine the payment required by law and whether the debtor can realistically afford it.

A successful Chapter 13 plan must satisfy both requirements.

1. There Is No Universal Chapter 13 Payment Percentage

Chapter 13 does not require every debtor to repay a fixed percentage of unsecured debt.

A debtor may propose a plan paying 100% of qualifying unsecured claims.

Another debtor may propose a plan paying substantially less.

In some circumstances, general unsecured creditors may receive no distribution.

The result depends on the debtor's financial circumstances and the applicable confirmation requirements.

The percentage paid is ordinarily a consequence of the required plan funding rather than an independently selected target.

2. The Four Principal Components of a Plan Payment

A practical Chapter 13 calculation generally requires consideration of four matters:

- The amount needed to pay secured obligations treated through the plan.
- The amount needed to pay priority claims.

- The amount required for general unsecured creditors under the disposable-income and liquidation tests.
- Trustee compensation and other allowable administrative expenses.

These components interact.

They should not automatically be added together without considering how particular payments satisfy multiple statutory requirements.

For example, payments toward qualifying secured debts may affect the calculation of disposable income.

The plan must be modeled as a whole.

3. Schedule I and Schedule J

Schedule I reports the debtor's current income.

Schedule J reports current household expenses.

Together, they provide a picture of the debtor's actual monthly cash flow.

For example, a debtor may report $6,500 in monthly take-home income and $5,700 in ordinary expenses.

The apparent monthly surplus is $800.

But that figure does not necessarily establish the legally required Chapter 13 payment.

The means test, secured obligations, priority claims, and liquidation value may produce a different result.

4. Current Monthly Income

Section 101(10A) defines current monthly income.

The calculation generally uses income received during the six full calendar months preceding the bankruptcy filing, subject to statutory requirements.

The resulting monthly average may differ from the debtor's current earnings.

For example, a debtor may have earned substantial overtime during the lookback period but no longer receive overtime.

The means-test calculation may initially reflect the higher historical income.

The debtor's current circumstances may require separate consideration under applicable law.

5. Household Size

Household size affects the applicable median-income threshold and certain expense allowances.

The Fourth Circuit addressed household size in *Johnson v. Zimmer*, 686 F.3d 224 (4th Cir. 2012).

The court adopted an economic-unit approach that considers the financial relationship among household members.

A debtor may live with adult children, parents, or other relatives.

The appropriate household size depends on the circumstances rather than simply counting everyone residing at the address.

Household contributions and shared expenses may also matter.

6. Above-Median and Below-Median Debtors

The debtor's current monthly income is compared with the applicable median income for a household of the relevant size.

The median figures are periodically updated.

A below-median debtor generally has a three-year applicable commitment period, subject to statutory qualifications.

An above-median debtor generally has a five-year period.

The classification also affects how certain reasonably necessary expenses are determined.

The debtor should use the median-income figures applicable to the filing date.

7. Below-Median Debtors

For below-median debtors, actual reasonably necessary expenses generally play a significant role in determining disposable income.

The debtor must provide a realistic budget.

Expenses should reflect the debtor's household circumstances and statutory requirements.

The court may scrutinize expenses that appear excessive or unsupported.

A below-median debtor should not assume that every claimed expense will automatically be accepted.

8. Above-Median Debtors

For above-median debtors, § 1325(b)(3) generally incorporates expense calculations under § 707(b)(2).

These provisions use specified standards and deductions.

Some expenses are based on IRS standards.

Others may depend on actual qualifying costs.

The resulting calculation may differ substantially from Schedule J.

A debtor should not assume that every actual expense is deductible in the amount paid.

9. IRS National and Local Standards

The means test incorporates specified expense standards concerning categories such as food, clothing, housing, utilities, and transportation.

The applicable amounts depend on the statutory rules, household size, and location.

Some deductions are standardized.

Others involve actual expenses or additional statutory conditions.

The debtor should use the figures effective for the relevant filing period.

10. Housing Expenses

Housing deductions may include applicable allowances for mortgage or rent expenses and utilities.

The treatment depends on the debtor's circumstances and the means-test provisions.

A debtor who owns a home with substantial mortgage payments may receive different deductions from a renter.

However, the debtor should not assume that every mortgage payment automatically reduces the required payment dollar for dollar.

The interaction between secured debt deductions and plan treatment must be examined.

11. Automobile Ownership and Operating Expenses

The means test distinguishes certain vehicle ownership and operating expenses.

In *Ransom v. FIA Card Services, N.A.*, 562 U.S. 61 (2011), the Supreme Court held that a debtor who did not have a loan or lease payment could not claim the vehicle ownership deduction under the statutory framework considered.

The decision illustrates that standardized deductions are subject to eligibility requirements.

A debtor who owns a vehicle free and clear may receive different treatment from one making loan payments.

The debtor should also distinguish vehicle operating costs from ownership costs.

12. Medical Expenses

Qualifying medical expenses may affect the means test and actual household budget.

A debtor may have substantial prescription costs, insurance premiums, ongoing treatment expenses, or other health-related obligations.

The statutory deductions and applicable documentation requirements must be examined.

The debtor should not assume that every medical bill qualifies as a current monthly expense.

Past unsecured medical debt is different from ongoing necessary medical spending.

13. Taxes and Payroll Deductions

Income taxes, Social Security taxes, Medicare taxes, and other qualifying payroll deductions may affect the debtor's available income.

The means test provides for specified deductions.

The debtor should distinguish mandatory deductions from voluntary expenditures.

For example, voluntary retirement contributions may present different issues from required payroll taxes.

The legal treatment depends on the statutory provisions and applicable precedent.

14. Retirement Contributions

Retirement contributions can create complicated Chapter 13 questions.

Section 541(b)(7) addresses certain amounts withheld or contributed to qualifying retirement plans.

Courts have considered how these provisions interact with projected disposable income.

The treatment of ongoing voluntary contributions may depend on the circumstances and controlling law.

A debtor should not assume that every proposed contribution automatically reduces the amount payable to unsecured creditors.

15. Retirement Plan Loans

Qualifying retirement plan loan repayments receive special treatment under § 1322(f).

The statute provides that specified amounts required to repay qualifying retirement plan loans do not constitute disposable income under § 1325.

The debtor should identify the plan, loan terms, repayment schedule, and statutory qualification.

The treatment differs from an ordinary unsecured personal loan.

16. Social Security Income

Section 101(10A) excludes benefits received under the Social Security Act from current monthly income.

The Fourth Circuit addressed this issue in *Mort Ranta v. Gorman*, 721 F.3d 241 (4th Cir. 2013).

The exclusion can materially affect projected disposable income.

However, Social Security benefits generally must still be disclosed on the appropriate bankruptcy schedules.

The debtor should distinguish statutory current monthly income from actual household cash flow.

17. Projected Disposable Income

Section 1325(b)(1)(B) generally requires commitment of projected disposable income during the applicable commitment period when the trustee or an unsecured creditor objects to confirmation and the plan does not pay unsecured claims in full.

The Supreme Court addressed the calculation in *Hamilton v. Lanning*, 560 U.S. 505 (2010).

The Court approved a forward-looking approach permitting consideration of changes in income or expenses that are known or virtually certain at confirmation.

This is important when the historical six-month average does not accurately reflect the debtor's expected financial circumstances.

18. The Liquidation Test

Section 1325(a)(4) generally requires unsecured creditors to receive at least as much under the Chapter 13 plan as they would receive in a hypothetical Chapter 7 liquidation.

This is often called the best-interests-of-creditors test.

The calculation generally examines nonexempt property value, liens, hypothetical liquidation costs, and other relevant factors.

A debtor with valuable nonexempt assets may need to pay substantial amounts to unsecured creditors even when disposable income is limited.

19. Example: Nonexempt Home Equity

Assume a debtor owns a residence with $80,000 in nonexempt equity after accounting for valid liens and available exemptions.

The hypothetical Chapter 7 liquidation analysis may require adjustments for costs of sale, trustee compensation, and other applicable expenses.

Suppose the resulting amount available for general unsecured creditors is $60,000.

The Chapter 13 plan generally must provide at least that required liquidation value to unsecured creditors.

Over sixty months, $60,000 represents an average of $1,000 per month before considering other plan costs and timing.

The debtor's ability to retain the home depends on funding a feasible plan.

20. Priority Taxes

Certain tax obligations receive priority under § 507(a)(8).

Chapter 13 generally requires specified treatment of priority claims under § 1322(a)(2).

For example, a debtor may owe $24,000 in qualifying priority income taxes.

The plan may need to provide for payment of that amount, subject to the applicable statutory provisions and creditor agreement.

The debtor should identify priority and nonpriority taxes separately.

A tax claim's age and classification can materially affect the required payment.

21. Domestic Support Obligations

Qualifying domestic support obligations receive priority treatment.

Chapter 13 imposes requirements concerning payment of domestic support obligations and compliance with ongoing obligations.

The debtor should identify arrears and current support.

Failure to remain current on qualifying postpetition support obligations can create confirmation and discharge problems.

The plan must account for applicable statutory requirements.

22. Mortgage Arrears

Chapter 13 may permit curing qualifying mortgage arrears while maintaining ongoing payments.

The arrears may be paid through the trustee.

For example, $30,000 in arrears over sixty months represents $500 per month before trustee compensation and other applicable costs.

The debtor must also afford ongoing mortgage payments.

A plan that cures arrears but leaves insufficient money for current housing expenses is not feasible.

23. Vehicle Loans

A Chapter 13 plan may provide for payment of secured vehicle claims.

The treatment depends on the loan, collateral value, acquisition date, and applicable statutory provisions.

Some claims may be modified.

Others may be subject to the 910-day restriction.

The plan must provide the treatment required by § 1325(a)(5).

24. Trustee Compensation

Chapter 13 trustees receive compensation under applicable federal law.

The percentage charged can vary.

The debtor should use the applicable trustee percentage when modeling plan funding.

For example, a plan requiring $50,000 in creditor distributions may need additional funding to cover trustee compensation.

The trustee's percentage should not be guessed.

The actual rate and treatment of payments must be confirmed under applicable procedures.

25. Attorney's Fees

Chapter 13 attorney's fees may be paid partly before filing and partly through the plan, subject to applicable court procedures and approval requirements.

Fees paid through the plan affect required funding.

The debtor should understand the fee arrangement.

The attorney should distinguish fees already paid from amounts remaining to be paid through the trustee.

26. Example: Calculating a Plan Payment

Assume a debtor proposes a sixty-month plan with the following required distributions:

Plan component	Amount
Mortgage arrears	$30,000
Priority taxes	$18,000
Vehicle secured claim	$15,000
Required unsecured distribution	$12,000
Attorney's fees through plan	$5,000
Total before trustee compensation	$80,000

The average monthly funding requirement before trustee compensation is:

$80,000 ÷ 60 = $1,333.33.

The actual payment must also account for trustee compensation, applicable interest on secured claims, distribution timing, and other plan requirements.

This example illustrates the arithmetic, not a universally applicable payment formula.

27. Disposable Income May Require a Higher Payment

A debtor may calculate the minimum required distributions and discover that projected disposable income requires greater payments to unsecured creditors.

For example, a plan may satisfy the liquidation test with $12,000 for unsecured creditors.

But the debtor may have projected disposable income requiring $30,000 in distributions over the applicable commitment period.

The plan generally must satisfy the applicable disposable-income requirement.

The debtor cannot simply select the lower figure.

28. Liquidation Value May Require a Higher Payment

The reverse can also occur.

A debtor may have limited projected disposable income but substantial nonexempt property.

The liquidation test may require greater distributions than the disposable-income calculation alone would produce.

For example, a debtor may have only $400 in monthly projected disposable income but possess $50,000 in nonexempt equity.

The debtor may need to fund the required liquidation value to retain the property.

The plan must satisfy both applicable tests.

29. The Feasibility Requirement

Section 1325(a)(6) requires a finding that the debtor will be able to make all payments under the plan and comply with it.

A mathematically sufficient plan is not necessarily feasible.

The debtor must have enough income to fund the proposed payments while meeting reasonable living expenses.

A plan based on speculative overtime, uncertain business profits, or unrealistic expense reductions may fail.

The debtor should account for foreseeable irregular expenses.

30. Why Plan Payments May Change

A confirmed Chapter 13 plan may be modified under § 1329 in specified circumstances.

Changes in income, expenses, secured claims, or other relevant conditions may affect the payment.

For example, a debtor may lose employment or experience a substantial reduction in income.

Alternatively, income may increase.

The debtor should promptly report material changes and seek appropriate relief when necessary.

31. The Difference Between Minimum Funding and Affordable Funding

The minimum amount required by the Bankruptcy Code may exceed what the debtor can realistically afford.

That creates a feasibility problem.

A debtor may need to consider surrendering collateral, reducing expenses, increasing reliable income, or selecting another bankruptcy chapter.

The law does not guarantee that every debtor can retain every asset through Chapter 13.

A successful plan must be both legally sufficient and financially sustainable.

Conclusion

Calculating a Chapter 13 payment requires more than subtracting expenses from income.

The plan must satisfy applicable projected disposable-income requirements, the liquidation test, secured claim treatment, priority debt requirements, and administrative expenses.

The means test may differ substantially from the debtor's actual budget.

A debtor with substantial nonexempt assets may need to make significant payments even when disposable income is limited.

Conversely, a debtor with little nonexempt property and limited disposable income may pay only a small portion of ordinary unsecured debt.

The correct Chapter 13 payment is the amount required to satisfy the Bankruptcy Code through a plan the debtor can realistically complete—not simply the lowest payment that can be proposed.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 101(10A) — Current monthly income.
- 11 U.S.C. § 1322 — Chapter 13 plan provisions.
- 11 U.S.C. § 1325 — Confirmation requirements.
- 11 U.S.C. § 1326 — Payments.
- 11 U.S.C. § 1329 — Modification.
- 11 U.S.C. § 507 — Priority claims.
- 11 U.S.C. § 707(b)(2) — Means-test expense provisions.

Selected decisions

- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Addresses projected disposable income and known or virtually certain changes.
- *Ransom v. FIA Card Services, N.A.*, 562 U.S. 61 (2011) — Addresses vehicle ownership expense deductions.
- *Mort Ranta v. Gorman*, 721 F.3d 241 (4th Cir. 2013) — Addresses Social Security income exclusion.
- *Johnson v. Zimmer*, 686 F.3d 224 (4th Cir. 2012) — Addresses household size.
- *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004) — Addresses present-value interest for secured claims.
- *In re Quigley*, 673 F.3d 269 (4th Cir. 2012) — Addresses projected disposable income and expenses associated with surrendered collateral.

IRS Expense Standards in Chapter 7 and Chapter 13: Why Debtors May Deduct More Than They Actually Spend

Belsky Bankruptcy Legal Library | Means Testing and Disposable Income

By Alan J. Belsky, Attorney at Law

The Means Test Does Not Always Use What the Debtor Actually Spends

One of the more counterintuitive features of consumer bankruptcy law is that a debtor may sometimes deduct more for living expenses than the debtor actually spends.

The Bankruptcy Code incorporates expense standards developed by the Internal Revenue Service. These standards are used in determining whether a presumption of abuse arises in Chapter 7 and in calculating disposable income for certain Chapter 13 debtors.

But the means test is not simply a household budget.

The distinction is especially important for individuals who live economically, share housing expenses, drive older vehicles, or otherwise spend less than the applicable standardized allowances.

In the Fourth Circuit, *Lynch v. Jackson*, 853 F.3d 116 (4th Cir. 2017), provides important guidance concerning the use of IRS expense standards.

However, the debtor must distinguish between expenses determined under statutory standards and expenses that depend on actual amounts paid.

The debtor must also distinguish the mechanical means test from Schedule J, which reports actual or reasonably anticipated household expenses.

1. Why Bankruptcy Uses IRS Standards

Congress incorporated specified IRS expense standards into the Bankruptcy Code through the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005.

Section 707(b)(2)(A)(ii)(I) addresses certain expense deductions in the Chapter 7 means test.

Section 1325(b)(3) generally incorporates the same expense framework for above-median-income Chapter 13 debtors.

The purpose is to create a standardized method for calculating specified living expenses rather than relying exclusively on each debtor's reported spending.

The statutory approach can produce deductions greater or smaller than actual expenditures.

2. IRS National Standards

IRS National Standards generally address categories such as food, clothing, and certain miscellaneous expenses.

The applicable amounts depend on household size and other relevant factors.

For qualifying categories, the debtor generally may use the standardized allowance even when actual spending is lower.

Example

Assume the applicable National Standard is $1,150 per month.

The debtor actually spends $800.

The debtor generally may claim the $1,150 standardized amount on the means test when the deduction applies.

The debtor does not need to increase spending to qualify.

3. IRS Local Standards

IRS Local Standards generally concern housing, utilities, and transportation.

The applicable figures may vary by geographic area and household circumstances.

The Bankruptcy Code refers to applicable monthly expense amounts specified under the National and Local Standards.

However, not every category operates identically.

The debtor must qualify for the particular deduction.

Vehicle ownership expenses present an important example.

4. The Fourth Circuit's Decision in *Lynch v. Jackson*

In *Lynch v. Jackson*, 853 F.3d 116 (4th Cir. 2017), the Fourth Circuit addressed the use of IRS standardized expense allowances in bankruptcy.

The court recognized the distinction between applicable standardized amounts and actual expenses.

The decision supports the principle that a qualifying debtor may claim the applicable standardized deduction even when actual expenditures are lower.

Lynch permits the full applicable National or Local Standard when the debtor incurs the category of expense, even if the actual amount is lower. It does not authorize an allowance for an inapplicable category; Ransom’s requirement of a qualifying loan or lease expense for the vehicle ownership allowance remains controlling.

This principle is important for Maryland debtors because federal bankruptcy courts in Maryland are bound by Fourth Circuit precedent.

A debtor should not assume that economical living automatically reduces the statutory means-test allowance.

5. Why IRS Collection Rules Are Different

The IRS uses expense standards when evaluating a taxpayer's ability to pay delinquent taxes.

In that context, the IRS may apply rules limiting certain allowances to the lesser of actual expenses or the applicable standard.

Bankruptcy law incorporates the standards through its own statutory language.

The IRS's administrative collection procedures do not automatically govern bankruptcy means testing.

The distinction was central to litigation concerning the meaning of standardized deductions.

A debtor should not assume that every instruction in the IRS Financial Analysis Handbook applies to bankruptcy.

6. Vehicle Ownership Expenses: The *Ransom* Limitation

In *Ransom v. FIA Card Services, N.A.*, 562 U.S. 61 (2011), the Supreme Court held that a debtor who owned a vehicle free and clear could not claim the vehicle ownership deduction under the statutory framework considered.

The debtor did not have a qualifying loan or lease payment.

The Court distinguished between an applicable expense category and a deduction for an expense the debtor would not incur.

Thus, a debtor who owns a vehicle without a loan or lease generally cannot claim the ownership allowance merely because the IRS publishes one.

7. Vehicle Operating Expenses

Vehicle operating expenses are different from ownership expenses.

A debtor who owns a vehicle may incur gasoline, maintenance, registration, and other operating costs even without a loan payment.

When the debtor qualifies for the applicable operating allowance, the standardized amount generally may be used despite lower actual expenditures.

The debtor must accurately identify the vehicles and circumstances relevant to the deduction.

The operating allowance should not be confused with the ownership allowance.

8. Housing and Utilities

Housing and utility deductions may include standardized allowances for specified categories.

A debtor may spend less than the applicable standard.

However, the treatment of mortgage payments and other secured obligations requires attention to the means-test calculation and applicable form instructions.

The debtor should not simply claim the full housing standard and separately deduct every mortgage payment without considering the statutory adjustments.

The correct calculation must avoid impermissible duplication.

9. Actual Expenses Under the Means Test

Not every expense is determined through a standardized allowance.

Section 707(b)(2) provides for specified actual expenses and additional deductions.

Examples may include qualifying health insurance expenses, certain secured debt payments, priority claims, and other amounts satisfying statutory requirements.

The debtor must distinguish standardized categories from actual-expense categories.

A debtor cannot automatically substitute an IRS allowance for an expense that the statute requires to be established by actual payment or other qualifying criteria.

10. Chapter 7 Means Testing

Chapter 7 means testing generally applies to qualifying individual debtors whose debts are primarily consumer debts.

A debtor whose current monthly income exceeds the applicable median may need to complete Form 122A-2.

The form calculates deductions under the statutory framework.

A debtor may properly claim standardized allowances greater than actual expenditures.

The resulting calculation determines whether a presumption of abuse arises under § 707(b)(2).

However, the means test is not the only possible basis for dismissal.

11. Below-Median Chapter 7 Debtors

A below-median-income debtor generally does not complete the full expense-deduction calculation on Form 122A-2.

The statutory presumption of abuse ordinarily does not arise.

The debtor still must disclose actual income and expenses on Schedules I and J.

A below-median debtor should not use IRS standardized allowances to inflate Schedule J.

The distinction is important.

12. Schedule J Is Not the Means Test

Schedule J reports the debtor's actual or reasonably anticipated monthly expenses.

It is intended to provide a realistic picture of the debtor's household budget.

The debtor should not automatically insert IRS standardized allowances when actual expenses are lower.

For example, a debtor who pays $400 in rent should not report $1,800 merely because a housing standard permits that amount on the means test.

The Schedule J figure should reflect the debtor's actual or reasonably anticipated expense.

The standardized allowance belongs in the appropriate means-test calculation.

13. Example: Means Test Versus Schedule J

Assume a debtor has the following expenses:

Expense	Actual monthly expense	Applicable IRS standard
Food, clothing, miscellaneous	$850	$1,200
Housing and utilities	$1,300	$1,900
Vehicle operating expenses	$225	$375

On the means test, the debtor generally may claim the applicable standardized amounts when the statutory requirements are satisfied.

On Schedule J, the debtor should report the actual or reasonably anticipated expenses.

The two forms may therefore show different amounts without either being incorrect.

14. Why a Debtor May Pass the Means Test but Have a Surplus

A debtor may qualify under the means test because standardized allowances reduce calculated disposable income.

But Schedule I and Schedule J may show a substantial actual monthly surplus.

This is not necessarily a mathematical error.

The forms serve different purposes.

However, the difference may become important under § 707(b)(3).

A debtor should not assume that passing the means test eliminates every possible abuse objection.

15. Section 707(b)(3): Totality of Financial Circumstances

Section 707(b)(3) permits consideration of bad faith and the totality of the debtor's financial circumstances when the statutory presumption of abuse does not arise or is rebutted.

The United States Trustee may examine the debtor's actual financial ability to repay creditors.

For example, a debtor may properly claim standardized means-test deductions but have a substantial actual monthly surplus.

That surplus may be relevant to the totality-of-circumstances inquiry.

However, the trustee cannot simply rewrite the statutory means test by substituting actual expenses for authorized standardized deductions.

The separate statutory inquiries must be respected.

16. The Fourth Circuit's Decision in *Green v. Staples*

In *Green v. Staples (In re Green)*, 934 F.2d 568 (4th Cir. 1991), the Fourth Circuit addressed substantial abuse under the pre-2005 statutory framework.

The court identified factors relevant to evaluating the debtor's financial circumstances.

The decision predates the current § 707(b) provisions.

Nevertheless, it remains historically important to the Fourth Circuit's treatment of ability to pay and abuse.

The current statutory framework must be applied rather than assuming the pre-2005 standard controls unchanged.

17. Primarily Nonconsumer Debts

Section 707(b) generally applies to individual debtors whose debts are primarily consumer debts.

A debtor whose obligations are primarily nonconsumer debts ordinarily is not subject to the § 707(b) means-test presumption or its separate abuse provisions.

Business loans, commercial guarantees, and certain investment-related debts may be nonconsumer obligations.

The classification depends on the purpose of the debt.

The debtor must still satisfy other Bankruptcy Code requirements.

18. Chapter 13 Above-Median Debtors

Section 1325(b)(3) generally requires above-median Chapter 13 debtors to calculate reasonably necessary expenses under § 707(b)(2).

The standardized allowances therefore can affect projected disposable income.

A debtor who spends less than the applicable IRS standard may nevertheless claim the qualifying standardized amount.

The result may reduce the amount required for general unsecured creditors.

However, the debtor must also satisfy feasibility, good faith, and other confirmation requirements.

19. Chapter 13 Below-Median Debtors

Below-median Chapter 13 debtors generally do not use the same standardized expense framework to determine reasonably necessary expenses under § 1325(b)(3).

Actual reasonable and necessary expenses are particularly important.

The debtor should provide an accurate household budget.

The court may examine whether expenses are reasonable under the circumstances.

A below-median debtor should not assume that every IRS standardized allowance automatically controls plan payments.

20. The Effect of *Hamilton v. Lanning*

In *Hamilton v. Lanning*, 560 U.S. 505 (2010), the Supreme Court addressed projected disposable income in Chapter 13.

The Court approved consideration of changes in income or expenses that are known or virtually certain at confirmation.

The decision recognizes that the mechanical calculation may not always reflect expected future financial circumstances.

However, *Lanning* does not authorize routine replacement of statutory standardized allowances with lower actual expenses merely because the debtor spends less.

The cases address related but distinct questions.

21. Feasibility in Chapter 13

Section 1325(a)(6) requires a finding that the debtor can make all payments under the plan.

A debtor may have a legally calculated disposable-income amount that differs from actual cash flow.

The proposed plan must nevertheless be financially feasible.

For example, a debtor may have substantial actual expenses exceeding standardized allowances.

The debtor may be unable to fund a plan payment calculated without considering the full financial circumstances.

The court must evaluate feasibility separately from the disposable-income test.

22. Good Faith

Section 1325(a)(3) requires that the plan be proposed in good faith and not by any means forbidden by law.

A debtor's use of a legally authorized standardized deduction does not automatically establish bad faith.

However, the debtor's overall conduct and circumstances may be relevant.

The court should distinguish lawful use of statutory allowances from inaccurate disclosures or manipulative conduct.

A debtor should not conceal actual financial circumstances merely because the means test permits standardized deductions.

23. Why Standardized Allowances Can Benefit Economical Debtors

The standardized system can benefit debtors who live below the published allowances.

A debtor who shares housing, purchases inexpensive food, or drives an economical vehicle may spend less than the applicable standards.

When the debtor qualifies for the statutory deduction, the means test generally permits use of the standardized amount.

The debtor should not be penalized within the mechanical calculation merely for spending less.

But the debtor must remain accurate in reporting actual expenses elsewhere.

24. Why the Distinction Matters in Practice

The difference between the means test and Schedule J can materially affect bankruptcy eligibility and Chapter 13 plan calculations.

An attorney who substitutes actual expenses for standardized allowances on Form 122A-2 may unnecessarily create a presumption of abuse.

Conversely, an attorney who copies IRS allowances into Schedule J may overstate actual household expenses.

Both errors can affect the case.

The correct approach is to apply the governing instructions to each form independently.

Conclusion

The Bankruptcy Code permits qualifying debtors to use applicable IRS National and Local Standard allowances in means-test calculations even when actual expenses are lower.

The Fourth Circuit's decision in *Lynch v. Jackson* is important to Maryland practice.

But the debtor must qualify for the deduction, and some categories depend on actual expenses.

Ransom limits vehicle ownership deductions when no qualifying loan or lease expense exists.

Schedule J remains a separate disclosure of actual or reasonably anticipated household expenses.

In Chapter 7, substantial actual disposable income may raise issues under § 707(b)(3) even when the debtor passes the mechanical means test.

In Chapter 13, standardized deductions interact with projected disposable income, feasibility, and good faith.

The correct approach is neither to substitute actual expenses for every IRS allowance nor to use IRS allowances as though they were actual household expenditures. Each calculation must be performed for its own statutory purpose.

Related Bankruptcy Cases and Authorities

Federal statutes and forms

- 11 U.S.C. § 707(b)(2) — Chapter 7 means-test deductions.
- 11 U.S.C. § 707(b)(3) — Bad faith and totality-of-circumstances abuse.
- 11 U.S.C. § 1325(b) — Chapter 13 projected disposable income.
- Official Bankruptcy Forms — Forms 122A-2, 122C-2, and Schedule J.

Selected decisions

- *Lynch v. Jackson*, 853 F.3d 116 (4th Cir. 2017) — Addresses the use of IRS standardized expense allowances.
- *Ransom v. FIA Card Services, N.A.*, 562 U.S. 61 (2011) — Addresses the vehicle ownership deduction.
- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Addresses projected disposable income and known or virtually certain changes.
- *Green v. Staples (In re Green)*, 934 F.2d 568 (4th Cir. 1991) — Addresses substantial abuse under the former statutory framework.
- *In re Quigley*, 673 F.3d 269 (4th Cir. 2012) — Addresses deductions concerning collateral the debtor intends to surrender.

Chapter 13 Plan Confirmation in Maryland: Trustee Objections, Creditor Objections, Feasibility, Good Faith, and the Confirmation Hearing

Belsky Bankruptcy Legal Library | Chapter 13 Bankruptcy

By Alan J. Belsky, Attorney at Law

Filing Chapter 13 Does Not Mean the Repayment Plan Has Been Approved

A Chapter 13 debtor ordinarily files a proposed repayment plan shortly after commencing the bankruptcy case. But filing the plan does not mean that the bankruptcy court has approved it.

Before confirmation, the Chapter 13 trustee and creditors have opportunities to examine the debtor's financial circumstances, evaluate the proposed treatment of claims, and object to provisions that do not comply with the Bankruptcy Code.

The bankruptcy court must determine whether the plan satisfies the requirements of 11 U.S.C. §§ 1322 and 1325.

A plan may be rejected because it fails to provide sufficient payments to creditors, improperly treats a secured claim, does not account for priority debts, or depends on income the debtor is unlikely to receive.

Other objections concern good faith, the value of nonexempt property, or whether the debtor has accurately disclosed financial information.

Many objections are resolved through amendments and negotiations rather than a contested evidentiary hearing.

The debtor's objective is not simply to obtain confirmation. It is to obtain confirmation of a plan that can realistically be completed.

1. What Is Confirmation?

Confirmation is the bankruptcy court's approval of the proposed Chapter 13 plan.

Section 1325 establishes the principal confirmation requirements.

The court must determine that the plan complies with applicable provisions of the Bankruptcy Code and satisfies the statutory standards.

Once confirmed, the plan generally binds the debtor and creditors under § 1327(a), subject to applicable law.

Confirmation is therefore a significant legal event.

It establishes the framework governing payments and treatment of claims during the plan.

2. Filing the Proposed Plan

Under § 1321, the debtor must file a Chapter 13 plan.

Federal Rule of Bankruptcy Procedure 3015 generally requires filing within fourteen days after the petition unless the court grants an extension.

The District of Maryland has local requirements concerning the form and content of Chapter 13 plans.

The debtor should use the applicable local plan form and comply with current filing and service requirements.

Maryland Local Bankruptcy Rule 3015-1 requires a plan conforming to Local Bankruptcy Form M, signed by the debtor, and a certificate of service using Form M-1. Plan provisions seeking valuation or lien avoidance require the additional evidence and service specified in that rule; ordinary mailing of the plan does not replace the required service on the affected lienholder.

An incomplete or improperly prepared plan may produce objections or delay confirmation.

3. Plan Payments Begin Before Confirmation

A common misunderstanding is that payments do not begin until the bankruptcy court approves the plan.

Under § 1326(a)(1), the debtor generally must begin making required payments within thirty days after filing the plan or the order for relief, whichever is earlier, unless the court orders otherwise.

The debtor should not wait for confirmation.

Payments made before confirmation generally are held or distributed according to the applicable statutory provisions.

Failure to commence payments can jeopardize the case.

4. The Chapter 13 Trustee

The Chapter 13 trustee reviews the debtor's schedules, income, expenses, assets, debts, and proposed plan.

The trustee evaluates whether the plan satisfies applicable confirmation requirements.

The trustee may request additional documents or explanations.

The trustee also monitors payments and administers distributions under confirmed plans.

In Maryland, the standing Chapter 13 trustee's procedures and applicable local requirements should be reviewed.

The trustee's recommendation or objection can materially affect the confirmation process.

5. The Meeting of Creditors

Under § 341, the debtor ordinarily must attend a meeting of creditors.

The trustee may examine the debtor under oath concerning income, expenses, assets, debts, transfers, and the proposed repayment plan.

Creditors may also ask appropriate questions.

The meeting is not itself confirmation.

However, information obtained at the meeting may lead to objections or requests for amendments.

The debtor should provide accurate testimony and requested documentation.

6. Trustee Objections

The Chapter 13 trustee may object to confirmation for several reasons.

Common objections include insufficient projected disposable income, inaccurate expenses, inadequate treatment of priority claims, failure to satisfy the liquidation test, and lack of feasibility.

The trustee may also question the debtor's household size, income calculation, property valuations, or claimed exemptions.

An objection does not necessarily mean the case will be dismissed.

Many objections identify issues that can be corrected through additional evidence or plan amendments.

7. Creditor Objections

Creditors may object when they believe the proposed plan improperly affects their rights.

A mortgage lender may dispute the stated arrearage.

An automobile lender may challenge collateral valuation or interest.

An unsecured creditor may argue that the debtor has failed to commit required disposable income.

A creditor may also raise good-faith or other confirmation issues.

The objection must be evaluated under the applicable statutory provisions.

A creditor's dissatisfaction with the proposed repayment percentage does not automatically establish a valid objection.

8. The Good-Faith Requirement

Section 1325(a)(3) requires that the plan be proposed in good faith and not by any means forbidden by law.

Section 1325(a)(7) separately addresses whether the debtor filed the petition in good faith.

The inquiry is fact-specific.

Courts may consider the debtor's financial disclosures, conduct, proposed treatment of creditors, and overall circumstances.

A low repayment percentage does not automatically establish bad faith.

Nor does the debtor's lawful use of statutory exemptions or expense allowances necessarily establish misconduct.

9. Fourth Circuit Good-Faith Decisions

In *Deans v. O'Donnell*, 692 F.2d 968 (4th Cir. 1982), the Fourth Circuit addressed good faith in Chapter 13 confirmation and rejected a rigid minimum-payment requirement.

In *Neufeld v. Freeman*, 794 F.2d 149 (4th Cir. 1986), the court addressed the relevance of the debtor's prepetition conduct and the dischargeability of particular obligations.

These decisions remain important to the development of Chapter 13 good-faith analysis.

However, both predate substantial statutory amendments.

Their application must be considered alongside current §§ 1325(a)(3), 1325(a)(7), and 1325(b).

10. Feasibility

Section 1325(a)(6) requires the court to determine that the debtor will be able to make all payments under the plan and comply with it.

This is the feasibility requirement.

A debtor may propose a mathematically sufficient plan but lack the income necessary to fund it.

For example, a plan may require $1,600 monthly while the debtor's actual household budget leaves only $900 available.

Unless the discrepancy can be explained or corrected, the plan may not be feasible.

The court must consider whether the proposed payments are realistically sustainable.

11. Projected Disposable Income

Section 1325(b) becomes particularly important when the trustee or an allowed unsecured creditor objects to confirmation.

The debtor generally must satisfy the applicable projected disposable-income requirement unless unsecured claims are paid in full.

For above-median debtors, statutory expense standards may apply.

For below-median debtors, actual reasonably necessary expenses generally play a greater role.

The Supreme Court addressed projected disposable income in *Hamilton v. Lanning*, 560 U.S. 505 (2010).

The calculation may account for known or virtually certain changes in financial circumstances.

12. The Liquidation Test

Section 1325(a)(4) requires general unsecured creditors to receive at least the value they would receive in a hypothetical Chapter 7 liquidation.

This is the best-interests-of-creditors test.

The debtor's nonexempt property value may therefore affect the plan.

For example, a debtor may have substantial nonexempt equity in real estate.

Even if projected disposable income is modest, the plan may need to provide unsecured creditors with the required liquidation value.

The trustee may object when property is undervalued or exemptions are improperly claimed.

13. Property Valuation Disputes

The trustee or a creditor may challenge the debtor's valuation of real estate, vehicles, business interests, or other assets.

The valuation may affect secured claim treatment or the liquidation test.

Evidence may include appraisals, comparable sales, account statements, and other reliable information.

A debtor should not assign arbitrary values merely to make the proposed plan affordable.

The relevant valuation standard depends on the statutory issue.

14. Secured Claim Objections

A secured creditor may object to the proposed treatment of its claim.

The dispute may involve collateral value, interest, maturity, arrears, or other contractual rights.

Section 1325(a)(5) establishes requirements concerning allowed secured claims.

A plan may need amendment to satisfy the statute.

The debtor should distinguish disputes concerning claim amount from disputes concerning plan treatment.

15. Mortgage Arrearage Disputes

A mortgage lender may file a proof of claim identifying prepetition arrears.

The debtor may disagree with the amount.

The discrepancy may involve missed payments, escrow advances, fees, or other charges.

The debtor should review the proof of claim and supporting documents.

A plan that understates the required cure amount may not provide the relief the debtor expects.

Mortgage claim procedures under Rule 3002.1 may also become important during plan performance.

16. Automobile Loan Objections

Vehicle lenders may challenge proposed collateral values, interest rates, or treatment under the 910-day provision.

The debtor should determine whether the purchase-money restriction applies.

If modification is permitted, the plan must still satisfy applicable secured-claim requirements.

The Supreme Court's decisions in *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004), and *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997), provide important guidance concerning interest and valuation.

17. Priority Claim Objections

Certain debts receive priority under § 507.

The plan generally must provide required treatment for qualifying priority claims.

Examples include domestic support obligations and certain taxes.

The trustee may object if the plan fails to account for these obligations.

A debtor should determine whether the claim is actually entitled to priority rather than accepting the creditor's designation without review.

Confirmation also requires payment of domestic support obligations first becoming payable after the petition as specified in § 1325(a)(8), and filing of applicable tax returns under §§ 1308 and 1325(a)(9). These are independent conditions, not simply matters of including arrears in the payment calculation.

18. Attorney's Fees and Administrative Expenses

Chapter 13 attorney's fees and other administrative expenses may be paid through the plan, subject to applicable procedures.

The plan must provide sufficient funding.

The debtor should distinguish fees paid before filing from amounts remaining payable through the trustee.

The court may review professional compensation under applicable provisions.

Unaccounted administrative expenses can make a plan underfunded.

19. Objections Based on Household Expenses

A trustee may question expenses that appear excessive, inconsistent, or unsupported.

The applicable legal standard depends on whether the debtor is above or below median income and the particular expense category.

For above-median debtors, certain IRS standardized allowances may apply even when actual expenditures are lower.

The Fourth Circuit's decision in *Lynch v. Jackson*, 853 F.3d 116 (4th Cir. 2017), is important in this regard.

However, Schedule J must accurately report actual or reasonably anticipated expenses.

A debtor should not confuse the standardized means-test calculation with the household budget.

20. Amending the Plan

A debtor may amend a proposed Chapter 13 plan before confirmation, subject to applicable rules.

Amendments may address trustee objections, creditor claims, or changes in financial circumstances.

For example, the debtor may need to increase payments to satisfy the liquidation test or adjust treatment of a secured claim.

Amended plans may require notice and an opportunity for objection.

The debtor should not assume that a revised payment becomes effective without complying with the required procedures.

21. Negotiating Objections

Many confirmation objections can be resolved without contested evidentiary hearings.

Counsel may provide additional documentation, correct calculations, amend the plan, or negotiate claim treatment.

However, an agreement with one creditor does not necessarily resolve all statutory requirements.

The court must still determine whether confirmation is appropriate.

The debtor should understand any changes to the payment amount or plan obligations.

22. The Confirmation Hearing

The bankruptcy court considers whether the plan satisfies the applicable confirmation requirements.

Some cases may proceed through streamlined or uncontested procedures under local practice.

Contested matters may require argument or evidence.

The debtor may need to testify when factual disputes remain.

The court may confirm the plan, continue the matter, require amendments, or deny confirmation.

The applicable Maryland procedures should be reviewed before the hearing.

Under Maryland Local Bankruptcy Rule 3015-2, the debtor and counsel must attend scheduled confirmation hearings unless excused by the trustee or court. The rule sets confirmation hearings at least 35 days after filing the plan, ordinarily requires objections no later than seven days before the hearing, and requires the Form O pre-confirmation certificate within the seven days before the initial hearing and an updated certificate before a continued hearing. Read these provisions together with the actual notice and applicable federal timing rules.

23. What Happens If Confirmation Is Denied?

Denial of confirmation does not necessarily require immediate dismissal.

The debtor may be permitted to file an amended plan.

However, § 1307(c)(5) identifies denial of confirmation and denial of a request for additional time to file another plan as potential cause for dismissal or conversion.

Repeated inability to propose a confirmable plan can jeopardize the case.

The debtor should address objections promptly.

24. The Binding Effect of Confirmation

Section 1327(a) generally provides that the confirmed plan binds the debtor and creditors.

This can be significant when a creditor received proper notice but failed to object.

However, confirmation does not eliminate every independent statutory requirement.

The Supreme Court's decision in *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010), illustrates the importance of finality while recognizing procedural and statutory limitations.

The effect of confirmation depends on the plan language, notice, and governing law.

25. Confirmation Does Not Guarantee Completion

A confirmed plan may last three to five years.

The debtor must continue making required payments and complying with other obligations.

Job loss, illness, increased expenses, or other changes may threaten completion.

The debtor may seek modification under § 1329 when appropriate.

Confirmation is an important milestone, but successful completion requires continued performance.

26. Why Confirmation Preparation Begins Before Filing

The best opportunity to obtain confirmation often arises before the petition is filed.

Counsel should identify secured claims, priority debts, nonexempt property, actual expenses, and available income.

The debtor should understand the proposed payment and the obligations that must be maintained outside the plan.

A realistic initial plan may reduce objections, amendments, and delays.

The objective is to obtain a plan that satisfies the Bankruptcy Code and can be completed.

Conclusion

Chapter 13 confirmation is the process through which the bankruptcy court determines whether the debtor's proposed repayment plan complies with federal law.

The trustee and creditors may object concerning disposable income, feasibility, good faith, secured claims, priority obligations, or liquidation value.

Many objections can be resolved through documentation and amendments.

But a debtor cannot obtain confirmation merely by proposing a payment that appears affordable.

The plan must satisfy statutory requirements and provide a realistic path to completion.

A successful Chapter 13 case begins with a confirmable plan, but it ends only when the debtor fulfills the required obligations and receives a discharge.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 1321 — Filing the Chapter 13 plan.
- 11 U.S.C. § 1322 — Plan contents.
- 11 U.S.C. § 1325 — Confirmation requirements.
- 11 U.S.C. § 1326 — Payments.
- 11 U.S.C. § 1327 — Binding effect of confirmation.
- 11 U.S.C. § 1329 — Postconfirmation modification.
- Federal Rule of Bankruptcy Procedure 3015 — Chapter 13 plans.
- Federal Rule of Bankruptcy Procedure 3015.1 — Local Chapter 13 plan forms.

Selected decisions

- *Deans v. O'Donnell*, 692 F.2d 968 (4th Cir. 1982) — Addresses Chapter 13 good faith and rejects a rigid minimum-payment requirement.
- *Neufeld v. Freeman*, 794 F.2d 149 (4th Cir. 1986) — Addresses prepetition conduct and Chapter 13 good faith.
- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Addresses projected disposable income.
- *Lynch v. Jackson*, 853 F.3d 116 (4th Cir. 2017) — Addresses IRS standardized expense allowances.
- *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004) — Addresses interest rates on secured claims.
- *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997) — Addresses collateral valuation.
- *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010) — Addresses the binding effect of confirmed plans and procedural defects.

Maryland practice authorities

- United States Bankruptcy Court for the District of Maryland — Local Rules, Chapter 13 plan forms, and filing procedures.

Chapter 13 Plan Modifications in Maryland: Job Loss, Increased Expenses, Changes in Income, and When Payments Can Be Reduced

Belsky Bankruptcy Legal Library | Chapter 13 Bankruptcy

By Alan J. Belsky, Attorney at Law

A Confirmed Chapter 13 Plan Is Binding, but It Is Not Necessarily Unchangeable

A Chapter 13 repayment plan ordinarily lasts three to five years. During that period, a debtor may lose employment, experience a serious illness, retire, become responsible for additional household expenses, or encounter other financial changes that make the original payment difficult or impossible.

Financial circumstances may also improve. A debtor may receive a substantial salary increase, inheritance, settlement, or other unexpected funds.

Congress recognized that a repayment plan lasting several years may need to be adjusted.

Under 11 U.S.C. § 1329, a confirmed Chapter 13 plan may be modified in specified circumstances before completion of plan payments.

But modification is not automatic. The debtor must obtain appropriate approval, and the modified plan must satisfy applicable statutory requirements.

The availability of modification also does not mean that every debtor can reduce payments merely because the original plan has become inconvenient.

The central questions are whether the proposed modification is legally permissible, whether it remains feasible, and whether the debtor can still satisfy the obligations required for discharge.

1. What Is a Postconfirmation Modification?

A postconfirmation modification changes the terms of a Chapter 13 plan after the bankruptcy court has confirmed it.

Section 1329 authorizes specified modifications before completion of payments.

A modification may increase or reduce payments to a particular class, extend or reduce the payment period within statutory limits, or address other matters permitted by the statute.

The debtor must follow the applicable procedural requirements.

A private agreement between the debtor and a creditor does not necessarily modify the confirmed plan.

2. Who Can Request Modification?

Under § 1329(a), a modification may be requested by the debtor, trustee, or holder of an allowed unsecured claim.

The statute does not grant every secured creditor an unrestricted independent right to seek modification under § 1329(a).

However, secured creditors may possess other rights and remedies under the Bankruptcy Code.

The identity of the party requesting modification can matter.

3. Is a Substantial Change in Circumstances Required?

Section 1329 does not expressly state that every modification requires proof of a substantial change in financial circumstances.

Courts have considered the effect of confirmation, res judicata, and changed circumstances.

The Fourth Circuit addressed postconfirmation modification in *In re Arnold*, 869 F.2d 240 (4th Cir. 1989).

The decision recognizes the significance of substantial and unanticipated changes in the circumstances considered at confirmation.

In the Fourth Circuit, Arnold and Murphy v. O'Donnell (In re Murphy), 474 F.3d 143 (4th Cir. 2007), require a substantial and unanticipated change in financial circumstances before res judicata will yield to a payment-changing modification of the kind addressed in those cases. If that threshold is met, the court still applies § 1329 and the incorporated confirmation requirements. The statutory text should not be used to suggest that Maryland debtors can disregard that controlling framework. Trantham v. Tate, No. 22-2263 (4th Cir. Aug. 13, 2024), reiterates Murphy's modification principle even where property vested in the debtor at confirmation.

A debtor should not assume that any desired change will automatically be approved.

4. Job Loss

Loss of employment is a common reason for seeking modification.

A debtor may have been earning $6,000 per month when the plan was confirmed but later become unemployed.

The debtor may no longer be able to make the required payment.

The debtor should promptly notify counsel and provide documentation concerning the job loss, unemployment benefits, severance, and prospects for replacement income.

Possible responses may include temporary relief, a reduced payment, modification, conversion, or dismissal.

The appropriate remedy depends on the circumstances.

5. Reduction in Income

A debtor may remain employed but experience reduced hours, lower commissions, or decreased self-employment income.

The change may affect plan feasibility.

The debtor should provide current pay statements or business records.

A modification may be appropriate when the reduction is sufficiently supported and the modified plan satisfies statutory requirements.

The debtor should not simply stop making payments without seeking advice.

6. Increased Medical Expenses

A serious illness or injury may increase household expenses.

The debtor may face recurring prescription costs, treatment expenses, transportation costs, or other necessary expenditures.

These expenses may reduce funds available for plan payments.

The debtor should document the costs and determine whether insurance or other benefits will cover them.

A proposed modification should reflect reasonable anticipated expenses.

7. Retirement

A debtor may retire during the Chapter 13 plan.

The resulting change in income may affect payment capacity.

However, retirement does not automatically justify reducing payments.

The court may consider the debtor's circumstances, reasons for retirement, financial resources, and ability to continue funding the plan.

A debtor approaching retirement should consider the anticipated change before proposing the original plan whenever possible.

8. Disability and Loss of Earning Capacity

A debtor who becomes unable to work may have grounds to seek modification.

The debtor may receive disability benefits or other replacement income.

The nature and amount of those benefits matter.

Social Security benefits receive special treatment under the Bankruptcy Code.

The debtor should distinguish statutory disposable-income calculations from actual cash flow and plan feasibility.

9. Increased Household Expenses

A debtor may experience higher rent, insurance premiums, transportation costs, or other necessary expenses.

Not every ordinary increase justifies modification.

The debtor should demonstrate the actual change and its effect on the budget.

A proposed modification must still satisfy applicable statutory requirements.

The debtor should not assume that all discretionary spending increases can be shifted to unsecured creditors.

10. Changes in Household Composition

A debtor may marry, divorce, have a child, or become responsible for another household member.

These changes can affect income and expenses.

The debtor may need to provide updated household information.

The legal treatment depends on the particular change and applicable provisions.

A modification should reflect the debtor's actual financial circumstances.

11. Increased Income

Modification is not limited to debtors experiencing financial hardship.

A trustee or qualifying creditor may seek increased payments when the debtor's income rises substantially.

For example, a debtor may receive a significant promotion or begin earning substantial additional commissions.

The effect depends on the confirmed plan, applicable law, and circumstances.

The debtor should not assume that all postconfirmation income increases may be retained without regard to creditor rights.

12. Bonuses and Overtime

A debtor may receive irregular bonuses or overtime.

The treatment depends on the plan and applicable law.

Some plans contain provisions requiring turnover of specified additional income.

Other circumstances may prompt a modification request.

The debtor should review the confirmed plan and disclose material changes as required.

A bonus is not automatically exempt from every plan obligation merely because it was unexpected.

13. Inheritances

An inheritance received during Chapter 13 can create substantial issues.

Under § 1306, the Chapter 13 estate generally includes specified property acquired after filing and before the case is closed, dismissed, or converted.

In *Carroll v. Logan*, 735 F.3d 147 (4th Cir. 2013), the Fourth Circuit held that an inheritance received more than 180 days after filing became property of the Chapter 13 estate.

The trustee may seek modification or other appropriate relief.

The debtor should promptly disclose the inheritance.

14. Personal Injury Settlements

A debtor may receive a personal injury settlement during the plan.

The claim may constitute estate property depending on when it arose and applicable law.

Maryland exemptions may protect qualifying personal injury compensation.

However, the debtor should not assume that settlement proceeds may be spent without disclosure or approval.

The trustee may examine the claim, exemptions, and effect on the plan.

The debtor should coordinate bankruptcy and personal injury counsel.

15. Tax Refunds

Tax refunds may affect Chapter 13 plan obligations.

Some confirmed plans require turnover of refunds or specified portions.

The treatment depends on the plan, applicable law, and the nature of the refund.

A debtor should not assume that a refund received during Chapter 13 is automatically available for unrestricted spending.

The debtor should review the plan before using the funds.

16. Reducing Payments to Unsecured Creditors

A debtor may seek to reduce distributions to general unsecured creditors when financial circumstances deteriorate.

However, the modified plan must satisfy applicable statutory requirements.

The liquidation test and other confirmation provisions may limit the reduction.

For example, a debtor whose original plan was required to pay substantial nonexempt liquidation value may not be able to eliminate that requirement merely because income has fallen.

The modified plan must be evaluated as a whole.

17. Priority Claims

Priority claims receive special treatment.

A modification generally cannot disregard mandatory statutory treatment of qualifying priority debts.

For example, certain tax obligations and domestic support arrears may require payment according to applicable provisions.

A debtor seeking reduced payments must determine whether the remaining plan term can accommodate those obligations.

18. Secured Claims

Modification of secured claim treatment may present additional issues.

The creditor's lien rights, prior payments, collateral, and confirmed plan terms must be examined.

Section 1329 contains provisions concerning certain secured claim modifications.

The debtor should not assume that surrendering collateral or changing payment terms automatically eliminates every secured creditor deficiency.

The applicable statute and case law control.

19. Surrendering a Vehicle During the Plan

A debtor may no longer be able to afford a vehicle.

The debtor may wish to surrender it and reduce plan payments.

The consequences depend on the confirmed plan, loan documents, collateral value, and applicable law.

The creditor may assert a deficiency claim.

The ability to reclassify or modify treatment after confirmation has generated litigation.

The debtor should seek appropriate relief rather than simply surrendering the vehicle and reducing payments unilaterally.

20. Extending the Plan

Section 1329(c) limits the duration of a modified plan.

A modified plan generally may not extend payments beyond five years after the first payment was due under the original confirmed plan.

The debtor cannot ordinarily obtain an unlimited extension merely because payments were missed.

The remaining statutory period may therefore limit available modification options.

21. Shortening the Plan

A debtor may seek to complete the plan earlier.

However, the applicable commitment period and projected disposable-income requirements may affect early completion.

The debtor should not assume that paying the originally projected dollar amount early automatically entitles the debtor to discharge.

The plan and statutory requirements must be examined.

22. Paying the Plan in Full Early

A debtor may receive funds sufficient to pay remaining obligations.

The effect depends on whether the plan provides for full payment of allowed claims or only a percentage distribution.

A lump-sum payment may not necessarily satisfy all applicable requirements when unsecured creditors are not being paid in full.

The debtor should obtain approval of any required modification or payoff arrangement.

23. The Procedure for Modification

Federal Rule of Bankruptcy Procedure 3015(h) governs modification of a Chapter 13 plan after confirmation.

The proposed modification generally must be filed and served according to applicable requirements.

Parties receive an opportunity to object.

The bankruptcy court determines whether the modification satisfies the statute.

Maryland local rules and forms may impose additional procedures.

Maryland Local Bankruptcy Rule 3015-5 requires a motion accompanied by the proposed modified plan. The movant selects a hearing through the court's scheduler more than 33 but fewer than 60 days after service, and serves the required parties with a notice conforming to Form M-2. The scheduler supplies the objection date for the notice. The motion must also comply with Rule 3012-1 where valuation or lien relief is sought.

The debtor should not assume that an informal request to the trustee changes the plan.

24. Objections to Modification

The trustee or creditors may object to a proposed modification.

Issues may include feasibility, good faith, liquidation value, secured claim treatment, and compliance with statutory limits.

The debtor may need to provide updated income and expense documentation.

A contested modification may require a hearing.

The court must determine whether the modified plan satisfies applicable requirements.

25. What If Modification Is Impossible?

A debtor may be unable to fund any feasible modified plan.

For example, the debtor may have permanently lost income while substantial priority or secured obligations remain unpaid.

The debtor may need to consider conversion to Chapter 7, dismissal, or a hardship discharge when statutory requirements are satisfied.

The appropriate option depends on assets, debts, and eligibility.

Continuing an impossible plan may simply delay the inevitable.

26. Conversion to Chapter 7

Section 1307 generally permits a Chapter 13 debtor to convert to Chapter 7, subject to applicable law.

Conversion may eliminate the obligation to continue plan payments.

However, Chapter 7 may expose nonexempt property to liquidation.

The debtor should determine what property would enter the converted estate and what exemptions apply.

The Supreme Court's decision in *Harris v. Viegelahn*, 575 U.S. 510 (2015), addresses undistributed Chapter 13 funds following conversion.

27. Dismissal

Dismissal generally terminates the Chapter 13 case without providing the ordinary discharge.

Creditors may resume lawful collection.

The debtor may lose protection against foreclosure, repossession, and garnishment.

Payments made during the case may have reduced some obligations, but unpaid balances may remain.

The debtor should understand the consequences before voluntarily dismissing.

28. Hardship Discharge

Section 1328(b) permits a hardship discharge in limited circumstances.

The debtor generally must establish that failure to complete payments is due to circumstances for which the debtor should not justly be held accountable.

The value distributed to unsecured creditors must satisfy the statutory liquidation requirement.

Modification under § 1329 must be impracticable.

The hardship discharge is narrower than the ordinary Chapter 13 discharge.

It does not necessarily eliminate the same debts.

29. Why Prompt Action Matters

A debtor who cannot make payments should contact counsel promptly.

Missed payments may accumulate.

The trustee may file a motion to dismiss.

The debtor may have fewer options as the five-year limit approaches.

Early review may permit modification or another appropriate solution.

The debtor should not wait until several months of payments have been missed before seeking assistance.

Conclusion

A confirmed Chapter 13 plan may be modified when the statutory requirements are satisfied.

Changes in employment, income, medical expenses, household circumstances, and other financial events may justify reconsideration of plan terms.

Trustees and qualifying creditors may also seek increased payments when circumstances improve.

But modification is not automatic and does not eliminate mandatory treatment of secured or priority obligations.

The five-year limit and feasibility requirement can restrict available relief.

A debtor who experiences a material financial change during Chapter 13 should seek review promptly rather than simply stopping payments or assuming the original plan cannot be changed.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 1329 — Postconfirmation modification.
- 11 U.S.C. § 1325 — Confirmation requirements.
- 11 U.S.C. § 1306 — Chapter 13 estate property.
- 11 U.S.C. § 1307 — Conversion and dismissal.
- 11 U.S.C. § 1328(b) — Hardship discharge.
- Federal Rule of Bankruptcy Procedure 3015(h) — Postconfirmation modification procedures.

Selected decisions

- *In re Arnold*, 869 F.2d 240 (4th Cir. 1989) — Addresses modification and substantial changes in circumstances.
- *Carroll v. Logan*, 735 F.3d 147 (4th Cir. 2013) — Addresses postpetition inheritances in Chapter 13.
- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Addresses projected disposable income.
- *Harris v. Viegelahn*, 575 U.S. 510 (2015) — Addresses undistributed plan funds following conversion.
- *In re Murphy*, 474 F.3d 143 (4th Cir. 2007) — Addresses postconfirmation modification and changed circumstances.

Maryland practice authorities

- United States Bankruptcy Court for the District of Maryland — Local Rules and Chapter 13 procedures.

Stripping Second Mortgages and Other Junior Liens in Chapter 13: When an Underwater Lien Can Be Eliminated

Belsky Bankruptcy Legal Library | Chapter 13, Homeownership, and Secured Claims

By Alan J. Belsky, Attorney at Law

Chapter 13 May Permit Elimination of a Second Mortgage That Is Completely Unsecured

A homeowner may owe more on a first mortgage than the home is worth while also having a second mortgage or home equity line of credit.

In that situation, the junior lender may possess a recorded lien but have no economic collateral supporting its claim.

Chapter 13 may permit the debtor to treat a wholly unsecured junior mortgage as an unsecured claim and eliminate the lien upon satisfying the applicable statutory and procedural requirements.

This process is commonly called *lien stripping*.

But lien stripping is not available merely because the home has little equity.

The distinction between a wholly unsecured junior lien and a partially secured lien is critical.

A second mortgage supported by even some collateral value may receive substantially different treatment.

The debtor must also distinguish lien stripping from judicial lien avoidance under § 522(f), which involves a separate statutory remedy.

1. What Is a Junior Mortgage?

A junior mortgage is a lien subordinate to another mortgage or lien.

For example, a homeowner may have a first mortgage and a second mortgage.

The first mortgage ordinarily receives payment before the second mortgage from foreclosure proceeds, subject to applicable priority rules.

A home equity line of credit may also be secured by a junior deed of trust.

The lien's priority depends on Maryland recording law and other applicable provisions.

2. What Does It Mean for a Lien to Be Wholly Unsecured?

A junior mortgage is wholly unsecured when the value of the collateral is insufficient to support any portion of that lien after accounting for liens with superior priority.

Example

Assume a Maryland residence has the following values:

Item	Amount

Item	Amount
Fair market value	$300,000
First mortgage	$340,000
Second mortgage	$75,000

The first mortgage exceeds the property's value.

No collateral value remains to support the second mortgage.

Subject to applicable law, the second mortgage may be treated as wholly unsecured for Chapter 13 lien-stripping purposes.

3. What If the Second Mortgage Is Partially Secured?

Consider a different example:

Item	Amount
Fair market value	$350,000
First mortgage	$340,000
Second mortgage	$75,000

Here, $10,000 in collateral value remains after the first mortgage.

The second mortgage is at least partially secured.

When the lien is secured only by the debtor's principal residence, the anti-modification provision of § 1322(b)(2) may prevent stripping the lien.

The difference between no collateral value and some collateral value can determine the result.

4. Section 506(a) and Secured Claim Valuation

Section 506(a) generally determines the secured status of an allowed claim by reference to the value of the creditor's interest in collateral.

A creditor may have a valid lien under state law but possess no allowed secured claim for relevant Chapter 13 purposes when senior liens exhaust the property's value.

The debtor must establish the relevant valuation.

The valuation may be disputed.

The court may need to determine the property's value and lien priorities.

5. Section 1322(b)(2)

Section 1322(b)(2) permits modification of the rights of certain secured claim holders but generally protects claims secured only by a security interest in real property that is the debtor's principal residence.

This is commonly called the home mortgage anti-modification provision.

The provision protects qualifying mortgage creditors from certain modifications.

However, courts have distinguished wholly unsecured junior mortgages from partially secured home mortgages.

The statutory interaction with § 506(a) is central to lien stripping.

6. The Supreme Court's Decision in *Nobelman*

In *Nobelman v. American Savings Bank*, 508 U.S. 324 (1993), the Supreme Court addressed modification of a mortgage secured by the debtor's principal residence.

The Court held that § 1322(b)(2) protected the rights of a mortgage creditor whose claim was at least partially secured.

The decision limits the ability to reduce qualifying home mortgage rights merely because the collateral value is less than the loan balance.

However, *Nobelman* did not directly resolve every issue concerning a wholly unsecured junior mortgage.

Lower courts subsequently addressed that distinction.

7. Fourth Circuit Authority: Branigan v. Davis

In Branigan v. Davis (In re Davis), 716 F.3d 331 (4th Cir. 2013), the Fourth Circuit rejected a categorical bar to stripping wholly unsecured junior liens in Chapter 13 cases filed by debtors ineligible for another discharge following a recent Chapter 7 discharge. These are often called Chapter 20 cases. The absence of discharge eligibility under § 1328(f) does not itself prevent the relief. The debtor must still establish that the lien is wholly unsecured and satisfy good faith, confirmation, service, plan-performance, and order requirements.

The result should not be extended automatically to partially secured junior mortgages.

8. Property Valuation

The debtor must establish the property's value.

Evidence may include a qualified appraisal, comparable sales, property condition information, and other reliable valuation materials.

A tax assessment may provide background information but does not necessarily establish fair market value.

The lender may challenge the debtor's valuation.

A relatively small valuation difference can determine whether the junior mortgage is wholly unsecured.

The debtor should obtain credible evidence before seeking lien stripping.

9. Which Date Controls Valuation?

The relevant valuation date can be important.

Courts may examine the statutory context, confirmation requirements, and applicable precedent.

The debtor should not assume that the property's value at the time of a later hearing necessarily controls every dispute.

A significant increase or decrease in value during the case may complicate the analysis.

The applicable Maryland bankruptcy procedures and controlling law should be examined.

10. Mortgage Balances and Priority

The debtor must establish the balances and priority of senior liens.

A first mortgage payoff statement may be necessary.

Other liens, including tax liens or judgments, may affect the priority analysis.

The debtor should not assume that the recorded order alone resolves every lien priority question.

The governing documents and Maryland law control.

11. Home Equity Lines of Credit

A home equity line of credit may be secured by a junior deed of trust.

If senior liens exhaust the property's value, the HELOC may be wholly unsecured.

The debtor may seek appropriate Chapter 13 treatment.

However, the lender may dispute valuation, priority, or the nature of the collateral.

The account's revolving character does not automatically determine whether lien stripping is available.

12. What If the Junior Mortgage Secures Additional Collateral?

Section 1322(b)(2) protects specified claims secured only by a security interest in real property that is the debtor's principal residence.

A loan secured by additional collateral may present different issues.

The nature of the collateral and contractual rights must be examined.

A debtor should not assume that every loan described as a home mortgage receives identical anti-modification protection.

13. What If the Property Is Not the Principal Residence?

A mortgage secured by investment property or other nonprincipal-residence property may receive different treatment.

The anti-modification provision of § 1322(b)(2) is specifically directed to qualifying principal-residence security interests.

Chapter 13 may permit modification of certain claims secured by other real estate.

However, the debtor must satisfy the applicable secured claim and plan confirmation requirements.

14. Lien Stripping Versus Lien Avoidance

Lien stripping and lien avoidance are different remedies.

Lien stripping generally concerns the treatment of a wholly unsecured junior mortgage or other qualifying lien under Chapter 13.

Section 522(f) permits avoidance of certain judicial liens that impair exemptions.

For example, a judgment lien may be avoidable under § 522(f) even when the property has equity.

The statutory requirements and procedures differ.

The debtor should select the remedy appropriate to the lien's legal character.

15. Judgment Liens

A judgment lien generally arises through judicial process.

Section 522(f)(1)(A) may permit avoidance of a qualifying judicial lien to the extent it impairs an exemption.

The debtor must apply the statutory impairment formula.

Maryland's residential exemption may materially affect the result.

A judgment lien should not automatically be analyzed under the same rules as a consensual second mortgage.

16. Tax Liens

Federal and Maryland tax liens may arise by statute.

They generally are not judicial liens merely because they are enforceable through legal proceedings.

Section 522(f) ordinarily does not provide a general mechanism for avoiding statutory tax liens.

Chapter 13 may permit treatment of certain secured tax claims under applicable provisions.

However, the debtor should not assume that a tax lien can be stripped in the same manner as a wholly unsecured second mortgage.

17. How Is Lien Stripping Requested?

The debtor must follow the applicable bankruptcy procedural requirements.

Depending on the nature of the relief and current rules, the debtor may seek valuation and lien treatment through the plan or an appropriate motion or proceeding.

Federal Rule of Bankruptcy Procedure 3012 addresses determination of secured claim amounts.

Rule 7001 identifies matters requiring adversary proceedings, subject to applicable exceptions.

The debtor should comply with the District of Maryland's current local procedures.

Maryland Local Bankruptcy Rule 3012-1 governs a separate valuation or lien-avoidance motion, while Rule 3015-1 addresses relief requested through the plan. The required evidence includes collateral value, senior liens and debts, claimed exemptions, and nondebtor ownership information as applicable. Service must satisfy Rules 9014 and 7004; insured depository institutions can trigger Rule 7004(h)’s special certified-mail requirements and exceptions.

Proper notice to the lienholder is essential.

18. The Importance of Notice

A lienholder must receive legally sufficient notice of the proposed treatment and opportunity to object.

The plan should identify the creditor and proposed lien treatment with sufficient clarity.

A creditor may challenge valuation or the legal basis for stripping.

Failure to provide proper notice can undermine the enforceability of the resulting order.

The debtor should not assume that merely listing the second mortgage as unsecured automatically eliminates the lien.

19. Confirmation and Lien Stripping

Plan confirmation may establish the treatment of a wholly unsecured junior claim when the applicable requirements are satisfied.

However, the legal effect of confirmation must be distinguished from the ultimate elimination of the lien.

The debtor must satisfy the plan and the conditions specified in the valuation and lien-stripping order, ordinarily including successful completion. A new discharge is not a universal prerequisite in the Fourth Circuit, as Davis establishes.

The plan and order should clearly address when lien avoidance becomes effective.

20. What Happens If the Debtor Completes Chapter 13?

Upon successful plan completion and satisfaction of the applicable order’s conditions, a properly stripped wholly unsecured junior lien may become unenforceable. A discharge may be entered when the debtor is eligible, but Davis permits the qualifying lien relief even when another discharge is unavailable.

The debtor may need to take additional steps to clear the land records.

The exact procedure depends on the plan, order, and Maryland recording requirements.

21. What If the Case Is Dismissed?

Dismissal can materially affect lien stripping.

Section 349(b) generally addresses reinstatement of certain liens and other consequences of dismissal, subject to court order.

A debtor who fails to complete the Chapter 13 plan may lose the benefit of the proposed lien stripping.

The creditor's lien may remain enforceable.

The debtor should not assume that obtaining a valuation order permanently eliminates the lien regardless of whether the case succeeds.

22. What If the Case Converts to Chapter 7?

Conversion may affect the treatment of a junior lien.

Chapter 7 generally does not permit stripping a wholly underwater junior mortgage merely because the collateral lacks value.

In *Bank of America, N.A. v. Caulkett*, 575 U.S. 790 (2015), the Supreme Court rejected use of § 506(d) to void a wholly underwater junior mortgage in the Chapter 7 circumstances presented.

A debtor who converts before completing Chapter 13 should not assume that the proposed lien stripping survives.

The relevant orders and statutory provisions must be examined.

23. Completion, Discharge Eligibility, and the Lien-Stripping Order

Confirmation, valuation, successful completion, and entry of discharge are different events. The order must clearly identify when the lien relief becomes effective and what performance is required.

In a qualifying Chapter 20 case, Davis permits stripping the valueless junior lien without eligibility for a new discharge. This is distinct from discharging the borrower’s personal liability and does not excuse failure to complete the plan or satisfy the order.

The debtor should obtain the operative completion and lien orders rather than rely on an informal understanding that the second mortgage has disappeared.

24. Clearing the Maryland Land Records

A recorded deed of trust may continue appearing in Maryland land records even after the bankruptcy court has determined that the lien is unenforceable.

The debtor may need to obtain and record appropriate documentation.

Depending on the circumstances, this may involve a certified bankruptcy order, release, or other legally sufficient instrument.

The debtor should verify that title records accurately reflect the result before selling or refinancing.

An effective bankruptcy order and a clear public title record are related but distinct objectives.

25. Why Lien Stripping Can Make Chapter 13 Attractive

A homeowner may have a substantial second mortgage that is entirely unsupported by property value.

If the debtor qualifies for Chapter 13 and can complete a feasible plan, lien stripping may provide substantial long-term relief.

For example, eliminating a wholly unsecured $90,000 second mortgage can materially improve the homeowner's financial position.

But the benefit depends on valuation, lien priority, statutory requirements, and successful completion.

The debtor should evaluate the entire Chapter 13 plan rather than focusing exclusively on the potential lien reduction.

Conclusion

Chapter 13 may permit elimination of a wholly unsecured second mortgage or home equity lien when senior liens exhaust the property's value.

The distinction between a wholly unsecured and partially secured mortgage is critical.

Nobelman protects certain home mortgage rights, while Fourth Circuit authority recognizes lien stripping for qualifying wholly unsecured junior liens.

The debtor must establish property value, lien priority, and proper procedural treatment.

Successful plan completion and compliance with the lien-stripping order are essential. A new discharge is not a categorical requirement for a qualifying Fourth Circuit Chapter 20 case.

A homeowner with a second mortgage exceeding the property's remaining collateral value should determine whether Chapter 13 lien stripping is available before assuming that the junior mortgage must be paid in full.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 506(a) — Secured claim valuation.
- 11 U.S.C. § 522(f) — Judicial lien avoidance.
- 11 U.S.C. § 1322(b)(2) — Modification of secured claims and home mortgage protection.
- 11 U.S.C. § 1325 — Plan confirmation.
- 11 U.S.C. § 1328 — Chapter 13 discharge.
- 11 U.S.C. § 349(b) — Effect of dismissal.

- Federal Rule of Bankruptcy Procedure 3012 — Determination of secured claim amounts.
- Federal Rule of Bankruptcy Procedure 7001 — Adversary proceedings.

Selected decisions

- *Nobelman v. American Savings Bank*, 508 U.S. 324 (1993) — Addresses anti-modification protection for qualifying home mortgages.
- *In re Davis*, 716 F.3d 331 (4th Cir. 2013) — Addresses wholly unsecured junior mortgage liens in Chapter 13.
- *Bank of America, N.A. v. Caulkett*, 575 U.S. 790 (2015) — Addresses wholly underwater junior liens in Chapter 7.
- *Dewsnup v. Timm*, 502 U.S. 410 (1992) — Addresses § 506(d) lien stripdown in Chapter 7.
- *In re Bartee*, 212 F.3d 277 (5th Cir. 2000) — Addresses wholly unsecured junior mortgage liens in Chapter 13.
- *In re Pond*, 252 F.3d 122 (2d Cir. 2001) — Addresses Chapter 13 treatment of wholly unsecured junior home mortgages.

Maryland practice authorities

- United States Bankruptcy Court for the District of Maryland — Local Rules, Chapter 13 plan forms, and lien valuation procedures.
- Maryland Land Records — Recorded deeds of trust and lien documents.

Chapter 13 Mortgage Arrears and Foreclosure in Maryland: Curing Defaults, Maintaining Payments, and What Happens When the Debtor Falls Behind Again

Belsky Bankruptcy Legal Library | Chapter 13 Bankruptcy and Homeownership

By Alan J. Belsky, Attorney at Law

Chapter 13 Can Save a Home From Foreclosure, but the Debtor Must Make Two Different Kinds of Mortgage Payments

Chapter 13 bankruptcy can provide a homeowner with a means of stopping foreclosure and curing mortgage arrears over time.

The automatic stay ordinarily prevents a scheduled foreclosure sale from proceeding while the stay applies. Chapter 13 may then permit the debtor to repay missed mortgage payments through a court-approved plan.

But saving the home requires more than paying the arrears.

The debtor generally must also maintain the regular mortgage payments that become due after filing.

This distinction is fundamental.

A homeowner who makes every Chapter 13 trustee payment but fails to maintain ongoing mortgage payments may still face a motion for relief from the automatic stay and renewed foreclosure proceedings.

Conversely, a debtor who pays the regular mortgage but fails to fund the arrearage cure may be unable to complete the Chapter 13 plan.

A successful strategy must address both obligations and account for escrow changes, lender fees, payment adjustments, and other expenses arising during the plan.

1. The Automatic Stay and Foreclosure

Under 11 U.S.C. § 362(a), filing Chapter 13 ordinarily stays foreclosure activity against qualifying property.

The stay generally arises when the petition is filed.

However, repeat-filing limitations, prior stay-relief orders, and other statutory provisions may affect protection.

A homeowner should not assume that every bankruptcy filing automatically stops a scheduled sale.

The status of the foreclosure proceeding and the debtor's prior bankruptcy history must be examined.

2. Maryland Foreclosure Procedure

Maryland foreclosure proceedings involving deeds of trust ordinarily are conducted under judicial supervision.

The process may include notices of intent to foreclose, an order to docket, mediation rights in qualifying cases, advertisement, auction, and judicial ratification.

The timing of the bankruptcy petition matters.

A filing before the foreclosure auction may provide different options from a filing after the sale.

The debtor should not assume that filing before final ratification necessarily restores every cure right.

Maryland decisions ordinarily treat the completed lawful foreclosure auction as the § 1322(c)(1) cure cutoff, even though ratification follows later. In re Schweiger, 587 B.R. 469 (Bankr. D. Md. 2018), recognizes a distinction where state-court proceedings restore the equity of redemption. A post-auction petition should not be presented as a routine method of reinstating the mortgage.

3. Section 1322(b)(5)

Section 1322(b)(5) permits a Chapter 13 plan to cure defaults within a reasonable time while maintaining payments on qualifying long-term obligations.

This provision is central to mortgage arrearage cures.

The debtor may pay the arrears through the plan while continuing regular mortgage payments.

The cure does not necessarily require immediate payment of the entire past-due balance.

However, the plan must be feasible and satisfy applicable statutory requirements.

4. Example: Curing Mortgage Arrears

Assume a homeowner has the following obligations:

Item	Amount
Monthly mortgage payment	$2,100
Prepetition mortgage arrears	$30,000
Chapter 13 plan duration	60 months

The arrears alone require an average of $500 per month over sixty months, before trustee compensation and other applicable costs.

The debtor must also maintain the regular $2,100 monthly mortgage payment.

Thus, the household must be able to support both obligations.

A plan that provides for arrears but ignores the ongoing mortgage payment is not a realistic cure strategy.

5. Trustee Payments Versus Direct Mortgage Payments

Chapter 13 plans may provide for some mortgage-related payments through the trustee and others directly by the debtor.

The arrangement depends on the plan and applicable local procedures.

A common structure involves paying prepetition arrears through the trustee while the debtor pays ongoing mortgage installments directly.

However, other arrangements may apply.

The debtor must understand precisely which payments are made to the trustee and which must be paid to the lender.

Confusion can result in postpetition defaults.

6. When Must the First Mortgage Payment Be Made?

The debtor generally must continue paying mortgage installments that become due after filing according to the applicable plan and loan obligations.

The exact timing depends on the payment due date and plan structure.

The debtor should not assume that the bankruptcy filing creates a payment holiday.

The automatic stay restricts collection activity but does not eliminate the need to maintain the loan when the debtor intends to retain the home.

7. The Mortgage Proof of Claim

A mortgage lender generally files a proof of claim identifying the debt and prepetition arrears.

Federal Rule of Bankruptcy Procedure 3001(c)(2)(C) requires specified information for certain claims secured by the debtor's principal residence.

The claim may include an attachment showing the amount necessary to cure the default.

The debtor should review the filing carefully.

Errors may involve missed payments, escrow advances, fees, charges, or payment application.

The trustee's distribution calculations may depend on the allowed claim.

8. Disputing the Arrearage Amount

A debtor may disagree with the lender's calculation.

For example, the lender may claim $38,000 in arrears while the debtor believes the correct amount is $29,000.

The discrepancy may involve payments not credited, escrow adjustments, or disputed fees.

The debtor should obtain a payment history and supporting documents.

A claim objection or other appropriate proceeding may be necessary.

The debtor should not assume that the amount stated in the lender's proof of claim is automatically correct.

9. Escrow Shortages

Mortgage payments may include principal, interest, taxes, and insurance.

An escrow shortage can increase the required monthly payment.

A debtor who originally paid $1,800 may later receive notice that the payment has increased to $2,100.

The Chapter 13 budget must account for the change.

A debtor should not assume that the mortgage payment remains fixed throughout the plan.

10. Rule 3002.1 Payment Change Notices

Federal Rule of Bankruptcy Procedure 3002.1 establishes procedures concerning certain home mortgage claims in Chapter 13.

The rule generally requires notice of specified payment changes, including adjustments resulting from interest rates or escrow accounts.

The notice requirements depend on the claim and plan treatment.

The current rule applies when a Chapter 13 plan provides for the debtor or trustee to make payments on debt secured by the debtor’s principal residence, subject to the rule’s termination provisions. Ordinary payment-change notices must be filed and served at least 21 days before the changed payment is due. Special annual reconciliation rules govern qualifying home-equity lines of credit, including additional notices for changes exceeding $10. The December 1, 2025 amendments also specify consequences for untimely notices of increases and decreases.

The debtor and trustee should review the notices.

A payment change may require adjustment of the debtor's budget or payment arrangements.

11. Postpetition Fees and Charges

A mortgage lender may incur fees or expenses during the Chapter 13 case.

Examples may include certain inspection charges, attorney's fees, or other amounts asserted under the loan documents.

Rule 3002.1 provides procedures for notifying parties of specified postpetition fees, expenses, and charges.

The debtor may dispute improper amounts.

The lender's assertion of a fee does not automatically establish that it is recoverable.

Under Rule 3002.1(c), the holder must file and serve an itemized notice of covered postpetition fees, expenses, and charges within 180 days after incurring them. A party in interest ordinarily has one year after service to move for a determination under subdivision (e), unless the court

orders a shorter period on request. The notice itself does not receive Rule 3001(f)'s prima facie evidentiary effect.

12. Falling Behind After Filing

A debtor may make regular trustee payments but fall behind on postpetition mortgage installments.

The lender may seek relief from the automatic stay.

The debtor should not assume that curing prepetition arrears protects against new defaults.

The Chapter 13 plan ordinarily must be performed together with ongoing mortgage obligations.

Failure to maintain payments may jeopardize the home.

13. Motions for Relief From Stay

Under § 362(d), a mortgage lender may seek relief from the automatic stay for cause or other statutory grounds.

Postpetition payment defaults may provide a basis.

The debtor may oppose the motion.

The bankruptcy court may consider the payment history, equity, adequate protection, and other circumstances.

The court may grant relief, deny relief, or impose conditions.

14. Adequate Protection

Adequate protection concerns the secured creditor's interest in collateral.

A lender may argue that missed payments, inadequate insurance, or other circumstances threaten its position.

The debtor may present evidence concerning property value, equity, insurance, and payment arrangements.

The legal standard depends on the statutory grounds asserted.

The existence of equity may be relevant but does not necessarily excuse ongoing payment defaults.

15. Consent Orders

Some stay-relief disputes are resolved through consent orders.

A consent order may require the debtor to cure postpetition defaults and remain current.

It may also establish procedures for future defaults.

The debtor should understand the consequences before agreeing.

A consent order may permit expedited stay relief if specified conditions are violated.

The terms should be reviewed carefully.

16. What If the Debtor Cannot Catch Up?

A debtor who cannot cure new mortgage defaults may need to consider modification of the Chapter 13 plan, loan modification, sale, surrender, or other alternatives.

However, not every postpetition mortgage default can simply be added to the existing arrearage cure.

The legal treatment depends on the plan, loan, statutory provisions, and applicable law.

The debtor should seek advice before assuming that new arrears can automatically be spread over the remaining plan term.

17. Postpetition Mortgage Defaults and Plan Modification

Section 1329 permits specified postconfirmation modifications.

A debtor may seek to address changed circumstances through an amended plan.

However, the modification must satisfy statutory requirements.

The five-year maximum period can limit available options.

The debtor should not assume that a plan can be extended indefinitely to accommodate new mortgage arrears.

18. Loan Modification During Chapter 13

A lender may agree to modify the mortgage.

A modification may change the interest rate, maturity, payment amount, or treatment of arrears.

The debtor may need bankruptcy court approval or compliance with local procedures.

The modification may also affect the confirmed plan.

The debtor should coordinate the mortgage modification with bankruptcy counsel and the trustee.

19. The Effect of Mortgage Forbearance

A mortgage servicer may offer forbearance or temporary payment relief.

The terms may affect when payments resume and how deferred amounts are handled.

A debtor should not assume that forbearance eliminates the underlying obligation.

The agreement should be reviewed to determine whether payments are deferred, capitalized, or otherwise addressed.

The Chapter 13 plan may require adjustment.

20. What If the Debtor Sells the Home?

A debtor may decide to sell the residence during Chapter 13.

The sale may require bankruptcy court approval or compliance with applicable procedures.

The proceeds may be subject to liens, exemptions, and estate interests.

The debtor should not assume that all net proceeds can be retained without further analysis.

The effect on the Chapter 13 plan must be determined.

21. What If the Debtor Has Substantial Equity?

A debtor with substantial equity may have additional options, including refinancing or selling the property.

However, equity can also affect the Chapter 13 liquidation test.

The debtor may be required to provide unsecured creditors with at least the amount they would receive in a hypothetical Chapter 7 liquidation.

The debtor should evaluate equity, exemptions, liens, and transaction costs.

22. Completion of the Mortgage Cure

At the end of the plan, the debtor should determine whether the prepetition arrears have been fully cured.

Current Rule 3002.1(g), effective December 1, 2025, provides an end-of-case notice of trustee disbursements and procedures for determining cure and postpetition payment status. It supersedes reliance on the former final-cure-notice timetable.

These procedures are important because disputes may arise over alleged remaining arrears or postpetition charges.

The debtor should not assume that completion of trustee payments automatically resolves every mortgage accounting issue.

23. The End-of-Case Notice and Payment-Status Determination

Within 45 days after the debtor completes all payments due to the trustee under the plan, the trustee must file and serve the Rule 3002.1(g) notice using Form 410C13-N. It addresses disbursements to cure defaults and to pay amounts coming due during the case. The claim holder must respond within 28 days after service using Form 410C13-NR.

A debtor or trustee may seek a final cure and payment determination within 45 days after service of the response, or after service of the trustee's notice if no response is filed, using Form 410C13-M2. The holder's response is due within 28 days under the rule. The court determines the disputed cure and postpetition payment issues through the prescribed process.

Subdivision (f) also permits an interim motion to determine claim status before the trustee's end-of-case notice, using Form 410C13-M1; a disagreeing holder has 28 days to respond. These tools allow accounting problems to be addressed during the case, rather than waiting until completion.

24. What If the Mortgage Company Claims Additional Arrears?

A lender may contend that the debtor remains behind despite completion of plan payments.

The alleged balance may involve postpetition defaults, fees, escrow charges, or accounting errors.

The debtor should obtain the payment history and relevant notices.

A motion under Rule 3002.1 may be appropriate.

The court may determine whether the default has been cured and whether required payments are current.

25. The Effect of Discharge

A Chapter 13 discharge generally eliminates qualifying personal obligations remaining after successful plan completion.

However, a long-term mortgage ordinarily survives to the extent provided by the Bankruptcy Code and confirmed plan.

The debtor must continue making payments after discharge if the loan remains outstanding.

Chapter 13 ordinarily cures defaults rather than eliminating the entire mortgage.

26. What If the Case Is Dismissed Before Completion?

Dismissal generally terminates the bankruptcy protection without producing the ordinary Chapter 13 discharge.

The mortgage lender may resume lawful foreclosure activity.

The debtor may receive credit for payments made through the trustee.

However, unpaid arrears and other enforceable obligations may remain.

The debtor should obtain a current accounting before deciding how to proceed.

27. Why Mortgage Accounting Matters Throughout the Plan

Mortgage servicers may change, payments may be misapplied, and escrow requirements may fluctuate.

The debtor should preserve monthly statements and payment confirmations.

Counsel should review material notices and respond promptly to disputed charges.

A Chapter 13 plan can fail even when the debtor believes payments are current if the lender's accounting is not monitored.

The Rule 3002.1 process provides important protections, but it does not eliminate the need for accurate records.

Conclusion

Chapter 13 can provide a powerful mechanism for curing mortgage arrears and preventing foreclosure.

But the debtor generally must make both the arrearage payments required by the plan and the regular mortgage installments that become due after filing.

Escrow changes, postpetition fees, and new payment defaults can complicate the process.

Rule 3002.1 provides procedures for reporting payment changes, postpetition charges, and completion of the cure.

A successful Chapter 13 mortgage cure requires more than completing trustee payments. The debtor must also maintain ongoing mortgage obligations and ensure that the lender's accounting accurately reflects the payments made.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 362 — Automatic stay and relief from stay.
- 11 U.S.C. § 1322(b)(5) — Cure and maintenance of long-term obligations.
- 11 U.S.C. § 1322(c)(1) — Cure rights concerning principal residences.
- 11 U.S.C. § 1325 — Confirmation requirements.
- 11 U.S.C. § 1329 — Plan modification.
- Federal Rule of Bankruptcy Procedure 3002.1 — Home mortgage payment changes, fees, and final cure procedures.

Maryland law

- Maryland Real Property Article, Title 7 — Foreclosure and deeds of trust.
- Maryland Rules 14-201 through 14-218 — Foreclosure procedures.

Selected decisions

- *Hurlburt v. Black*, 925 F.3d 154 (4th Cir. 2019) (en banc) — Addresses treatment of certain home-secured claims under § 1322(c)(2).
- *Nobelman v. American Savings Bank*, 508 U.S. 324 (1993) — Addresses protection of qualifying home mortgage rights.
- *Johnson v. Home State Bank*, 501 U.S. 78 (1991) — Addresses surviving mortgage claims in Chapter 13.
- *In re Taddeo*, 685 F.2d 24 (2d Cir. 1982) — Addresses curing mortgage defaults in Chapter 13.
- *In re Heinzle*, 511 B.R. 69 (Bankr. W.D. Tex. 2014) — Discusses Rule 3002.1 mortgage accounting issues.
- *In re Gravel*, 6 F.4th 503 (2d Cir. 2021) — Addresses sanctions concerning mortgage servicing and Rule 3002.1.

Chapter 13 and Automobile Loans in Maryland: Cramdown, the 910-Day Rule, Interest Rates, Surrender, and What Happens When the Car Is Totaled

Belsky Bankruptcy Legal Library | Chapter 13 Bankruptcy and Secured Vehicle Debt

By Alan J. Belsky, Attorney at Law

Chapter 13 Can Change How a Vehicle Loan Is Paid, but Not Every Automobile Loan Can Be Reduced to the Vehicle's Value

A debtor who files Chapter 13 may need to retain an automobile to work, transport family members, or meet ordinary daily obligations.

But the debtor may owe substantially more than the vehicle is worth.

Chapter 13 can provide options unavailable in Chapter 7, including payment of certain secured vehicle claims through a repayment plan and, in appropriate circumstances, reduction of the secured claim to the vehicle's value.

That reduction is commonly called *cramdown*.

However, the Bankruptcy Code restricts cramdown for certain recently purchased vehicles.

The 910-day rule can require different treatment of qualifying purchase-money automobile loans.

Other issues arise when the vehicle is surrendered, repossessed, destroyed in an accident, or subject to insurance and GAP coverage.

The debtor must distinguish the amount owed, the value of the collateral, the creditor's security interest, and the statutory requirements governing plan treatment.

1. Automobile Loans Are Secured Debts

An automobile lender ordinarily holds a security interest in the financed vehicle.

The lien gives the creditor rights against the collateral when the borrower defaults.

In Chapter 13, the debtor may propose treatment of the secured claim through the repayment plan.

The creditor's rights depend on the loan agreement, lien validity, collateral value, and applicable bankruptcy provisions.

The debtor should not assume that filing bankruptcy automatically eliminates the lender's lien.

2. Section 1325(a)(5)

Section 1325(a)(5) establishes principal requirements for treatment of allowed secured claims.

The creditor may accept the plan.

Alternatively, the plan may provide treatment satisfying the statutory requirements, including retention of the lien and distribution of the required value.

The debtor may also surrender the collateral.

The appropriate treatment depends on the claim and the debtor's objectives.

3. What Is Cramdown?

Cramdown generally refers to modifying a secured claim based on the value of the collateral when the Bankruptcy Code permits that treatment.

Example

Assume a debtor owes $28,000 on a vehicle worth $15,000.

If cramdown is available, the plan may treat $15,000 as secured and the remaining $13,000 as unsecured.

The secured portion generally must receive the required present-value treatment.

The unsecured deficiency receives treatment with other unsecured claims.

However, the 910-day rule may prevent this treatment for certain recently acquired vehicles.

4. The 910-Day Rule

The hanging paragraph following § 1325(a)(9) restricts application of § 506 to certain purchase-money security interests in motor vehicles acquired for the debtor's personal use within 910 days before filing.

When the statutory requirements are satisfied, the debtor generally cannot reduce the qualifying claim to the vehicle's current value through ordinary cramdown.

The debtor should determine the purchase date, loan purpose, and nature of the security interest.

The restriction does not apply automatically to every automobile loan.

The statutory wording tests whether the qualifying debt was incurred within 910 days before the petition and whether the motor vehicle was acquired for the debtor’s personal use; the age of the vehicle alone is not the test. Refinancing and mixed loan components require separate purchase-money analysis. The same hanging paragraph also contains a one-year restriction for qualifying purchase-money debt secured by other things of value.

5. Why 910 Days Matters

Nine hundred ten days is approximately two and one-half years.

A debtor who purchased a qualifying vehicle within that period may face different plan treatment from one who purchased the same vehicle earlier.

Example

A debtor owes $30,000 on a vehicle worth $17,000.

If the vehicle was acquired 800 days before filing and the other statutory requirements are satisfied, the 910-day restriction may prevent cramdown.

If the vehicle was acquired 1,100 days before filing, cramdown may be available, subject to the remaining statutory requirements.

The exact acquisition date should be verified.

6. Purchase-Money Security Interests

The 910-day restriction generally concerns qualifying purchase-money security interests.

A purchase-money obligation ordinarily involves financing used to acquire the collateral.

However, automobile financing agreements may include additional amounts.

These may include taxes, fees, service contracts, GAP products, and negative equity from a trade-in.

Whether each component qualifies as purchase-money debt can be disputed.

The governing law and applicable precedent must be examined.

7. Negative Equity From a Trade-In

A borrower may trade in a vehicle worth less than the outstanding loan balance.

The dealer may include the unpaid negative equity in the financing for the replacement vehicle.

For example, the borrower may owe $8,000 more than the trade-in is worth.

That amount may be rolled into the new loan.

The bankruptcy treatment of negative equity under the 910-day provision has generated litigation.

The debtor should obtain the retail installment contract and transaction documents.

8. GAP Coverage

Guaranteed Asset Protection, commonly called GAP coverage, may address certain deficiencies when a financed vehicle is totaled or stolen.

The actual coverage depends on the contract.

GAP products may be insurance policies or contractual debt-cancellation arrangements.

The debtor should determine whether coverage exists, whether the event qualifies, and what amount is payable.

Bankruptcy does not automatically create GAP protection when none was purchased.

9. Vehicle Valuation

When cramdown is available, collateral valuation becomes important.

Section 506(a)(2) generally provides a replacement-value standard for specified personal property acquired for personal, family, or household purposes.

The Supreme Court addressed valuation in *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997).

The debtor should consider vehicle condition, mileage, equipment, and market information.

A generic book value may not accurately reflect the particular vehicle.

10. The *Rash* Decision

In *Associates Commercial Corp. v. Rash*, the Supreme Court addressed valuation of collateral retained by a Chapter 13 debtor.

The Court adopted a replacement-value approach under the statutory framework then applicable.

Congress later added § 506(a)(2), which provides more specific valuation guidance for qualifying personal property.

The decision remains important to the development of Chapter 13 valuation law.

The debtor should apply the current statutory language.

11. Interest Rates on Secured Claims

A creditor receiving payments over time may be entitled to interest sufficient to satisfy the present-value requirement.

In *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004), the Supreme Court addressed the appropriate interest-rate methodology.

The plurality endorsed a formula approach beginning with the prime rate and adjusting for risk.

The applicable rate depends on governing law and the case circumstances.

The debtor should not assume that the original contract rate automatically controls every modified secured claim.

12. Why the Plan Interest Rate Matters

A lower interest rate may materially reduce the amount required to pay a secured claim over the plan term.

For example, a debtor may have an automobile loan with a contract interest rate of 19%.

The Chapter 13 plan may propose a different rate when legally permissible.

The resulting monthly payment can be substantially lower.

However, the creditor may object.

The proposed rate must satisfy applicable law.

13. Paying Vehicle Loans Through the Trustee

A Chapter 13 plan may provide for vehicle payments through the trustee.

The trustee distributes funds according to the confirmed plan.

The debtor must make sufficient plan payments.

The arrangement can simplify administration of arrears and modified secured claims.

However, trustee compensation and distribution timing may affect the calculation.

The debtor should understand whether payments are made through the trustee or directly to the lender.

14. Adequate Protection Before Confirmation

Section 1326(a)(1)(C) addresses certain preconfirmation payments to creditors holding purchase-money security interests in personal property.

The debtor may be required to provide adequate protection before confirmation.

The precise payment arrangements depend on applicable law and court procedures.

The debtor should not assume that the lender receives no protection until the plan is confirmed.

15. What If the Debtor Is Behind on Payments?

Chapter 13 may provide a mechanism for addressing arrears.

The debtor may propose treatment of the secured claim through the plan.

However, the creditor may seek relief from the automatic stay when adequate protection is lacking or other statutory grounds exist.

The debtor must maintain required insurance and comply with applicable obligations.

A plan that cannot fund the vehicle treatment may not be feasible.

16. What If the Vehicle Was Repossessed Before Filing?

A debtor may retain certain rights after repossession under Maryland law.

However, filing bankruptcy does not automatically require immediate return of the vehicle.

In *City of Chicago v. Fulton*, 592 U.S. 154 (2021), the Supreme Court held that mere retention of property seized before bankruptcy does not itself violate § 362(a)(3).

The debtor may need to seek turnover or other relief.

The status of the repossession and any completed sale matters.

17. Surrendering the Vehicle

Section 1325(a)(5)(C) permits surrender of collateral as a form of secured claim treatment.

A debtor may choose surrender when the vehicle is unaffordable or substantially underwater.

The creditor may liquidate the collateral according to applicable law.

A deficiency may remain.

The deficiency's treatment depends on the claim, plan, and applicable bankruptcy provisions.

Surrender does not necessarily mean the creditor has received full payment.

18. Surrender After Confirmation

A debtor may initially retain a vehicle but later decide to surrender it.

This can create complicated modification issues.

The creditor may have received payments under the confirmed plan.

After surrender, the creditor may assert a deficiency.

Courts have disagreed about the permissible reclassification or modification of secured claims after confirmation.

The debtor should not assume that surrender automatically reduces the remaining plan obligation.

19. What If the Car Is Totaled During Chapter 13?

A vehicle may be destroyed in an accident during the repayment plan.

The lender may possess rights to insurance proceeds under the policy and security agreement.

The debtor may need replacement transportation.

The Chapter 13 trustee and bankruptcy court may also have interests in the disposition of proceeds.

The debtor should promptly notify counsel and the insurer.

The insurance settlement should not be distributed without determining the applicable rights.

20. Insurance Proceeds

Insurance proceeds may be payable jointly to the debtor and lienholder.

The creditor may assert rights under the security agreement.

The debtor may have an interest in any excess proceeds.

The bankruptcy estate's interest depends on the circumstances and applicable law.

The debtor should obtain the insurer's valuation, payoff information, and settlement documents.

21. GAP Claims After a Total Loss

If the vehicle is totaled, GAP coverage may reduce or eliminate a qualifying deficiency.

However, the coverage may contain exclusions or conditions.

For example, certain unpaid charges or overdue payments may not be covered.

The debtor should submit the claim promptly and preserve documentation.

The debtor should not assume that GAP automatically pays every amount remaining on the loan.

22. What If There Is No GAP Coverage?

A debtor whose vehicle is totaled may remain liable for a deficiency after application of insurance proceeds.

The deficiency may be treated as an unsecured claim when appropriate.

However, the plan and secured claim treatment may require modification.

The debtor should determine whether replacement financing is necessary and affordable.

The resulting financial circumstances may affect plan feasibility.

23. Replacing a Vehicle During Chapter 13

A debtor may need to purchase another vehicle during the plan.

New borrowing may require trustee consent, court approval, or compliance with applicable local procedures.

The debtor should not assume that financing can be obtained without regard to the confirmed plan.

The proposed payment must be affordable.

The debtor should consult counsel before signing a new financing agreement.

24. Vehicle Insurance

The debtor generally must maintain insurance required by the financing agreement.

Failure to insure collateral may support a creditor's request for stay relief.

Insurance costs should be included accurately in the Chapter 13 budget.

The debtor should notify counsel of substantial premium increases that threaten plan feasibility.

25. Cosigners

A vehicle loan may have a nonfiling cosigner.

Chapter 13 provides a limited codebtor stay for certain consumer obligations under § 1301.

The protection is subject to statutory exceptions.

The debtor's plan treatment may affect the cosigner.

Surrender or nonpayment may expose the cosigner to collection when the stay does not apply or relief is granted.

The debtor should consider the consequences for family members or other obligated parties.

26. Why Vehicle Loan Documents Must Be Reviewed

The attorney should obtain the retail installment contract, payment history, title information, insurance documents, and any GAP agreement.

These records establish the acquisition date, security interest, loan components, and payment terms.

The debtor should also provide accurate vehicle condition and mileage information.

The documents may determine whether cramdown is available and how the claim must be treated.

Conclusion

Chapter 13 provides important options for retaining or surrendering financed vehicles.

When cramdown is permitted, the secured claim may be reduced to the vehicle's value, with the remaining balance treated as unsecured.

But the 910-day rule restricts cramdown for qualifying recently acquired vehicles.

Interest, collateral valuation, adequate protection, and plan feasibility also affect the required treatment.

A vehicle destroyed during Chapter 13 presents additional issues involving insurance proceeds, GAP coverage, deficiencies, and replacement financing.

The appropriate Chapter 13 treatment depends on the loan's legal characteristics, the vehicle's value, the debtor's ability to pay, and the circumstances that arise during the plan.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 506 — Secured claim valuation.
- 11 U.S.C. § 1325(a)(5) — Secured claim treatment.
- 11 U.S.C. § 1326(a) — Preconfirmation payments.
- 11 U.S.C. § 1329 — Plan modification.
- 11 U.S.C. § 1301 — Codebtor stay.
- 11 U.S.C. § 362 — Automatic stay.

Maryland law

- Maryland Commercial Law, Title 12, Subtitle 10 — Credit Grantor Closed End Credit Provisions, where validly elected; distinguish the separate Retail Installment Sales Act and the agreement’s governing law.
- Maryland Commercial Law Article, Title 9 — Secured transactions.

Selected decisions

- *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004) — Addresses Chapter 13 secured claim interest rates.
- *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997) — Addresses valuation of retained collateral.
- *In re Price*, 562 F.3d 618 (4th Cir. 2009) — Addresses the 910-day provision and vehicle claim treatment.
- *City of Chicago v. Fulton*, 592 U.S. 154 (2021) — Addresses retention of property seized before bankruptcy.
- *In re Wright*, 492 F.3d 829 (7th Cir. 2007) — Addresses surrendered collateral and the 910-day provision.
- *In re Nolan*, 232 F.3d 528 (6th Cir. 2000) — Addresses postconfirmation surrender and modification of secured claims.

Chapter 13 and Priority Debts in Maryland: Taxes, Child Support, Alimony, and Obligations That Must Be Paid Through the Plan

Belsky Bankruptcy Legal Library | Chapter 13 Bankruptcy and Priority Claims

By Alan J. Belsky, Attorney at Law

Not All Creditors Receive the Same Treatment in Chapter 13

Chapter 13 permits qualifying individuals to repay debts through a court-supervised plan lasting generally three to five years.

But the debtor cannot simply decide which creditors to pay and how much each will receive.

The Bankruptcy Code establishes priorities for certain obligations.

Domestic support obligations, specified taxes, and certain administrative expenses receive treatment different from ordinary credit card balances and medical bills.

Some priority claims generally must be paid in full through the plan unless the creditor agrees to different treatment or a statutory exception applies.

Other obligations may be nondischargeable even when they do not receive priority treatment.

The distinction between priority and nondischargeability is important.

A debtor may have a debt that survives discharge but is not entitled to priority distribution. Conversely, a priority claim may receive mandatory plan treatment even though the debtor could discharge some related obligations under different circumstances.

Understanding these categories is essential to calculating a feasible Chapter 13 payment.

1. What Is a Priority Claim?

Section 507 establishes categories of claims entitled to priority in bankruptcy distributions.

Priority determines the order and treatment of qualifying claims.

In Chapter 13, § 1322(a)(2) generally requires full payment of claims entitled to priority under § 507 unless the holder agrees to different treatment, subject to statutory exceptions.

The debtor should not assume that every governmental or legally important debt is a priority claim.

The creditor must establish entitlement under the applicable statutory provision.

2. Priority Versus Nondischargeability

Priority and nondischargeability are separate concepts.

Priority concerns distribution through the bankruptcy process.

Nondischargeability concerns whether the debtor remains personally liable after discharge.

For example, a qualifying domestic support obligation generally receives priority and is nondischargeable.

A student loan may be nondischargeable under § 523(a)(8) but ordinarily does not receive general priority merely because it is a student loan.

The distinction affects plan design.

3. Domestic Support Obligations

Section 101(14A) defines domestic support obligations.

Qualifying child support and alimony generally fall within the definition.

Domestic support obligations receive first-priority treatment under § 507(a)(1), subject to statutory distinctions.

They generally are nondischargeable under § 523(a)(5).

The debtor should identify the obligee, amount owed, and whether arrears exist.

4. Child Support Arrears

A debtor may owe past-due child support when Chapter 13 is filed.

The arrears may constitute a priority domestic support obligation.

The plan generally must provide the required statutory treatment.

The debtor also must remain current on qualifying postpetition domestic support obligations.

Failure to do so may prevent confirmation or discharge.

5. Alimony Arrears

Qualifying alimony obligations may also constitute domestic support obligations.

The legal character depends on the substance of the obligation.

A payment labeled alimony in a divorce agreement may require examination of its actual purpose.

Likewise, an obligation described as a property settlement may function as support.

The underlying order and circumstances matter.

6. Divorce Property Settlements

Not every divorce-related debt is a domestic support obligation.

Section 523(a)(15) addresses certain obligations owed to a spouse, former spouse, or child arising from divorce or separation that are not domestic support obligations.

Such obligations may be nondischargeable in Chapter 7 but receive different treatment in Chapter 13.

They do not automatically receive domestic support priority.

The debtor should distinguish support from property division and indemnification.

7. Ongoing Support Payments

A debtor must address domestic support obligations arising after filing.

Section 1325(a)(8) requires the specified postpetition domestic support obligations to have been paid as a condition of confirmation. Applicable procedures may require evidence or certification of compliance; a certification is not a substitute for the substantive payment requirement.

Section 1328(a) contains related discharge requirements.

A debtor who fails to remain current may face serious consequences even when trustee payments are otherwise complete.

8. Domestic Support Certifications

The debtor may be required to certify that qualifying domestic support obligations due after filing have been paid.

The applicable requirements arise under the Bankruptcy Code and procedural rules.

The debtor should maintain payment records.

A certification must be accurate.

The debtor should not assume that completion of the repayment plan automatically establishes compliance with support obligations.

9. Priority Income Taxes

Section 507(a)(8) grants priority to specified tax claims.

Certain relatively recent income taxes may qualify.

The classification depends on return due dates, assessment dates, and other statutory provisions.

The debtor should obtain federal and Maryland tax records.

A tax debt's priority status cannot reliably be determined merely from the tax year.

10. The Three-Year Rule

Section 507(a)(8)(A)(i) generally addresses certain income taxes for which returns were last due, including extensions, within three years before filing.

The period may be suspended or extended under applicable provisions.

A debtor should not simply count three calendar years from the end of the tax year.

The actual return due date matters.

11. The 240-Day Assessment Rule

Section 507(a)(8)(A)(ii) generally addresses certain income taxes assessed within 240 days before filing.

The period may be adjusted by specified events.

An old tax year may still produce a priority claim when additional tax was assessed recently.

The debtor should review assessment records.

12. Tax Claims and Late Returns

Late-filed returns can complicate tax dischargeability.

However, priority classification and nondischargeability are distinct.

A tax may be nondischargeable because of return-filing issues even when it does not qualify for priority under every provision of § 507(a)(8).

The debtor should not assume that every nondischargeable tax must be paid in full as a priority claim through Chapter 13.

The precise statutory classification controls.

13. Federal Payroll Taxes

Certain taxes withheld or collected from others receive special treatment.

These may include employee withholding taxes and other trust fund obligations.

Section 507(a)(8)(C) provides priority treatment for qualifying taxes required to be collected or withheld and for which the debtor is liable.

These obligations generally are not treated like ordinary older income taxes.

Business owners and responsible persons may face substantial personal exposure.

14. Maryland Sales and Withholding Taxes

Maryland tax obligations may include income taxes, sales and use taxes, and employer withholding obligations.

The bankruptcy classification depends on the nature of the tax and applicable law.

Certain obligations may qualify as trust fund taxes.

Others may fall under different priority provisions.

The debtor should obtain itemized records from the Maryland Comptroller.

15. Tax Penalties

Tax penalties may receive different treatment from the underlying tax.

Some penalties may be subordinated or classified as general unsecured claims.

Others may be nondischargeable under applicable provisions.

The debtor should distinguish principal tax, interest, penalties, and collection charges.

The entire tax balance should not automatically be classified as priority.

16. Interest on Priority Taxes

Interest on tax claims may require separate treatment depending on whether the claim is secured, unsecured, priority, or nondischargeable.

Prepetition interest may be included in the allowed claim under applicable law.

Postpetition interest generally raises different questions.

The debtor should not assume that every priority tax claim continues accruing interest payable through the plan in the same manner.

The applicable statutes and claim status matter.

Where the Code requires interest on a tax claim, § 511 generally uses the rate determined under applicable nonbankruptcy law, rather than simply applying Till's vehicle-loan formula. For unsecured nondischargeable obligations, § 1322(b)(10) limits voluntary payment of accruing postpetition interest to disposable income remaining after provision for full payment of all allowed claims. Interest liability and the amount permitted or required through the plan must be analyzed separately.

17. Secured Tax Claims

A taxing authority may possess a valid lien.

A secured tax claim is not identical to an unsecured priority tax claim.

The plan must address the government's secured rights under applicable provisions.

The lien may survive unless properly treated or otherwise resolved.

The debtor should determine whether federal or Maryland tax liens exist before filing.

18. Administrative Expenses

Section 507(a)(2) provides priority for qualifying administrative expenses allowed under § 503(b).

In Chapter 13, administrative expenses may include approved attorney's fees and other qualifying costs.

The plan must provide appropriate treatment.

The debtor should distinguish administrative expenses from ordinary unsecured debts.

19. Chapter 13 Attorney's Fees

Attorney's fees may be paid partly before filing and partly through the plan.

The amount and treatment depend on the fee agreement, applicable law, and court procedures.

Fees paid through the trustee increase the amount that must be funded.

The debtor should understand how much of each plan payment is allocated to administrative expenses.

20. Trustee Compensation

The Chapter 13 trustee receives compensation under applicable federal law.

The trustee percentage affects plan funding.

The rate may vary.

The debtor should use the applicable trustee compensation rate rather than an assumed universal percentage.

The payment calculation must account for the trustee's administration of plan distributions.

21. What If Priority Claims Are Larger Than Expected?

A creditor may file a priority claim exceeding the amount scheduled by the debtor.

For example, the IRS may file a $35,000 priority claim when the debtor anticipated only $18,000.

The discrepancy may materially affect feasibility.

The debtor may need to object to the claim, amend the plan, or consider another option.

The creditor's designation of priority should be reviewed rather than automatically accepted.

22. Objecting to Priority Claims

A debtor may challenge a claim's amount, validity, or priority classification.

Section 502 and applicable Bankruptcy Rules govern claims allowance and objections.

The debtor should obtain supporting documentation.

For tax claims, account transcripts and assessment records may be necessary.

A successful objection may reduce the required plan funding.

However, the debtor must establish the legal basis for the objection.

23. Can Priority Creditors Agree to Different Treatment?

Section 1322(a)(2) generally permits a priority claim holder to agree to different treatment.

The agreement should be clear and legally effective.

The debtor should not assume that silence necessarily constitutes consent to improper treatment.

The plan must satisfy the applicable confirmation requirements.

Section 1322(a)(4) supplies a particular exception for claims entitled to priority under § 507(a)(1)(B), generally specified assigned or governmental support claims: less than full payment may be proposed only if all projected disposable income for the prescribed five-year period is applied to plan payments. This is not a general power to reduce support owed directly to a spouse, former spouse, or child.

24. Priority Debts and the Plan Payment

Priority obligations can materially increase the required monthly payment.

Example

Assume a debtor has:

Obligation	Amount

Obligation	Amount
Priority income taxes	$24,000
Domestic support arrears	$12,000
Attorney's fees through plan	$4,000
Total	$40,000

Over sixty months, $40,000 requires average funding of approximately $666.67 per month before trustee compensation and other required distributions.

The debtor may also need to fund secured claims and general unsecured creditor payments.

The plan must account for all applicable requirements.

25. What If the Debtor Cannot Pay Priority Claims in Full?

A debtor may lack sufficient income to pay required priority obligations within the maximum plan term.

The debtor may seek a permissible alternative arrangement or creditor agreement.

But Chapter 13 does not automatically authorize reduction of mandatory priority payments.

If no feasible plan can be proposed, the debtor may need to consider Chapter 7, Chapter 11, or nonbankruptcy alternatives.

The appropriate response depends on the debts and financial circumstances.

26. Priority Claims and Discharge

Completion of a Chapter 13 plan generally results in discharge of qualifying debts under § 1328(a).

However, some obligations survive discharge.

Domestic support obligations generally remain nondischargeable.

Certain tax debts and other obligations may also survive.

The debtor should not assume that payment of all required priority distributions necessarily eliminates every related personal obligation.

27. Why Priority Classification Matters Before Filing

A debtor may appear capable of funding a Chapter 13 plan until priority claims are identified.

For example, substantial tax obligations may require full payment over the plan period.

The debtor should obtain tax transcripts, support orders, and other relevant records before filing.

Accurate classification can prevent an unrealistic plan.

Conclusion

Chapter 13 gives special treatment to certain priority claims.

Domestic support obligations, specified taxes, and administrative expenses can materially affect the required plan payment.

But priority and nondischargeability are different concepts.

Not every nondischargeable debt receives priority, and not every amount claimed by a government agency qualifies for priority treatment.

A feasible Chapter 13 plan begins with accurate identification of priority obligations and the amount that must be paid through the plan.

Related Bankruptcy Cases and Authorities

Federal statutes

- 11 U.S.C. § 101(14A) — Domestic support obligations.
- 11 U.S.C. § 507 — Priority claims.
- 11 U.S.C. § 503 — Administrative expenses.
- 11 U.S.C. § 523 — Exceptions to discharge.
- 11 U.S.C. § 1322(a)(2) — Priority claim treatment.
- 11 U.S.C. § 1325 — Confirmation requirements.
- 11 U.S.C. § 1328 — Chapter 13 discharge.

Selected decisions

- *United States v. Sotelo*, 436 U.S. 268 (1978) — Addresses trust fund tax liability.
- *United States v. Noland*, 517 U.S. 535 (1996) — Addresses equitable subordination of tax penalty claims.
- *In re Kestell*, 99 F.3d 146 (4th Cir. 1996) — Addresses debtor conduct and abuse; relevance to priority classification is limited.

Maryland practice authorities

- United States Bankruptcy Court for the District of Maryland — Chapter 13 procedures and local forms.
- Maryland Comptroller — State tax records and claims.

Where Does Your Chapter 13 Payment Go? How the Trustee Distributes Money to Creditors

Belsky Bankruptcy Legal Library | Chapter 13 Trustee Payments and Creditor Distributions

By Alan J. Belsky, Attorney at Law

Paying the Chapter 13 Trustee Is Not the Same as Paying Each Creditor Directly

A Chapter 13 debtor may make substantial monthly payments for several years and still be surprised to discover that certain creditors have received relatively little money.

For example, a debtor may pay $1,500 monthly for two years, contributing $36,000 to the Chapter 13 trustee.

Yet a particular unsecured creditor may have received only a small distribution.

That does not necessarily mean that money has disappeared or been improperly handled.

Chapter 13 payments are distributed according to the confirmed repayment plan, the Bankruptcy Code, and applicable trustee procedures.

Some funds may be used for trustee compensation, attorney's fees, secured claims, mortgage arrears, and priority debts before substantial distributions reach general unsecured creditors.

Other creditors may receive payments concurrently.

Understanding the difference between the debtor's payments to the trustee and the trustee's payments to creditors is essential to evaluating plan progress.

1. The Trustee Is a Disbursing Agent

The Chapter 13 trustee receives payments from the debtor and administers distributions under the confirmed plan.

The trustee does not ordinarily decide independently which creditor deserves payment.

The Bankruptcy Code and confirmed plan govern treatment.

The trustee also performs statutory duties concerning administration, claims, and financial reporting.

The debtor should distinguish the trustee's role from that of the bankruptcy judge.

2. The Confirmed Plan Controls Distributions

Section 1327(a) generally provides that a confirmed Chapter 13 plan binds the debtor and creditors.

The plan specifies the treatment of secured claims, priority obligations, administrative expenses, and general unsecured claims.

The trustee distributes funds according to the confirmed terms and applicable law.

A debtor should not assume that each monthly payment is divided proportionately among every creditor.

The allocation may vary over the life of the plan.

3. Trustee Compensation

Chapter 13 trustees receive compensation under federal law.

The trustee generally retains the authorized percentage from qualifying payments received.

The applicable percentage may vary.

The debtor should not assume that a fixed national rate applies to every Chapter 13 case.

The trustee's compensation reduces the amount available for creditor distributions.

4. Attorney's Fees

Chapter 13 attorney's fees may be paid partly before filing and partly through the plan.

Fees paid through the trustee generally receive administrative expense treatment when allowed.

Section 1326(b)(1) addresses payment of qualifying unpaid administrative expenses.

The plan and applicable procedures determine the distribution arrangement.

The debtor should know how much of the attorney's fee remains unpaid.

5. Secured Claims

Secured creditors possess liens against property.

A Chapter 13 plan may provide for payment of certain secured claims through the trustee.

Examples include automobile loans and other qualifying collateral obligations.

The payment schedule must satisfy applicable statutory requirements.

Some secured creditors may receive distributions before general unsecured creditors.

Others may receive concurrent payments.

6. Adequate Protection Payments

Certain secured creditors may receive adequate-protection payments before confirmation.

Section 1326(a)(1)(C) addresses specified payments concerning purchase-money security interests in personal property.

For example, a vehicle lender may receive preconfirmation adequate-protection payments.

These payments may affect the remaining secured claim balance.

The debtor should not assume that every preconfirmation payment remains undistributed until confirmation.

7. Mortgage Arrearage Payments

A Chapter 13 plan may provide for curing prepetition mortgage arrears through trustee payments.

The debtor may separately pay ongoing mortgage installments directly to the lender.

For example, the trustee may distribute $400 monthly toward mortgage arrears while the debtor pays the regular mortgage outside the plan.

The two obligations are distinct.

The debtor should monitor both.

8. Priority Domestic Support Obligations

Domestic support obligations receive special priority under § 507(a)(1).

The plan must provide the treatment required by the Bankruptcy Code.

Section 1326(b)(1) addresses unpaid § 507(a)(2) administrative claims before or at the time of creditor payments; it is not a special governmental-support rule. Governmental or assigned support claims require analysis under § 507(a)(1)(B) and the particular treatment permitted by § 1322(a)(4), alongside the remaining priority and plan requirements.

The trustee must follow the applicable statutory requirements.

The debtor also must remain current on qualifying postpetition support obligations.

9. Priority Tax Claims

Certain tax obligations receive priority under § 507(a)(8).

The plan generally must provide required treatment of these claims.

However, priority does not necessarily mean that every tax claim must be paid in full before any other creditor receives money.

The confirmed plan and applicable law govern distribution timing.

The debtor should distinguish priority tax principal from penalties, secured tax claims, and other components.

10. General Unsecured Creditors

General unsecured creditors may include credit card companies, medical providers, personal lenders, and other creditors without collateral or priority status.

Their distributions depend on the confirmed plan.

A plan may provide full payment, partial payment, or no distribution to general unsecured creditors, subject to statutory requirements.

The debtor should not assume that every unsecured creditor receives monthly payments from the beginning of the case.

11. Why Unsecured Creditors May Receive Little Money Initially

A plan may require substantial early payments toward attorney's fees, secured claims, or priority obligations.

General unsecured distributions may therefore be delayed or relatively small.

For example, a debtor may pay $1,200 monthly while most funds are allocated to a vehicle loan and mortgage arrears.

The confirmed plan may provide that unsecured creditors receive larger distributions later.

The debtor should review the trustee's disbursement history rather than assuming that limited early payments indicate an error.

12. Example of Monthly Distribution

Assume a debtor pays $1,500 monthly.

An illustrative distribution might be:

Recipient	Monthly amount
Trustee compensation	$120
Attorney's fees	$250
Vehicle lender	$400
Mortgage arrears	$350
Priority taxes	$300
General unsecured creditors	$80
Total	$1,500

These amounts are hypothetical.

The actual distribution depends on the trustee's authorized percentage, the confirmed plan, claim allowances, and applicable procedures.

The example illustrates concurrent distributions rather than a mandatory payment order.

13. Distribution Order May Change During the Plan

The allocation of payments may change as claims are satisfied.

For example, attorney's fees may be paid in full during the first portion of the plan.

Funds previously allocated to those fees may then become available for other creditors.

Likewise, completion of payments on a secured claim may change the distribution pattern.

The debtor's required monthly payment does not necessarily decrease.

14. Why Paying Off a Vehicle Does Not Automatically Reduce the Plan Payment

A debtor may believe that once the automobile lender is paid in full, the monthly plan payment should decrease by the amount previously distributed to that creditor.

That is not necessarily correct.

The plan may require the same total payment to satisfy projected disposable income, liquidation value, or other obligations.

Funds previously paid to the vehicle lender may be redirected to other creditors.

The debtor should not reduce payments without an approved modification or other appropriate authorization.

15. What Happens Before Confirmation?

Section 1326(a) governs specified preconfirmation payments.

The trustee generally retains payments until confirmation, subject to statutory exceptions and authorized adequate-protection distributions.

After confirmation, the trustee distributes funds under the plan.

If confirmation is denied, the statute provides for return of retained funds after specified deductions.

The debtor should distinguish funds received by the trustee from funds already disbursed.

16. What If a Creditor Never Files a Proof of Claim?

A creditor's entitlement to distribution may depend on whether an allowed claim exists.

In Chapter 13, filing deadlines and claims procedures matter.

A creditor that fails to file a timely proof of claim may receive no distribution, subject to applicable exceptions and procedures.

The debtor or trustee may be permitted to file a claim on a creditor's behalf under Rule 3004.

The debtor should not assume that an omitted claim automatically eliminates every underlying obligation.

17. Claims That Are Disallowed

A claim may be disallowed after objection.

The trustee generally should not distribute funds on a disallowed claim except as permitted by applicable law or order.

The funds may become available for other plan obligations.

The debtor should review claims carefully.

An incorrect claim can materially affect plan funding and distributions.

18. Claims That Are Larger Than Expected

A creditor may file a claim exceeding the amount scheduled.

For example, a mortgage lender may assert $25,000 in arrears when the debtor anticipated $18,000.

The larger claim may require increased funding or plan modification.

The debtor should not assume that the scheduled amount controls the creditor's allowed claim.

The proof of claim and supporting documents must be reviewed.

19. Trustee Accounting Statements

Chapter 13 trustees maintain records of payments received and distributions made.

The debtor may be able to review account information through trustee statements or authorized online systems.

The records may show the date and amount of each payment, trustee compensation, distributions to creditors, and remaining claim balances.

The debtor should review the information periodically.

Errors or discrepancies should be raised promptly.

Online Access to Your Chapter 13 Trustee Account

Many Chapter 13 trustees provide debtors with online access to information about their repayment plans.

One commonly used service is the National Data Center (NDC), which allows participating Chapter 13 debtors to register and review information reported by their trustees.

Depending on the trustee and available records, debtors may be able to see payments received, distributions made to individual creditors, claim balances, and the overall progress of their Chapter 13 plans.

Access generally requires registration and verification of the debtor's identity and bankruptcy case information.

Not every trustee uses the same online system, and information may not be updated immediately after a payment or distribution.

Debtors should periodically review their accounts to confirm that payments have been credited and that distributions appear consistent with the confirmed plan.

Online account information is useful for monitoring progress, but it does not replace the confirmed plan, official court records, or advice from bankruptcy counsel.

20. How to Read a Trustee Statement

A trustee statement may distinguish between money received and money disbursed.

For example, the debtor may have paid $30,000 into the plan.

The trustee may have distributed $26,000 to creditors and retained or allocated the remaining amount according to applicable requirements.

The debtor should identify whether any funds remain on hand.

The statement may also show claim balances and distribution categories.

The debtor should not assume that the total paid to the trustee equals the total reduction in principal owed to creditors.

21. Why Principal Balances May Decline Slowly

Some secured claims require interest payments.

Other claims may include fees or other allowed charges.

Trustee compensation and administrative expenses also consume part of the plan funding.

A debtor may therefore contribute substantial money without seeing an equivalent reduction in the principal balance of a particular loan.

The correct comparison is between the plan's required treatment and the trustee's actual distributions.

22. Direct Payments Outside the Plan

Some obligations may be paid directly by the debtor rather than through the trustee.

Examples may include ongoing mortgage payments, utilities, insurance, and other current expenses.

These payments generally do not appear as trustee distributions.

The debtor should maintain separate records.

A debtor who is current with the trustee may nevertheless be delinquent on a direct mortgage obligation.

23. What If the Debtor Pays More Than Required?

A debtor may make additional payments to the trustee.

The effect depends on the confirmed plan and applicable law.

Extra payments may reduce the remaining amount needed to satisfy certain obligations.

However, they do not necessarily shorten the applicable commitment period or automatically entitle the debtor to an early discharge.

The debtor should consult counsel before making substantial lump-sum payments.

24. What If the Debtor Misses Payments?

Missed payments reduce the funds available for distribution.

The trustee may seek dismissal when the debtor falls behind.

The debtor may seek modification or other relief when appropriate.

The debtor should not assume that creditors will continue receiving scheduled distributions regardless of payment defaults.

25. Final Accounting and Completion

At the end of the plan, the trustee must determine whether the debtor has completed required payments.

The trustee's final accounting may identify distributions made and claims satisfied.

Certain mortgage cure procedures under Rule 3002.1 may also be required.

The debtor must satisfy applicable discharge conditions.

The completion of payments and entry of discharge are distinct events.

Conclusion

Chapter 13 payments are distributed according to the confirmed plan, statutory priorities, and applicable trustee procedures.

The trustee may pay administrative expenses, secured claims, mortgage arrears, priority obligations, and general unsecured creditors at different times or concurrently.

The debtor's monthly payment does not necessarily correspond to an equal reduction in every creditor's balance.

As claims are paid, distribution patterns may change without automatically reducing the debtor's required payment.

A debtor should review trustee accounting records periodically to understand where plan payments are going and whether the distributions are consistent with the confirmed plan.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 507 — Priority claims.
- 11 U.S.C. § 1322 — Plan provisions.
- 11 U.S.C. § 1326 — Payments and distributions.
- 11 U.S.C. § 1327 — Effect of confirmation.
- 11 U.S.C. § 1329 — Plan modification.
- Federal Rule of Bankruptcy Procedure 3004 — Filing claims on behalf of creditors.
- Federal Rule of Bankruptcy Procedure 3002.1 — Home mortgage claim procedures.

Selected decisions

- *Harris v. Viegelahn*, 575 U.S. 510 (2015) — Addresses undistributed Chapter 13 funds following conversion to Chapter 7.
- *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010) — Addresses binding effect of confirmed plans.
- *Till v. SCS Credit Corp.*, 541 U.S. 465 (2004) — Addresses interest on secured claims.
- *In re Michael*, 699 F.3d 305 (3d Cir. 2012) — Addresses disposition of funds following Chapter 13 conversion.

- *In re Nash*, 765 F.2d 1410 (9th Cir. 1985) — Addresses payments following dismissal of a Chapter 13 case.

Maryland practice authorities

- United States Bankruptcy Court for the District of Maryland — Chapter 13 plan forms and local procedures.
- National Association of Chapter 13 Trustees — Trustee administration information.

Chapter 13 and Tax Refunds, Inheritances, Bonuses, and Personal Injury Settlements: Who Gets the Money During the Plan?

Belsky Bankruptcy Legal Library | Chapter 13 Bankruptcy and Postpetition Property

By Alan J. Belsky, Attorney at Law

Receiving Money During Chapter 13 Does Not Necessarily Mean You Can Keep or Spend It

A Chapter 13 repayment plan generally lasts three to five years. During that period, a debtor's financial circumstances may change substantially.

The debtor may receive an inheritance, a tax refund, a substantial employment bonus, proceeds from a personal injury settlement, or money from the sale of property.

These events raise an important question: Who is entitled to the money?

Unlike Chapter 7, Chapter 13 generally includes certain property and earnings acquired after the bankruptcy petition within the bankruptcy estate.

However, the fact that property becomes part of the estate does not automatically mean that the Chapter 13 trustee is entitled to take all of it.

Exemptions, the confirmed plan, disposable-income requirements, and the Bankruptcy Code's modification provisions may affect the result.

A debtor should not assume that every unexpected payment belongs to the trustee.

Nor should the debtor assume that money received after filing is available for unrestricted personal use.

1. Chapter 13 Estate Property

Section 541 generally defines property of the bankruptcy estate.

Section 1306 expands the Chapter 13 estate to include specified property acquired after filing and earnings from services performed after commencement of the case.

The statutory period generally extends until the case is closed, dismissed, or converted.

The scope of estate property can therefore be broader than in an ordinary Chapter 7 case.

The debtor should disclose material acquisitions and changes as required by law and applicable court procedures.

2. The Effect of Confirmation

Section 1327(b) generally provides that confirmation vests property of the estate in the debtor unless the plan or confirmation order provides otherwise.

Section 1306, however, addresses property acquired during the Chapter 13 case.

Courts have developed different approaches to reconciling these provisions.

The confirmed plan and applicable Fourth Circuit precedent are important.

The debtor should not assume that confirmation automatically removes every later-acquired asset from bankruptcy administration.

Trantham v. Tate, No. 22-2263 (4th Cir. Aug. 13, 2024), holds that a local form's default vesting provision cannot categorically prevent a debtor from proposing a Code-compliant alternative that vests property at confirmation. Whether property remains in the estate affects the need for approval of its use or sale. The decision also preserves Murphy's rule allowing a qualifying modification based on a substantial and unanticipated change; vesting does not eliminate every later payment issue.

3. Tax Refunds

A debtor may receive federal or Maryland income tax refunds during the plan.

The treatment depends on the confirmed plan, applicable law, and the source of the refund.

Some plans require turnover of tax refunds or specified portions.

Other circumstances may permit the debtor to retain funds.

The debtor should review the confirmed plan before spending a substantial refund.

The fact that the refund was received after filing does not automatically establish that it is unrestricted.

4. Why Tax Refunds Can Be Significant

A tax refund generally represents an overpayment of tax.

The debtor may have received less take-home income during the year because of withholding.

The trustee may argue that substantial recurring refunds indicate that more income is available for plan payments.

However, the treatment depends on the plan and applicable law.

The debtor should distinguish recurring excess withholding from an unusual one-time refund.

5. Adjusting Tax Withholding

A debtor who consistently receives large refunds may consider adjusting withholding to more closely approximate actual tax liability.

However, the debtor should not change withholding merely to avoid plan obligations.

The change may affect monthly disposable income and plan funding.

The debtor should consult counsel and a tax professional when appropriate.

The objective is accurate tax payment and compliance with the confirmed plan.

6. Employment Bonuses

A debtor may receive an annual bonus, commission, profit-sharing payment, or other additional compensation.

The treatment depends on the plan and applicable law.

A recurring bonus may have been anticipated in the original income calculation.

An unexpected substantial bonus may prompt review of disposable income or modification.

The debtor should disclose material income changes as required.

7. Overtime Earnings

A debtor may begin working substantial overtime during the plan.

The additional income may affect the debtor's financial circumstances.

However, not every temporary increase necessarily requires modification.

The trustee may examine whether the increase is substantial, continuing, or otherwise relevant under applicable law.

The debtor should preserve pay statements and provide accurate information when requested.

8. Salary Increases

A debtor may receive a promotion or substantial raise.

The trustee or a qualifying unsecured creditor may seek modification under § 1329.

The Fourth Circuit has addressed postconfirmation modification when financial circumstances materially improve.

The debtor should not assume that all increased earnings may be retained without regard to the plan.

However, the applicable legal standard and confirmed plan terms must be examined.

9. Inheritances

An inheritance received during Chapter 13 can present substantial issues.

In *Carroll v. Logan*, 735 F.3d 147 (4th Cir. 2013), the Fourth Circuit held that an inheritance received more than 180 days after filing became property of the Chapter 13 estate.

The decision is particularly important in Maryland.

A debtor should not assume that an inheritance received more than six months after filing is automatically excluded.

The timing, nature, and value of the inheritance matter.

10. The 180-Day Rule

Section 541(a)(5) generally includes certain inheritances and other specified interests acquired within 180 days after filing.

However, § 1306 expands Chapter 13 estate property.

The Fourth Circuit's decision in *Carroll* illustrates that the 180-day limitation does not necessarily exclude later inheritances from the Chapter 13 estate.

The debtor should distinguish Chapter 7 treatment from Chapter 13 treatment.

11. What If the Inheritance Is Exempt?

An inheritance may include cash, real estate, retirement interests, or other property.

The debtor may possess applicable exemption rights.

However, the availability and amount of exemptions depend on the property and governing law.

The debtor should not assume that every inherited asset is exempt.

Nor should the debtor assume that estate property must automatically be surrendered without considering exemptions and plan requirements.

12. Inherited Real Estate

A debtor may inherit an interest in a residence or other real property during Chapter 13.

The interest may become estate property.

The debtor should determine ownership, liens, value, and available exemptions.

A proposed sale or transfer may require compliance with bankruptcy procedures.

The debtor should not convey the property without evaluating the bankruptcy consequences.

13. Personal Injury Claims

A debtor may be injured in an automobile accident or other incident during Chapter 13.

The resulting cause of action may constitute property of the bankruptcy estate.

The debtor should disclose the claim.

The bankruptcy court may need to approve employment of counsel, settlement, or other matters under applicable law and procedures.

The debtor should not assume that a claim arising after filing is outside the bankruptcy case.

14. Maryland Personal Injury Exemptions

Maryland provides substantial exemption protection for qualifying personal injury compensation under Courts and Judicial Proceedings § 11-504(b)(2).

The exemption may protect compensation for personal injury, subject to statutory language and applicable law.

The Fourth Circuit addressed Maryland's personal injury exemption in *In re Butcher*, 125 F.3d 238 (4th Cir. 1997).

The exemption can be particularly important when a Chapter 13 debtor receives settlement proceeds.

However, the debtor must distinguish exemption rights from plan modification and other statutory issues.

Maryland § 11-504(i) expressly permits execution on a child-support-arrearage judgment against 25% of the debtor's defined net personal injury or qualifying workers' compensation indemnity recovery. The ordinary personal injury exemption also does not itself extinguish valid liens or reimbursement rights.

15. Personal Injury Settlement Proceeds

A debtor may receive a substantial settlement during the plan.

The settlement may include compensation for medical expenses, lost income, pain and suffering, or other damages.

The legal treatment may depend on the nature of the claim and applicable exemptions.

The debtor should coordinate bankruptcy and personal injury counsel.

Settlement proceeds should not be distributed without determining the estate's interest, exemption rights, liens, and applicable court requirements.

16. Workers' Compensation Benefits

A debtor may receive workers' compensation benefits or a settlement during Chapter 13.

Maryland law provides protections for qualifying workers' compensation benefits.

However, the debtor should disclose the claim and determine its bankruptcy treatment.

The nature of the payment may affect exemption and disposable-income questions.

A lump-sum settlement may require different analysis from periodic wage-replacement benefits.

17. Life Insurance Proceeds

A debtor may become entitled to life insurance proceeds during Chapter 13.

The treatment depends on the policy, beneficiary designation, timing, and applicable exemption law.

Section 541(a)(5) addresses certain interests acquired within 180 days after filing.

Section 1306 may expand the Chapter 13 estate beyond that period.

The debtor should disclose the proceeds and determine available exemptions.

18. Gifts

A debtor may receive a substantial gift from a family member or another person.

The gift may constitute property acquired during Chapter 13.

The debtor should not assume that a gift is excluded merely because it was not earned income.

The confirmed plan and applicable law may affect whether the funds must be disclosed or used for plan payments.

Ordinary small gifts may present different practical considerations from substantial transfers.

19. Lottery and Gambling Winnings

A debtor may receive lottery winnings or other gambling proceeds during Chapter 13.

The winnings may constitute property of the estate under § 1306.

A substantial award may affect the debtor's financial circumstances and prompt modification.

The debtor should disclose the winnings.

The fact that the funds were acquired through chance rather than employment does not automatically exclude them from bankruptcy administration.

20. Sale of Property During Chapter 13

A debtor may wish to sell real estate, a vehicle, or other valuable property during the plan.

The sale may require bankruptcy court approval or compliance with applicable procedures.

The proceeds may be subject to liens, exemptions, and estate interests.

The debtor should determine how the transaction affects the confirmed plan.

A sale should not be completed without considering the bankruptcy consequences.

21. Refinancing Real Estate

A debtor may refinance a home during Chapter 13.

The transaction may generate cash proceeds or change secured obligations.

The debtor may need court approval or compliance with local procedures.

The trustee may examine the effect on creditors and plan feasibility.

The debtor should not assume that equity withdrawn through refinancing can be spent without restriction.

22. Trustee Motions to Modify

Section 1329 permits specified parties to seek modification before completion of plan payments.

The trustee may seek increased payments when the debtor's financial circumstances improve.

The proposed modification must satisfy applicable statutory requirements.

The debtor may oppose the modification.

The court determines whether the change is permissible.

23. The Fourth Circuit's Decision in *Murphy*

In *In re Murphy*, 474 F.3d 143 (4th Cir. 2007), the Fourth Circuit addressed postconfirmation modification in circumstances involving changes in property value and financial circumstances.

The decision is important when evaluating whether a debtor's improved financial position may support increased payments.

The court considered the effect of substantial and unanticipated changes.

The case should be examined alongside § 1329 and the confirmed plan.

24. Exempt Property and Modification

The fact that property is exempt does not automatically resolve every Chapter 13 disposable-income or modification question.

Exemptions protect specified property interests from creditor administration under applicable law.

The plan's treatment of income and postconfirmation changes may involve separate statutory provisions.

The debtor should not assume that every exempt asset can be spent without regard to the confirmed plan.

Conversely, the trustee should not assume that every receipt of exempt property automatically requires turnover.

The precise legal basis for any proposed modification must be established.

25. Why Disclosure Matters

A debtor who receives substantial funds during Chapter 13 should promptly notify counsel.

Failure to disclose an inheritance, settlement, or other significant asset may create serious problems.

The debtor may face objections, modification proceedings, or allegations of bad faith.

Accurate disclosure permits counsel to determine whether the funds are exempt, subject to the plan, or otherwise available.

The debtor should not wait until the trustee independently discovers the transaction.

26. What If the Debtor Spends the Money Before Disclosure?

Spending substantial proceeds without determining their bankruptcy status can create complications.

The trustee may seek information or relief.

The court may examine the debtor's conduct.

The debtor may be unable to restore funds that should have been preserved.

The debtor should obtain legal advice before using substantial unexpected funds during Chapter 13.

27. Why the Confirmed Plan Must Be Reviewed

The confirmed plan may contain provisions concerning tax refunds, additional income, property sales, or other financial changes.

Those provisions may affect the debtor's obligations.

The debtor should not rely solely on general statements about Chapter 13 estate property.

The actual plan, confirmation order, and applicable law control.

Conclusion

Chapter 13 debtors may acquire substantial property or income during the repayment period.

Section 1306 generally expands the bankruptcy estate to include specified postpetition property and earnings.

Tax refunds, bonuses, inheritances, settlements, gifts, and other funds may therefore affect the case.

However, inclusion in the estate does not automatically establish that every dollar belongs to the trustee.

Exemptions, confirmed plan provisions, and modification requirements must be considered.

A Chapter 13 debtor who receives substantial unexpected money should disclose it promptly and determine its legal treatment before spending or transferring the funds.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 541 — Property of the bankruptcy estate.
- 11 U.S.C. § 1306 — Chapter 13 estate property.
- 11 U.S.C. § 1327 — Effect of confirmation.
- 11 U.S.C. § 1329 — Postconfirmation modification.
- 11 U.S.C. § 522 — Exemptions.

Maryland law

- Maryland Courts and Judicial Proceedings § 11-504 — Maryland exemptions.

Selected decisions

- *Carroll v. Logan*, 735 F.3d 147 (4th Cir. 2013) — Holds that an inheritance acquired more than 180 days after filing may become Chapter 13 estate property.
- *In re Murphy*, 474 F.3d 143 (4th Cir. 2007) — Addresses postconfirmation modification and changes in financial circumstances.
- *In re Arnold*, 869 F.2d 240 (4th Cir. 1989) — Addresses modification following changed circumstances.
- *In re Butcher*, 125 F.3d 238 (4th Cir. 1997) — Addresses Maryland's personal injury exemption.
- *Hamilton v. Lanning*, 560 U.S. 505 (2010) — Addresses projected disposable income.
- *Harris v. Viegelahn*, 575 U.S. 510 (2015) — Addresses undistributed Chapter 13 funds following conversion to Chapter 7.

Chapter 13 Dismissal, Conversion, and Hardship Discharge: What Happens When the Debtor Cannot Finish the Plan?

Belsky Bankruptcy Legal Library | Chapter 13 Bankruptcy, Claims, and Discharge

By Alan J. Belsky, Attorney at Law

A Chapter 13 Case Can End in Several Different Ways—and the Consequences Are Not the Same

A Chapter 13 debtor may spend years making payments to the bankruptcy trustee but encounter financial difficulties before completing the repayment plan.

Job loss, illness, increased living expenses, divorce, or unexpected financial obligations may make continued payments impossible.

The debtor may seek to modify the plan, convert to Chapter 7, request dismissal, or, in limited circumstances, obtain a hardship discharge.

These alternatives have very different consequences.

1. The Four Principal Ways a Chapter 13 Case May End

A Chapter 13 case may conclude through successful completion and discharge, dismissal, conversion to another bankruptcy chapter, or a hardship discharge under § 1328(b).

Successful completion generally produces the ordinary Chapter 13 discharge.

Dismissal ordinarily leaves the debtor without that discharge.

Conversion changes the governing bankruptcy chapter and may expose nonexempt property to liquidation.

A hardship discharge is available only when specific statutory requirements are satisfied and is narrower than the ordinary Chapter 13 discharge.

The debtor should understand the consequences before selecting an alternative.

2. Missing Chapter 13 Payments

Under § 1307(c)(4), failure to commence making timely payments under § 1326 may constitute cause for dismissal or conversion.

A debtor who falls behind after confirmation may also face dismissal proceedings for material default under the confirmed plan.

The trustee may file a motion seeking dismissal.

The debtor may be able to cure the delinquency, propose a modification, or otherwise respond.

However, repeated missed payments can make successful completion increasingly difficult.

3. Motions to Dismiss

Section 1307(c) authorizes dismissal or conversion for cause, subject to applicable requirements.

Grounds may include unreasonable delay prejudicial to creditors, failure to make required payments, material default under a confirmed plan, or denial of confirmation under specified circumstances.

The debtor ordinarily receives notice and an opportunity to respond.

The court may determine whether dismissal or conversion is in the best interests of creditors and the estate.

A debtor should not ignore a trustee's motion merely because payments have resumed.

4. Can the Debtor Reduce Payments Instead?

Section 1329 permits specified modifications of a confirmed Chapter 13 plan before completion of payments.

A debtor whose income has declined may seek reduced payments or other permissible adjustments.

But the modified plan must satisfy applicable statutory requirements.

Priority obligations, secured claims, liquidation value, and the maximum plan duration may restrict the available relief.

A debtor cannot necessarily reduce payments below the amount needed to satisfy mandatory plan obligations.

5. The Five-Year Limit

Chapter 13 plans generally cannot extend beyond five years.

Section 1329(c) restricts the duration of modified plans.

A debtor who falls substantially behind late in the case may have limited time to cure the delinquency.

The court ordinarily cannot extend the plan indefinitely merely because the debtor needs more time.

This is one reason prompt attention to missed payments matters.

6. Voluntary Dismissal

Section 1307(b) generally gives a Chapter 13 debtor who did not previously convert the case a right to seek dismissal.

The statute contains specific language governing that right.

Questions concerning bad faith, pending motions, and the relationship between dismissal and conversion have generated litigation.

A debtor should not assume that dismissal eliminates the consequences of conduct occurring during the case.

Dismissal also ordinarily terminates bankruptcy protection and leaves unpaid debts enforceable.

7. What Happens to Creditors After Dismissal?

Dismissal generally terminates the automatic stay under § 362(c)(2)(B).

Creditors may resume lawful collection activity, subject to applicable nonbankruptcy law and court orders.

A mortgage lender may resume foreclosure.

An automobile lender may pursue repossession.

Unsecured creditors may resume lawsuits or judgment enforcement.

The debtor generally does not receive a discharge of unpaid debts.

8. Are Payments Made During Chapter 13 Lost?

Not necessarily.

Money already distributed to creditors ordinarily remains credited according to applicable law.

For example, trustee payments may have reduced a vehicle loan or cured part of a mortgage arrearage.

However, the debtor may have paid trustee compensation, attorney's fees, and other expenses during the case.

Dismissal does not ordinarily require creditors to return all payments received under the plan.

The debtor should obtain a trustee accounting before evaluating the remaining debts.

9. What Happens to Money Still Held by the Trustee?

Undistributed funds require separate analysis.

The result can depend on whether the case is dismissed, converted, or otherwise terminated, and on the applicable statutory provisions.

In *Harris v. Viegelahn*, 575 U.S. 510 (2015), the Supreme Court held that undistributed postpetition wages held by a Chapter 13 trustee ordinarily must be returned to the debtor following conversion to Chapter 7 in the circumstances addressed.

Dismissal presents a different statutory framework, including § 349 and § 1326.

The debtor should not assume that all funds held by the trustee receive identical treatment regardless of how the case ends.

10. Conversion to Chapter 7

Under § 1307(a), a Chapter 13 debtor generally may convert the case to Chapter 7, subject to applicable statutory requirements.

Conversion may be appropriate when the debtor can no longer afford plan payments.

However, the debtor must qualify for Chapter 7 relief.

The debtor should also determine whether nonexempt property may become available for liquidation.

Conversion may eliminate the obligation to continue the Chapter 13 plan, but it does not guarantee that the debtor can retain every asset.

11. Property of the Converted Chapter 7 Estate

Section 348(f) generally governs property of the estate when a Chapter 13 case converts to Chapter 7.

In a qualifying good-faith conversion, the converted estate generally includes property belonging to the estate on the original petition date that remains in the debtor's possession or control at conversion.

Section 348(f)(2) instead uses property of the estate as of conversion when the debtor converts in bad faith. Section 348(f)(1)(B) also prevents the Chapter 13 valuation and allowed-secured-claim determination from automatically carrying into Chapter 7. Asset ownership, disposition, valuation, and lien issues should be examined before conversion.

The debtor should examine property acquired or disposed of during Chapter 13 before converting.

12. The Hardship Discharge

Section 1328(b) permits a hardship discharge when the debtor cannot complete payments because of circumstances for which the debtor should not justly be held accountable.

The debtor must also satisfy the statutory liquidation-value requirement.

Modification under § 1329 must be impracticable.

The hardship discharge is not automatically available whenever the debtor loses employment or becomes ill.

The court must determine whether all requirements have been met.

13. The Hardship Discharge Is Narrower

A hardship discharge under § 1328(b) does not provide the same scope of relief as an ordinary Chapter 13 discharge under § 1328(a).

Section 1328(c) limits the hardship discharge to covered unsecured debts and incorporates all § 523(a) categories, as well as excluding debts provided for under § 1322(b)(5). Non-support divorce obligations and certain intentional-injury debts therefore can receive a different result from an ordinary completion discharge.

Certain debts that might be discharged following successful plan completion may survive a hardship discharge.

The debtor should compare the consequences before requesting relief.

31. Why Completing the Plan Matters

The financial benefit of Chapter 13 may extend beyond the amounts paid through the trustee.

A debtor may complete a plan in which some unsecured creditors receive only partial distributions and others receive none because they failed to file timely claims.

Upon entry of discharge, qualifying remaining personal liabilities may be eliminated.

Dismissal before discharge can leave those obligations enforceable.

The discharge—not the expiration of the claims deadline—is ordinarily the event that permanently eliminates qualifying remaining personal liability.

Conclusion

A Chapter 13 case may end through successful completion, dismissal, conversion, or hardship discharge. The consequences differ substantially. A debtor who cannot finish should compare modification, the converted estate, and the scope of hardship relief before choosing a course. Dismissal ordinarily leaves unpaid obligations enforceable and terminates the automatic stay. Payments already made and funds still held by the trustee require separate accounting and legal analysis.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 501 — Filing proofs of claim.
- 11 U.S.C. § 502 — Allowance and disallowance of claims.
- 11 U.S.C. § 348 — Effect of conversion.
- 11 U.S.C. § 349 — Effect of dismissal.
- 11 U.S.C. § 1307 — Conversion and dismissal.
- 11 U.S.C. § 1328 — Ordinary and hardship discharge.
- 11 U.S.C. § 1329 — Modification.
- Federal Rule of Bankruptcy Procedure 3002 — Proof-of-claim deadlines.
- Federal Rule of Bankruptcy Procedure 3004 — Claims filed by debtors or trustees.
- Federal Rule of Bankruptcy Procedure 1019 — Procedures following conversion.

Selected decisions

- *Harris v. Viegelahn*, 575 U.S. 510 (2015) — Addresses undistributed postpetition wages following conversion from Chapter 13 to Chapter 7.
- *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010) — Addresses the binding effect of confirmed plans and procedural requirements.
- *Rake v. Wade*, 508 U.S. 464 (1993) — Discusses claims provided for by a Chapter 13 plan.
- *In re Arnold*, 869 F.2d 240 (4th Cir. 1989) — Addresses postconfirmation modification.
- *In re Murphy*, 474 F.3d 143 (4th Cir. 2007) — Addresses changed circumstances and plan modification.

Maryland practice

- United States Bankruptcy Court for the District of Maryland — Local Rules, claims register, and Chapter 13 procedures.
- National Data Center — Online access to payment and distribution information for participating Chapter 13 trustees.

Chapter 13 Proofs of Claim: Filing Deadlines, Missing Creditors, Claim Objections, and How Debts Can Be Discharged Without Payment

Belsky Bankruptcy Legal Library | Chapter 13 Bankruptcy

By Alan J. Belsky, Attorney at Law

A Creditor Can Lose the Right to Be Paid Without the Underlying Debt Immediately Disappearing

One of the less widely understood features of Chapter 13 bankruptcy is that a creditor may lose its right to receive payments because it failed to file a timely proof of claim.

A debtor may list a $25,000 credit card balance, provide proper notice to the creditor, and complete a Chapter 13 plan without the creditor receiving a dollar.

If the debt is covered by the debtor's eventual discharge, the remaining personal liability may be eliminated.

But the creditor's failure to file a claim does not itself discharge the debt.

The distinction is important.

A proof of claim establishes the creditor's asserted right to participate in distributions from the bankruptcy estate. Discharge determines whether the debtor remains personally liable after the bankruptcy case.

Chapter 13 debtors and their attorneys should pay close attention to claims deadlines, the claims register, and the treatment of creditors that do not participate.

The results can materially affect the amount needed to complete a plan.

1. What Is a Proof of Claim?

A proof of claim is a written statement asserting a creditor's claim against the debtor or bankruptcy estate.

Under § 501 and Federal Rule of Bankruptcy Procedure 3001, the claim generally identifies the creditor, amount owed, and nature of the obligation.

The creditor may assert secured, priority, or general unsecured status.

Supporting documents may be required.

A proof of claim is not necessarily conclusive.

It may be challenged under the applicable claims-allowance procedures.

2. Why Proofs of Claim Matter in Chapter 13

The Chapter 13 trustee ordinarily distributes funds on allowed claims according to the confirmed plan.

A creditor generally must file a timely proof of claim to receive distributions, subject to applicable exceptions.

The debtor's schedules identify creditors and obligations, but scheduling a debt does not automatically establish an allowed claim for distribution.

The claims process determines which creditors participate and in what amounts.

3. The General 70-Day Deadline

Under Rule 3002(c), nongovernmental creditors in an ordinary Chapter 13 case generally must file proofs of claim within seventy days after the order for relief.

In a voluntary case, the petition date ordinarily constitutes the order for relief.

The deadline is not generally calculated from the date of the § 341 meeting.

Certain exceptions and extensions apply.

The debtor should verify the actual deadline established in the case.

4. Governmental Creditors Generally Have 180 Days

Governmental units generally have 180 days after the order for relief to file proofs of claim.

The IRS, Maryland Comptroller, and other qualifying governmental creditors may therefore have a longer filing period.

For a claim resulting from a return filed under § 1308, Rule 3002(c)(1) permits filing within 180 days after the order for relief or within 60 days after the return is filed, whichever deadline allows the timely filing. A governmental unit may also seek a for-cause extension by motion before its time expires.

The debtor should not assume that the ordinary 70-day deadline applies to every creditor.

5. The Claims Bar Date

The deadline for filing proofs of claim is commonly called the *claims bar date*.

The bankruptcy court's notice ordinarily identifies applicable deadlines.

The debtor should preserve the notice and verify the dates.

A claim filed after the bar date may be subject to disallowance.

However, the applicable rules contain exceptions.

The debtor should not assume that every late-filed claim is automatically invalid without examining the governing provisions.

6. What Happens If a Credit Card Company Does Not File?

Assume a debtor lists a $22,000 credit card debt.

The creditor receives proper notice but does not file a proof of claim.

Neither the debtor nor trustee files a claim on the creditor's behalf.

The creditor ordinarily will not receive Chapter 13 distributions on that claim.

If the debtor completes the plan and receives a discharge covering the obligation, the remaining personal liability generally is eliminated.

The creditor's failure to file may therefore produce a substantial benefit.

7. The Debt Does Not Disappear on the Bar Date

The missed claims deadline does not automatically extinguish the underlying debt.

If the Chapter 13 case is dismissed before discharge, the creditor may retain an enforceable obligation under applicable law.

The debtor may still face collection after dismissal.

The creditor's inability to participate in the bankruptcy distributions is different from elimination of personal liability.

The ordinary Chapter 13 discharge is generally the event that provides lasting relief.

8. Section 1328(a)

Section 1328(a) generally provides for discharge of qualifying debts provided for by the plan or disallowed under § 502, subject to statutory exceptions.

A debt may be provided for by the plan even though the creditor receives no distribution because no allowed claim was filed.

However, proper notice and the nature of the debt matter.

A debtor should not assume that merely listing a creditor guarantees discharge in every circumstance.

9. Nondischargeable Debts

Some debts survive Chapter 13 discharge.

Examples include qualifying domestic support obligations, student loans absent undue hardship, certain taxes, and other statutory exceptions.

A creditor's failure to file a proof of claim generally does not make a nondischargeable debt dischargeable.

The debtor may finish the plan and still owe the obligation.

This distinction can make it beneficial to ensure that certain creditors receive payments during the case.

10. Secured Creditors

A secured creditor may possess a lien against real estate, a vehicle, or other property.

Rule 3002(a) provides that a lien is not void solely because the creditor failed to file a proof of claim.

A mortgage lender that misses the claims deadline may therefore retain its lien.

The debtor should not assume that the missed deadline eliminates the mortgage.

The creditor's right to plan distributions and its surviving lien rights must be distinguished.

11. Why a Debtor Might File a Claim for a Mortgage Lender

A debtor may need to cure mortgage arrears through the Chapter 13 plan.

If the lender fails to file a claim, the debtor may wish to file one on the lender's behalf.

Otherwise, the arrearage cure may not be administered as anticipated.

The debtor should review the applicable claim documents and filing requirements.

A debtor seeking to save a home should not assume that a missing mortgage claim is necessarily beneficial.

12. Rule 3004: Filing a Claim for a Creditor

Under § 501(c) and Rule 3004, the debtor or trustee may file a proof of claim on behalf of a creditor that failed to file timely.

The debtor or trustee generally has thirty days after the creditor's deadline.

The procedure can be useful for secured or nondischargeable obligations.

However, filing a claim for an ordinary dischargeable unsecured creditor may increase required distributions in some plans.

The decision should be made strategically and lawfully.

13. Priority Tax Claims

A governmental tax creditor may hold a priority or nondischargeable claim.

The debtor may want the obligation paid through the plan.

If the taxing authority does not file a claim, the debtor should evaluate whether a debtor-filed claim is appropriate.

The debtor should not assume that failure to file automatically eliminates the tax.

The debt's priority and dischargeability must be determined separately.

14. Domestic Support Obligations

Domestic support obligations generally receive special priority and are nondischargeable.

The debtor may need to address arrears through the plan.

The creditor's failure to file does not necessarily eliminate the debtor's obligation.

The debtor should ensure that the plan and claims administration properly address qualifying support obligations.

15. Late-Filed Claims

Section 502(b)(9) generally permits disallowance of untimely claims, subject to statutory and procedural exceptions.

A creditor may file a claim after the deadline.

The debtor or trustee may need to object.

The court determines whether the claim is allowable.

The debtor should not assume that a late-filed claim will automatically be removed from the claims register.

16. Can the Court Extend the Deadline?

Rule 3002(c) provides specified circumstances in which the filing period may be extended.

The court's authority is limited by the rule and other applicable provisions.

A creditor should not assume that ordinary neglect automatically justifies an extension.

Rule 3002(c)(7) permits a creditor to move before or after expiration for an extension of no more than 60 days after the court's order where notice was insufficient to give a reasonable time to file. Rule 3002(c)(6) separately permits specified principal-residence claim documentation to follow within 120 days, provided the proof of claim and the required mortgage attachment were filed within 70 days. Those are distinct exceptions, not an unrestricted excusable-neglect extension.

The debtor should review the particular basis for any requested extension.

17. Claims Filed Without Adequate Documentation

Rule 3001 requires specified information and documentation for certain claims.

A creditor may fail to attach required documents.

The consequences depend on the nature of the omission and applicable provisions.

A deficient claim is not necessarily disallowed automatically.

The debtor may seek appropriate relief or object when a legal basis exists.

The creditor may have an opportunity to provide additional documentation.

18. The Prima Facie Effect of a Proof of Claim

Under Rule 3001(f), a proof of claim executed and filed in accordance with the rules constitutes prima facie evidence of the validity and amount of the claim.

That evidentiary effect may be challenged.

A debtor who objects should identify a factual or legal basis.

A mere statement that the debtor disputes the debt may not be sufficient.

The burden of proof depends on the claim and applicable law.

19. Objecting to a Claim

Section 502 governs allowance and disallowance of claims.

A debtor may object because the amount is incorrect, the debt was paid, the claim is unenforceable, or another statutory basis exists.

The objection must comply with applicable procedural requirements.

The creditor may respond.

Rule 3007 ordinarily requires the objection and prescribed notice to be filed and served at least 30 days before the hearing or the deadline to request one. Serve the claimant's designated notice recipient and comply with the special rules for the United States and insured depository institutions. Relief of a type requiring an adversary proceeding may not simply be added to a claim objection. The court determines whether the claim should be allowed, reduced, or disallowed.

20. Duplicate Claims

A debtor may discover that both an original creditor and debt purchaser filed claims concerning the same obligation.

The claims register should be reviewed for duplication.

The debtor may need to determine which entity owns the debt.

Duplicate payment should not occur merely because multiple claims were filed.

Appropriate objections or amendments may be necessary.

21. Claims That Are Larger Than Scheduled

A creditor may file a claim exceeding the amount listed in the debtor's schedules.

For example, a credit card company may claim $18,000 when the debtor scheduled $13,000.

The difference may reflect interest, fees, or other charges.

The debtor should obtain supporting information.

The filed claim may affect distributions unless successfully challenged.

The scheduled amount does not automatically control.

22. Claims That Are Smaller Than Scheduled

A creditor may file a claim for less than the debtor anticipated.

The smaller allowed amount may reduce the total required distribution under some plans.

However, the effect depends on the plan structure.

The debtor should not automatically reduce trustee payments.

The confirmed plan and other statutory requirements remain controlling.

23. Percentage Plans

A percentage plan may provide that general unsecured creditors receive a specified percentage of allowed claims.

For example, a plan may provide for payment of 25% of allowed unsecured claims.

If fewer claims are allowed than anticipated, the total required distribution may be lower, subject to the plan and other statutory requirements.

The debtor's payment obligation may still be governed by projected disposable income or liquidation value.

24. Pot Plans

A pot plan generally commits a fixed amount for distribution to a class of creditors.

For example, the debtor may be required to pay $30,000 to general unsecured creditors.

If some creditors fail to file claims, the remaining allowed creditors may receive larger percentages.

The total required distribution may remain unchanged.

The debtor should determine which plan structure applies.

25. Example: Missing Claims in a Percentage Plan

Assume the debtor schedules $120,000 in general unsecured debts.

The plan provides for payment of 20% of allowed claims.

Creditors holding $40,000 fail to file timely claims.

Only $80,000 in qualifying claims are allowed.

A 20% distribution would total $16,000 rather than $24,000.

However, the debtor must still satisfy disposable-income, liquidation-value, and other plan requirements.

The $8,000 difference does not automatically become money the debtor may retain.

26. Example: Missing Claims in a Pot Plan

Assume the plan requires $24,000 for general unsecured creditors.

Only $80,000 in claims are allowed instead of the anticipated $120,000.

The $24,000 distribution would represent 30% of the allowed claims.

The debtor may still be required to fund the entire $24,000.

The creditors that filed timely receive a larger percentage.

27. Why the Claims Register Should Be Reviewed

The claims register identifies claims filed in the case.

Counsel should compare it with the debtor's schedules and plan.

The review should identify missing claims, late claims, duplicate claims, incorrect amounts, and disputed secured or priority status.

The debtor should not assume that the trustee will object to every defective claim.

A timely claims review can materially affect the plan.

28. When Should the Claims Review Occur?

An initial review should occur as claims are filed.

A more comprehensive review should occur after the applicable nongovernmental and governmental claims deadlines.

The attorney should determine whether any debtor-filed claims are needed.

The plan may require amendment if allowed claims differ materially from anticipated amounts.

The review should not be postponed until the debtor approaches completion.

29. Claims After Conversion

If a Chapter 13 case converts to Chapter 7, § 348 and Rule 1019 govern important procedural consequences.

The claims process may change.

The debtor should not assume that a creditor's failure to file a Chapter 13 claim permanently bars participation in every later bankruptcy proceeding.

The applicable rules and conversion circumstances control.

30. Claims After Dismissal

Dismissal generally ends the Chapter 13 case without the ordinary discharge.

A creditor that failed to file a claim may still possess an enforceable obligation under nonbankruptcy law.

The missed claims deadline generally does not eliminate the debt outside bankruptcy.

The debtor should understand that the benefit of an unfiled claim may depend on successful completion and discharge.

31. The Importance of Accurate Creditor Notice

A debtor must accurately identify creditors and provide required notice.

Failure to list a creditor or provide a proper address may affect dischargeability and due process rights.

The debtor should not deliberately omit creditors to cause them to miss filing deadlines.

The bankruptcy process requires full and accurate disclosure.

The potential benefit of a missed claim arises from lawful application of the rules, not concealment.

Additional original claims discussion preserved from the combined manuscript

An equally important issue arises when creditors fail to file proofs of claim. A creditor may be listed in the bankruptcy schedules but receive no distributions because it failed to submit a timely claim.

In a successfully completed Chapter 13 case, the remaining personal liability on many such debts may be discharged even though the creditor received nothing.

But a creditor's failure to file a proof of claim does not, by itself, extinguish the debt. The outcome depends on the claim's legal character, the applicable deadlines, notice, lien rights, and whether the debtor ultimately receives a discharge.

Understanding the distinction between claims allowance, plan distributions, and discharge is essential.

Proofs of Claim: Why Filing Deadlines Matter

A proof of claim is the formal document through which a creditor asserts a right to payment in the bankruptcy case.

The creditor generally identifies the amount owed, the nature of the obligation, and any asserted security interest or priority.

A claim that is properly filed may be allowed under § 502 unless an appropriate objection or other basis for disallowance applies.

But a creditor that fails to file a required proof of claim by the applicable deadline may lose the right to receive distributions.

This can have substantial consequences in Chapter 13, particularly for general unsecured creditors.

The General Creditor Deadline: 70 Days

Under Federal Rule of Bankruptcy Procedure 3002(c), a nongovernmental creditor in an ordinary Chapter 13 case generally must file its proof of claim within 70 days after the order for relief.

In a voluntary case, the petition date ordinarily constitutes the order for relief.

This deadline is different from the former rule that measured the claims period from the first scheduled meeting of creditors.

Certain exceptions apply, including provisions concerning mortgage claim documentation and other specified circumstances.

Example: A Credit Card Company Misses the Deadline

Assume a debtor lists a $19,000 credit card debt and properly provides notice to the creditor.

The creditor fails to file a proof of claim within the applicable period.

No qualifying exception applies, and neither the debtor nor trustee files a claim on its behalf.

The creditor generally cannot receive distributions on that claim.

If the debtor successfully completes the Chapter 13 plan and receives a discharge covering the obligation, the remaining personal liability ordinarily is eliminated.

The creditor's failure to file may therefore mean that a substantial debt is discharged without the creditor receiving any payment.

That is an important practical benefit of Chapter 13.

Governmental Creditors Generally Have 180 Days

Governmental units ordinarily have a longer period to file proofs of claim.

Under Rule 3002(c)(1), the general governmental deadline is 180 days after the order for relief.

Special rules apply to certain claims arising from tax returns filed under § 1308, including an alternative deadline measured from the filing of the return.

A debtor should not assume that the ordinary 70-day deadline applies to the IRS, Maryland Comptroller, or another qualifying governmental unit.

Can a Late Proof of Claim Be Disallowed?

Yes.

Section 502(b)(9) generally provides a basis for disallowing untimely claims, subject to statutory and procedural exceptions.

A creditor that misses the deadline may lose the right to participate in Chapter 13 distributions.

The debtor or another party in interest may need to file a claim objection.

A late-filed claim should not simply be ignored if it has been entered on the claims register.

The court's claims-allowance procedures must be followed.

Can the Debtor File a Claim for a Creditor?

Yes.

Under § 501(c) and Rule 3004, the debtor or trustee may file a proof of claim on behalf of a creditor that failed to file timely.

The debtor or trustee generally has 30 days after the creditor's filing deadline to do so.

This can be particularly important when the debtor wants a claim paid through the plan.

For example, a debtor curing mortgage arrears may have a strong interest in ensuring that the lender's claim is properly administered.

Likewise, filing a claim for a nondischargeable creditor may help address an obligation that would otherwise survive the bankruptcy.

Why Would a Debtor File a Claim for a Creditor Who Failed to File?

At first glance, it may seem counterproductive to file a claim for a creditor that missed its deadline.

But there are circumstances in which doing so benefits the debtor.

A mortgage lender may need to receive arrearage payments to complete a cure.

A tax creditor may hold a nondischargeable obligation that the debtor wants paid during the plan.

A creditor may possess a surviving lien.

The debtor should distinguish creditors whose claims may be discharged without payment from creditors whose unpaid obligations could create serious problems after bankruptcy.

Secured Creditors and Surviving Liens

Rule 3002(a) expressly provides that a lien is not void solely because a creditor failed to file a proof of claim.

This is a critical distinction.

A vehicle lender or mortgage creditor may fail to file a claim but retain an otherwise valid lien.

The debtor should not assume that the missed claims deadline eliminates the security interest.

The creditor's right to receive plan distributions and its right to enforce collateral are separate matters.

Nondischargeable Debts Do Not Disappear Merely Because No Claim Was Filed

Some debts survive Chapter 13 discharge under § 1328(a).

Examples include qualifying domestic support obligations, certain taxes, student loans absent undue hardship, and other specified obligations.

A creditor's failure to file a proof of claim generally does not transform a nondischargeable debt into a dischargeable one.

The debtor may complete the plan and still owe the obligation.

This is why claims review should distinguish dischargeable unsecured debts from debts that will survive.

The Importance of Proper Notice

A creditor must receive legally sufficient notice of the bankruptcy and applicable proceedings.

Section 523(a)(3), incorporated into Chapter 13 discharge through § 1328(a), may affect debts when a creditor was not properly listed or notified in time to protect its rights.

The debtor should not deliberately omit a creditor or provide an incorrect address in the hope that the creditor will miss the deadline.

A discharge obtained through concealment or improper notice can create serious legal problems.

The objective is accurate disclosure and lawful administration, not manipulation of the claims process.

What Does “Provided for by the Plan” Mean?

Section 1328(a) generally discharges qualifying debts provided for by the plan or disallowed under § 502, subject to statutory exceptions.

The phrase *provided for by the plan* is important.

A debt may be addressed by the plan even though the creditor ultimately receives no distribution because it failed to file a claim.

But the plan, notice, and statutory requirements must be examined.

The Supreme Court discussed the meaning of plan treatment in *Rake v. Wade*, 508 U.S. 464 (1993), in the context of mortgage claims.

The debtor should not assume that merely listing a creditor somewhere in the schedules resolves every discharge question.

How Unfiled Claims Can Benefit Other Creditors

When a creditor fails to file a timely claim, the effect on other creditors depends on the plan's structure.

In a plan committing a fixed amount to general unsecured creditors, the absence of one claim may increase the percentage distributed to other allowed unsecured claims.

In a plan requiring payment of a specified percentage, the absence of a claim may reduce the total amount necessary to satisfy that distribution requirement, subject to the plan and other confirmation obligations.

The debtor's payment obligation does not necessarily decrease automatically.

The confirmed plan controls.

Example: A Creditor Misses the Deadline in a Percentage Plan

Assume a confirmed plan provides for payment of 20% of allowed general unsecured claims.

The debtor schedules $100,000 in unsecured debt.

One creditor holding a $30,000 claim fails to file timely, and no claim is filed on its behalf.

Assuming only $70,000 in qualifying unsecured claims are allowed, a 20% distribution would equal $14,000 rather than $20,000.

However, the debtor cannot automatically reduce plan payments by $6,000.

The disposable-income requirement, liquidation test, plan language, and other obligations must still be satisfied.

Example: A Creditor Misses the Deadline in a Pot Plan

A plan may instead provide a fixed total distribution to unsecured creditors.

Assume the plan requires $25,000 for allowed general unsecured claims.

If one creditor fails to file, the remaining allowed creditors may receive a larger percentage of their claims.

The total required unsecured distribution may remain $25,000.

Thus, a creditor's failure to file does not necessarily create savings for the debtor.

The effect depends on how the plan was confirmed.

Reviewing the Claims Register

The claims register identifies proofs of claim filed in the bankruptcy case.

Counsel should compare it with the debtor's schedules and the confirmed plan.

The review should identify missing claims, duplicate claims, late claims, unexpected secured or priority designations, and amounts that appear incorrect.

The debtor should not assume that the trustee will automatically object to every defective claim.

Claims review is an important part of Chapter 13 representation.

Why the Claims Deadline Can Change the Plan

The claims deadline may materially change the amount required to complete a Chapter 13 plan.

A debtor may initially anticipate substantial distributions to creditors that never file claims.

Conversely, unexpected priority or secured claims may increase required funding.

The attorney should revisit the plan after the applicable claims deadlines have passed.

The debtor may benefit from a modification, claim objection, or other appropriate action.

Dismissal Before Discharge Changes Everything

A debtor may complete several years of payments and benefit from creditors' failure to file claims.

But if the case is dismissed before discharge, the debtor ordinarily does not receive the benefit of discharge under § 1328(a).

A creditor that failed to file a proof of claim may still possess an enforceable debt under applicable nonbankruptcy law.

The missed bankruptcy deadline generally does not extinguish the underlying obligation outside the bankruptcy case.

This is one of the most important reasons to complete the plan whenever reasonably possible.

Conversion to Chapter 7

If the debtor converts to Chapter 7, the Chapter 13 claims process does not simply continue unchanged.

The treatment of previously filed claims and additional filing requirements depends on § 348 and Rule 1019.

The debtor's discharge will be governed by Chapter 7 rather than the ordinary Chapter 13 discharge provisions.

A creditor's failure to file a Chapter 13 claim does not independently establish that its debt will be discharged after conversion.

A Chapter 13 case may end through successful completion, dismissal, conversion, or hardship discharge.

The consequences differ substantially.

The proof-of-claim process adds another important dimension. Nongovernmental creditors generally have 70 days after the order for relief to file claims, while governmental units generally have 180 days, subject to exceptions.

A creditor that misses the applicable deadline may receive no distribution.

If the debtor successfully completes the plan and obtains a discharge, the remaining personal liability on many such obligations may disappear.

But valid liens and nondischargeable debts can survive, and dismissal ordinarily eliminates the opportunity for an ordinary Chapter 13 discharge.

The practical lesson is that a missed claims deadline can benefit a Chapter 13 debtor, but successful plan completion is usually what makes that benefit permanent.

Conclusion

Proofs of claim determine which creditors may participate in Chapter 13 distributions.

Nongovernmental creditors generally must file within seventy days after the order for relief, while governmental units generally have 180 days, subject to exceptions.

A creditor that misses the applicable deadline may receive nothing through the plan.

If the debtor completes the plan and receives a discharge, qualifying remaining personal liability may be eliminated.

But liens and nondischargeable debts may survive, and dismissal ordinarily leaves unpaid obligations enforceable.

A careful review of the claims register after the filing deadlines can identify opportunities to reduce unnecessary distributions, correct claims, and improve the likelihood of successfully completing Chapter 13.

Related Bankruptcy Cases and Authorities

Federal statutes and rules

- 11 U.S.C. § 501 — Filing proofs of claim.
- 11 U.S.C. § 502 — Claims allowance and disallowance.
- 11 U.S.C. § 1328 — Chapter 13 discharge.

- 11 U.S.C. § 348 — Effect of conversion.
- Federal Rule of Bankruptcy Procedure 3001 — Proof-of-claim requirements.
- Federal Rule of Bankruptcy Procedure 3002 — Filing deadlines.
- Federal Rule of Bankruptcy Procedure 3004 — Claims filed by debtors or trustees.
- Federal Rule of Bankruptcy Procedure 1019 — Procedures following conversion.

Selected decisions

- *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010) — Addresses the binding effect of confirmed plans and procedural requirements.
- *Rake v. Wade*, 508 U.S. 464 (1993) — Addresses claims provided for by a Chapter 13 plan.
- *Midland Funding, LLC v. Johnson*, 581 U.S. 224 (2017) — Addresses filing a proof of claim for a time-barred debt.
- *Harris v. Viegelahn*, 575 U.S. 510 (2015) — Addresses funds held following conversion from Chapter 13.
- *In re Pajian*, 785 F.3d 1161 (7th Cir. 2015) — Addresses proof-of-claim deadlines for secured creditors under the prior version of Rule 3002; current rule must be applied.

Maryland practice authorities

- United States Bankruptcy Court for the District of Maryland — Claims register and local bankruptcy procedures.
- National Data Center — Chapter 13 trustee payment and distribution information for participating trustees.