

## CHAPTER 7, 11 AND 13 BANKRUPTCY EXPLANATIONS & TERMINOLOGY

This section will contain most of the terminology that a credit grantor needs to know. Included in the explanations are homestead allowances, the plan of reorganization, involuntary petition, motions, post-petition debt, administrative claim, trustee, dismissed, discharged and debtor-in-possession.

**FILING FOR RELIEF** – Any individual or business entity may seek relief by filing a Chapter 7, 11 or 13 bankruptcy. Under bankruptcy law, collection efforts after being informed of or receiving a notice are prohibited. Creditors may intercede in the bankruptcy by retaining counsel to represent their interest by filing “Motions” in the Bankruptcy Court for consideration by the bankruptcy judge. Typically, bankruptcies are handled by the filing of Motions and the bankruptcy judge rules on such motions. All creditors, debtors and other parties in interest are supposed to receive copies of Motions scheduled to be heard in the Bankruptcy Court. The Motions are supposed to be directed to all parties well in advance of the Motion date.

**CHAPTER 7** – A Chapter 7 bankruptcy is known as a liquidation bankruptcy. All forms of businesses and individuals may file a Chapter 7. A Trustee is appointed in all Chapter 7’s. The Trustee is usually an attorney but this is not a requirement. The Trustee is a court advocate protecting the interest of all creditors. Upon appointment, the Trustee will review the books and records of a debtor and automatically, whether justified or not, request that all payments that the debtor made within 90 days prior to the date of the bankruptcy filing be returned to the Bankruptcy Court for distribution. The Trustee receives compensation based on a percentage of all assets that flow through the Bankruptcy Court. The Trustees’ claim that a “preferential payment” is returned can be fought if certain defenses are raised. For more about these defenses see [Defenses to Bankruptcy Preference Claims](#).

**EXEMPTIONS** – Exemptions are allowed in bankruptcies. Most states follow the federal guidelines, which include equity in the primary living residence of \$7,500.00 (\$15,000.00 on a joint spousal bankruptcy filing). The bankruptcy law allows states to add homestead provisions. The state of Texas allows the primary residence designated for living purposes with an unlimited value. The state of Florida has the same primary residence exemption. Both the states of Texas and California allow for other more liberal exemptions in addition to the federal guidelines. Some states protect a certain percentage of wages and income. Also, there are allowances for transportation, furniture and other living expenses.

**CHAPTER 11** – A Chapter 11 is known as a bankruptcy reorganization with a “debtor-in-possession.” The purpose of a Chapter 11 is an order for business entities to file a plan of reorganization within 120 days of the bankruptcy filing. In a Chapter 7, the debtor serves in the role of the Trustee. No Trustee is appointed unless the debtor requests a Trustee. Unlike a Chapter 7, a Trustee is not a mandatory element of a Chapter 11. A debtor has 120 days to file a plan of reorganization with the Bankruptcy Court. After that time, if no plan has been filed, the Bankruptcy Court can move to have the Chapter 11 converted to a Chapter 7. It is rare, but allowed, that business proprietorships and business partnerships be reorganized under a Chapter 11; however, the Schedule of Assets must include all personal holdings and assets. It is not uncommon that a debtor liquidates under the guise of a Chapter 11. In other words, a Chapter 11

is filed and instead of reorganization, the debtor liquidates assets during the 120 days where the debtor is supposed to be formulating a plan of reorganization.

**INVOLUNTARY CHAPTER 7** – One large creditor or three small creditors may petition a debtor into a Chapter 7 bankruptcy. The debtor has the option of responding by Motion to convert the Chapter 7 to a Chapter 11. Bankruptcy judges always allow this.

**CONVERSION OF A CHAPTER 11 TO A CHAPTER 7** – A debtor in a Chapter 11 is supposed to pay post-petition debt within terms. If these terms are violated, the creditor has the right to file a Motion to have the Chapter 11 converted to a Chapter 7, or file suit on the post-petition amount. Post petition creditors are afforded the same rights as if the Chapter 11 was never filed.

**MOTIONS TO RECOVER SECURED INVENTORY** – A creditor may file a Motion in the Bankruptcy Court stating that terms were breached and they are entitled to have their inventory back since title has not transferred. Typically, these Motions are allowed unless the inventory is deemed as “a necessity” for the continued operation of the business in which the petitioner in bankruptcy would have to make allowances to pay for said secured inventory.

**GROUND TO CONVERT TO A CHAPTER 7** – If the debtor fails to act as required in a Chapter 11 or Chapter 13 bankruptcy, then the grounds exist to file a Motion to have the Chapter 11 or 13 converted to a Chapter 7.

**ADMINISTRATIVE CLAIM** – An Administrative Claim is a preferred category of claim. Administrative Claims are paid before there are any distributions in bankruptcy. Administrative Claims include COD transactions and in some states NSF checks are allowed as Administrative Claims.

**CHAPTER 13** – A Chapter 13 is known as wage earner reorganization. The debtor repays debt from wages or income. The purpose of the Chapter 13 is to repay all debt or whatever plan is filed and accepted by creditors. The type of party seeking relief under a Chapter 13 would be proprietorships, all partners in a partnership or individuals that wish to address debt by means of their income and wages.

**DISMISSED AND DISCHARGED** – These are the two all-important D’s of bankruptcy. Dismissed means that the parties seeking relief under bankruptcy no longer come under the jurisdiction of the Bankruptcy Court. The Bankruptcy Court is no longer involved, which means that creditors may pursue all parties dismissed from the Bankruptcy Court and take whatever collection efforts are available. Discharged means the debtor has fulfilled all obligations under bankruptcy and the debtor has been absolved from all debt by following the bankruptcy plan. There is a time limitation when a debtor can seek relief again under bankruptcy.

**MOTIONS** – Motions conduct all bankruptcy activity. This is not considered to be a normal collection matter. Williams & Williams, Inc. can refer a client to an attorney to file a Bankruptcy Motion to protect their interest. Typically, there is an hourly charge for this and they flow together with a rough estimate of hours needed to accomplish the objective and the Motion should be considered.