

WHAT
CAN I DO
IF I CAN'T
PAY MY
DEBTS?

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What can I do if I can't pay my debts?

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1 *Can my property be taken to pay a debt?*

Yes, under certain circumstances. A *creditor*—the person or company that says you owe a debt—usually must go to court and win a lawsuit against you before taking your property. Let's say, however, you make a written promise to either pay your debt or give the creditor something you own. The item you promise to give is called the *security*, and the money you owe is called a *secured debt*. If you fail to pay a secured debt, the creditor usually can take the security.

Let's say you borrow money to buy a car and the car is the security. If you fall behind in your payments, the lender can *repossess* (take back) the car without going to court. The car must, however, be on public property when it is repossessed. And even if the car is repossessed, you could still wind up owing the lender money. Suppose, for example, you owe \$8,000 on the car when it is repossessed and the lender sells the car at an auction for \$7,000. You could be sued for the \$1,000 that the lender is out—plus any money spent to repossess the car and sell it.

Companies that repair or store items also can take property from you without going to court. For example, if a shop cleans your rug and you do not pick it up and pay for the cleaning, the shop can keep the rug and sell it after a certain period of time.

2 *Can my creditors harass me?*

Creditors or *collection agencies*—companies that try to collect payment for past due bills—cannot, by law, repeatedly call you on the telephone. It is also against the law for them to threaten you with harm or contact you at work if you have told them not to. And if you ask them, in writing, to stop contacting you, they must leave you alone. At that point, they can only contact you to inform you that they are filing a lawsuit. Be sure to keep copies of all correspondence.

Creditors and collection agencies are not supposed to contact your employer either, except to make sure that you are employed. And they cannot send you anything that is meant to look like a legal document if it is not.

If you are bothered in any of these ways, contact a consumer protection or law enforcement agency. Or you could seek a lawyer's help.

3 *Can I be forced to pay someone else's debts?*

Yes, in some instances. For example, if your spouse obtains a necessity of life—such as food, clothing or medical care—and cannot pay for it, you can be forced to pay. This may be true for a former spouse, too, if you were not separated when your spouse got into debt.

In most cases, people under age 18 can get out of an agreement to buy something. If, however, you are an adult and you co-sign a contract or loan agreement for someone under 18 (or for anyone else, for that matter), you would be responsible for the debt. This means you have promised to make the payments if the other person fails to live up to the agreement.

What if you co-sign an agreement for someone who ends up filing for bankruptcy? The other person may not have to pay the debt, but you will.

In addition, you legally may have to pay certain debts, such as medical bills, for your minor child.

4 *What should I do if I'm billed for something I didn't buy?*

Try to settle the problem as soon as possible. If you get a bill for something that you didn't agree to buy, write to the creditor. Do the same thing if you don't believe you received everything for which you have been billed. Keep copies of all your letters.

If you can't work the situation out on your own, seek out a consumer protection agency. Look in the white pages of your telephone directory under "Consumer Complaint and Protection Coordinators." Or, call the state Department of Consumer Affairs toll-free at 1-800-952-5210 or contact them by email at dca@dca.ca.gov to find out who might be able to assist you with your particular problem. Or go to dca.ca.gov.

Or you may want to consult a lawyer (see #16), because most debts are based on a *contract*—a

legally binding agreement that can be written or spoken.

In any case, take action immediately. It could turn out that you owe a debt and, if you do not respond, you could end up with serious money and legal problems.

5 *Can other people find out about my debts?*

Yes. If you don't pay your bills, you can end up with a bad credit rating, which is a report on your financial situation. Credit ratings are issued by credit-reporting agencies. These companies get information about your debts from your creditors, and they make their reports available to other creditors, employers and landlords.

A credit report includes such information as whether you pay your bills on time, have had a foreclosure, owe money as the result of a lawsuit or were convicted of a crime. Each piece of information stays in the report for a certain number of years. For example, a bankruptcy usually will be listed for 10 years.

What if a store refuses to give you a charge account because you have a bad credit rating? The store must give you the name and address of the credit-reporting agency that made the report, and the agency must let you see the report.

If you tell the agency that some of the information in the report is wrong, it must look into the matter. If the agency decides that its report is correct, you can explain your side of the story in writing. Then, anyone who checks your credit rating will see your explanation. If you ask, the agency also must send your explanation to anyone who received your credit rating for employment purposes in the last two years and to anyone else who received your rating within the last six months.

It is a good idea to check your credit report periodically for errors, signs of identity theft or anything else that might affect your credit rating. By law, you are entitled to receive one free credit report from each of the three major credit bureaus each year. To order your free annual reports, call 1-877-322-8228 or visit the program's website at **annualcreditreport.com**.

6 *What happens if I am sued?*

If you have a secured debt (see #1), the creditor can sue you either to recover the security or for the amount of money you owe or both. If you do not have a secured debt, you will be sued for the money you owe.

If the debt is \$5,000 or less (up to \$7,500 if the creditor is an individual), the creditor might decide to take you to small claims court. You cannot be represented by a lawyer in this court, but you can talk to one beforehand. For more information, see the State Bar pamphlet *How Do I Use the Small Claims Court?*

Lawsuits for larger amounts are filed in a higher court, where it is best to have a lawyer represent you.

In any event, if you receive a court summons because you are being sued, do not ignore it. If you do not respond within a certain time, you will lose the case automatically – and your property or bank accounts can be taken without notice.

As soon as you receive a summons, you should:

- Consult a lawyer (see #16).
- Get in touch with the lawyer hired by the person suing you and try to negotiate, or work out, a way to settle the dispute.

You can try to negotiate a settlement even after the suit has been filed, but you should do so only if you have responded first in writing to the summons.

7 *What happens if I lose the lawsuit?*

It depends on the terms of the lawsuit. If the lawsuit demanded the return of a secured item, the creditor could get an order from the judge allowing a sheriff or marshal to take the item from you. Once this happens, your debt may be canceled.

If the suit demanded money and you do not pay the amount that the judge ordered you to pay, something you own could be *attached* (legally claimed as payment). The property – such as a car or bank account – would be about the same value as the amount of your debt. A car, for example, could be sold in order to pay the creditor. You may,

however, be able to keep certain items (see #8).

A judge also can order your employer to withhold up to 25 percent of your take-home earnings to pay a debt. This is called a *garnishment of wages*.

8 *Can I protect my property if I am sued?*

If you lose a lawsuit, you also may lose some of your property. The law, however, lets you claim that some property is exempt, which means that it cannot be taken from you.

When you receive a notice that your property is being attached, you have 10 days to deliver a *Claim of Exemption* form to the sheriff or marshal. This form describes the property and explains why it legally cannot be attached. Most sheriff, marshal and court clerk offices have these forms.

The creditor can either accept your claim or challenge it at a court hearing. At the hearing, you must prove that the property is exempt. If you do not go to the hearing, you automatically lose the exemption.

You cannot file a Claim of Exemption if your debt is for unpaid federal income taxes or for a necessity of life such as food, shelter or medical treatment. These debts must be paid.

However, among other things, you and your spouse together can claim exemptions for:

- Up to \$100,000 in equity in your home if you are part of a family unit (up to \$75,000 if you are single), and up to \$175,000 if you are 65 years old or older, disabled, or on a low income.
- A \$2,725 equity in one or more cars.
- Up to \$7,175 in tools and other items that you need for your work (or up to \$14,350 for items used by both spouses who do the same work).
- 75 percent of your salary for the last 30 days or wages that have not yet been paid.
- Up to \$7,175 worth of jewelry, heirlooms and works of art.

- Life insurance policies with a cash value of up to \$11,475. Married couples may combine this exemption; it doesn't matter whether the policies belong to you, your spouse or both of you.
- Up to \$1,425 in an inmate's trust account.
- Up to \$2,875 each in a bank account in which your Social Security payments have been directly deposited (\$4,300 if the one payment is directly deposited for the benefit of both spouses).

In addition, you and your spouse each can claim exemptions for:

- Household furnishings and clothing that your family needs.
- A cemetery plot.
- All or part of retirement, disability and health insurance, workers' compensation, welfare, unemployment, union and other benefits that are needed to support your family.

9 *What if I just need more time to pay my debts?*

You could contact your creditors and ask for more time to make payments. You might ask, for example, if you can make a series of small payments over a period of time. If any creditor agrees to such an arrangement, write a letter confirming the agreement and keep a copy of the letter.

It might help to contact a credit and debt counseling agency as well. Such services can sometimes help people work out plans with their creditors. However, shop carefully for one that you believe gives good advice. And keep in mind that if you wind up filing for bankruptcy, you will be *required* to complete such counseling from an agency approved by the U.S. Trustee Program. (See #10.)

Be careful about getting a debt consolidation loan to pay off your debts. If the *interest* (the money that lenders charge for loans) is too high, you may end up with a bigger problem. If you do get a loan, however, make sure all of the

financial statements that you give the lender are true and complete.

10 *When should I consider filing for bankruptcy?*

It depends on your particular set of circumstances. You should seek an attorney's advice before making such a decision. Filing for bankruptcy will impact your credit and may not wipe out all of your debts. If your creditors, however, will not give you more time to pay off your debts and you have no other good options, it may be the best way to begin turning your situation around.

Before filing for bankruptcy, you will have to complete credit counseling with a U.S. Trustee Program-approved agency. To locate such an agency, visit the program's website at [usdoj.gov/ust](https://www.usdoj.gov/ust) (go to *Consumer Information*, then *Credit Counseling & Debtor Education*). Keep in mind that credit counseling is required even if there is no possibility of setting up a repayment plan. If you fail to obtain the credit counseling and file the certificate with the court, your bankruptcy case will be dismissed without wiping out your debts. In addition, you will be required—once you have filed for bankruptcy—to complete a personal financial management course before any of your debts can be wiped out.

11 *Are there different types of bankruptcy?*

Yes. There are two types of personal bankruptcy: *Chapter 13* and *Chapter 7*. Chapter 13 allows you to stop most debt collection in exchange for your promise to pay your available funds to creditors according to a repayment plan (see #15). You can file a Chapter 13 bankruptcy in the nearest United States Bankruptcy Court. The repayment plan allows you to pay your debts over five years. It also allows you to keep your property as long as you continue to make payments. And at the end of the repayment period, most of your debts can be canceled—even if you have not paid them in full—as long as you make all the payments or fully perform your plan.

In filing for Chapter 7 bankruptcy, however, you are not seeking a repayment plan (see #12). Instead, you are asking the bankruptcy court to cancel most of your debts because you don't have enough money or property to pay them off. Certain assets (assets that are not exempt) would be sold to pay off your creditors.

To file Chapter 13 or Chapter 7, you must pay a filing fee in bankruptcy court, either alone or with your spouse. If you meet certain criteria, you may be able to file without paying the fee. Contact a lawyer to determine whether you meet the criteria. A trustee is appointed when you file your case.

Once you have filed for Chapter 13 or Chapter 7, the creditors you had before you filed (except those seeking child or spousal support payments) cannot attach your salary or other possessions as payment without bankruptcy court permission. Those seeking payment of child or spousal support debts, however, can attach your salary and your possessions—even your exempt property—if they obtained a court order from the family court before you filed for bankruptcy.

12 *When should I file for Chapter 7?*

If you can't work out any other reasonable way to pay your debts, you might consider filing for Chapter 7. It allows an honest debtor to make a fresh start by having a court *discharge* (in other words, cancel) most debts. Chapter 7 is a way to get out of debt when you owe more money than you can be expected to pay in a reasonable amount of time.

To qualify for a Chapter 7 bankruptcy, however, your income cannot exceed certain limits. If your income is greater than the median income in California, for example, you may not be eligible for this type of bankruptcy. You would be required to pass a "means" test to determine your eligibility. The purpose of such a test is to find out if you have enough income to participate in some sort of Chapter 13 repayment plan instead. If, after subtracting certain expenses and debt payments, your balance exceeds the monthly limit, you would not qualify for Chapter 7.

If you do file for Chapter 7, your appointed trustee will sell any of your property that is not exempt (see #14) and distribute the funds among

your creditors.

The law says that an employer can't fire you or refuse to hire or promote you because you filed for Chapter 7. Chapter 7 bankruptcy, however, can have a bad effect on your credit rating for a long time. Also, Chapter 7 may solve the problems you have now, but it won't protect you if you can't pay new bills. And keep in mind that your debts can be discharged through Chapter 7 only once in an eight-year period.

In filing for Chapter 7, you or your lawyer will have to file a number of forms and papers with the bankruptcy court. These include a list of your debts and property, plus information on your income and how you spend it. The court decides if you are better suited for Chapter 13 than Chapter 7 if requested to do so. In addition, your case can be dismissed.

Also, a judge can refuse to discharge all or some of your debts through Chapter 7. For example, if you run up a lot of bills on purpose or borrow money with a dishonest motive just before filing for bankruptcy, you may not be allowed to have your debts canceled.

13 *Will Chapter 7 wipe out all of my debts?*

No. Chapter 7 does not cancel:

- Any lien on personal or real property (the debt will be canceled, but you don't get to keep the security if you don't pay for it).
- Most income taxes incurred in the last three years.
- All student loans, unless you qualify for a hardship discharge.
- Child support and spousal support or property settlements.
- Any money that you owe as a result of injuring or killing someone while you were operating a motor vehicle, vessel or aircraft under the influence of alcohol, drugs, or another substance.

Your debts also will not be canceled if a creditor

proves that you lied about how much money you have, tried to hide property or committed fraud.

You may choose to *reaffirm* a secured debt. This means that you decide to pay the debt and keep the secured item, even though Chapter 7 would otherwise cancel the debt. If you do not reaffirm the debt and the contract allows repossession of the item because bankruptcy was filed, the item can be repossessed even if you are current on the payments.

14 *If I file for Chapter 7, can I keep any property?*

Yes, probably. If the property is exempt (see #8 and below), it cannot be used to pay off your debts – unless you owed spousal or child support when you filed for bankruptcy. Even exempt property can be used to pay spousal or child support claims. When you file for Chapter 7, you can choose between two sets of exemptions. To claim these exemptions, you must have lived in California for at least two years before filing for bankruptcy. (Otherwise, you would have to use the exemptions available in the state where you used to live.)

One set of exemptions is the same as the one you can use to protect your property from creditors in a lawsuit (see #8). Homeowners generally prefer this set because it allows a much larger home equity exemption than the other set. For some examples of what you and your spouse can keep if you choose the second set of exemptions, see below (the dollar amounts will change in April of 2013):

- A \$22,075 interest in a home and/or burial plot. If you do not own either one, you can apply this amount elsewhere to keep non-exempt property, such as an income tax refund. In addition, you have a \$1,175 *floating* exemption that can be applied to any non-exempt property.
- A \$3,525 interest in a car or other motor vehicle.
- All items (not to exceed \$550 in value in any one particular item) that are household furnishings and goods, clothing, appliances, books, crops and musical instruments.

- \$1,425 in jewelry.
- \$2,200 worth of books or tools that you need to earn a living.
- A life insurance policy that has not matured and cash value in a life insurance policy up to \$11,800.
- Social Security and veterans' benefits, unemployment insurance money, and pension and profit-sharing plans.

15 *When should I use a Chapter 13 plan instead?*

You should consider a Chapter 13 plan if you can work out a way to pay off your debts (or at least part of them) over a period of time and still afford the reasonable costs of living. Also, this type of bankruptcy may be your only option if you are not eligible to file for Chapter 7 (see #12).

The law says you can use a Chapter 13 plan if you have a steady income. This means you work for wages, own a small business or receive pension, Social Security or other benefits. You also must owe less than \$1,081,400 in secured debts, such as a mortgage, and less than \$360,475 in other debts. (These dollar amounts will change on April 1, 2013.)

If you qualify for Chapter 13, you and your lawyer will have to work out a plan for the court to approve. The plan must show how you intend to pay all or part of your debts. Certain debts must be paid in full. (These include secured debts, federal or state income taxes incurred in the past three years, and the court, trustee and attorney fees involved in setting up and carrying out the plan.) The appointed trustee collects your payments and pays your creditors. And if your circumstances change — you lose your job, for example, or become ill — while you are paying off your debts through a Chapter 13 plan, you can ask the court to switch you to Chapter 7.

16 *How can I find a lawyer to represent me?*

If you do not know a lawyer, ask a friend, co-worker, employer or business associate to recommend one. Or, call a local State Bar-certified lawyer referral service. For an online list of certified lawyer referral services, visit the State Bar's website at calbar.ca.gov/lrs. To hear a recorded message that will provide you with the phone numbers of certified services in your county, call 1-866-44-CA-LAW (442-2529). If you are out of state, call 415-538-2250. Or check the Yellow Pages of your telephone directory or contact your local bar association.

State Bar-certified lawyer referral services, which must meet minimum standards established by the California Supreme Court, can assist you in finding the right lawyer for your particular problem. Most of these services offer half-hour consultations for a modest fee.

Attorneys who are members of State Bar-certified lawyer referral services must carry insurance, agree to fee arbitration for fee disputes, meet certain standards of experience and be State Bar members in good standing.

Lawyer referral service fees do vary. Don't forget to ask whether there is a fee for the referral or initial consultation. And if you decide to hire a lawyer, make sure you understand what you will be paying for, how much it will cost and when you will be expected to pay your bill.

In addition, be aware that lawyers are generally required to notify new clients if they do *not* carry malpractice insurance. Such notification must be made when the client hires the lawyer if it is "reasonably foreseeable" that the representation will exceed four hours.

The State Bar also certifies "specialists" in bankruptcy law (and 10 other legal areas). To become a State Bar-certified specialist, a lawyer must show that he or she has extensive experience and tested ability in that field of law. In addition, the bar accredits certification programs of private certifying organizations in a variety of legal areas, including consumer bankruptcy law and creditors' rights law. Keep in mind, however, that there are lawyers with extensive experience in their legal

fields who simply do not seek certification. For an online list of State Bar-certified specialists, visit californiaspecialist.org (go to *Specialist Search*). Or call the State Bar's Legal Specialization Program at 415-538-2120.

If you have very little income, you might qualify for free or low-cost legal help. Check the white pages of your telephone directory for a legal services program in your county. (California's legal services website—LawHelpCalifornia.org—can help you locate a local program as well.) You also could ask your local bar association if its State Bar-certified lawyer referral service offers free legal advice to those with little income.

For more information, see the State Bar pamphlet *How Can I Find and Hire the Right Lawyer?* To order a free copy or to request information on ordering other consumer education pamphlets from the State Bar, send an email to pamphlets@calbar.ca.gov. Or visit the bar's website—calbar.ca.gov—where you'll find online versions of these consumer education pamphlets, as well as information on ordering them. For information on ordering the pamphlets by mail, call 1-888-875-LAWS (5297).

The purpose of this pamphlet is to provide general information on the law, which is subject to change. It is not legal advice. Consult a lawyer if you have a specific legal problem.

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