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A close-up photograph of a car's interior, showing a hand on the steering wheel, the dashboard, and a digital display showing '107.8'. The image is overlaid with a dark blue semi-transparent rectangle.

YOUR VEHICLE IN BANKRUPTCY

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Your vehicle is probably one of the most valuable assets you own. Not only have you put a lot of money into it, you may be hard pressed to manage without it. It may be essential for getting to and from work, school, and medical appointments, especially if you live in a place with little to no public transportation. It's not surprising that one of the most common questions asked of bankruptcy attorneys is: Will I be able to keep my car/SUV/truck if I file for bankruptcy?

What happens to your vehicle depends on whether it is fully paid for, financed, or leased and which type of bankruptcy you file. Vehicles are treated differently in Chapter 7 and Chapter 13 bankruptcy. The process begins when you list your vehicle in your bankruptcy petition. Then, depending on the specifics of your case, you may have some choices in how your vehicle is treated by the bankruptcy laws.

VALUING YOUR VEHICLE

Every item you own must be listed in your bankruptcy papers with a dollar amount for its current value. This includes your vehicle, whether an ordinary car, SUV, motor home, or motorcycle. Obtaining a proper value for your vehicle is important before filing your case for three reasons.

- First, the figure determines whether the equity in your vehicle is wholly protected.
- Second, if you have a loan against the vehicle, the value has an impact on much you will pay the lender if you wish to redeem your vehicle during the bankruptcy. (Redeeming vehicles in bankruptcy is further described in detail below).
- Third, you sign the bankruptcy papers under "penalty of perjury." This means that the value you provide for your vehicle, and all assets, is true and honest, to the best of your ability. A dishonest valuation may result in the dismissal of your bankruptcy case and loss of your discharge. In egregious cases, the failure to be truthful can even mean jail time, fines, and other penalties.

The value you place on your vehicle should be the replacement value, and not the trade-in value. The replacement value is the price a retail merchant would charge today for a vehicle like yours, taking into consideration its age and condition. There are several easy ways to obtain an accurate value and you want to take the time to get it right. It is important to be honest about the make/model, mileage, and condition. These are things that a bankruptcy judge or trustee could ask to verify. Here are some options for obtaining the replacement value:

Trade Publications (including online): This is the most common method that bankruptcy filers and trustees use to value vehicles. Some examples include Kelley Blue Book, N.A.D.A. Guides, and Edmunds. All have online calculators that allow you to input particular vehicle criteria (make,



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model, mileage, general condition, upgrades, etc.) and then choose from several types of values (private party sale, retail, trade-in value). These online forums allow you to print out your valuation as verification for how you obtained your value. However, these trade publications do have some limitations. They do not take into consideration major condition flaws such as a broken engine part or leaky gas tank.

Vehicle Max and Dealership Appraisals: Many vehicle sale outlets will provide you with an estimate of what your vehicle is worth in its current condition if you bring the vehicle in. Some will provide written verification and others will not. If you use this method, make sure the establishment you choose will give you a written estimate. Tell them you want a value based on resale value or market value, not the trade-in value. The trade-in value tends to be lower than the resale value.

Formal Appraisal: Licensed vehicle appraisers will do a thorough valuation of your vehicle and provide with you a full written appraisal. Although these are usually more thorough (and arguably trustworthy than the other methods), they also cost money out of your pocket to complete and they can be expensive. If you use this method, you might want to tell the appraiser that the appraisal is for a bankruptcy. For most filers, this method is more involved than they need for valuing a vehicle. However, if you are trying to protect a classic, antique, specially modified, or high-end vehicle, a formal appraisal is something you will want to consider. The other methods cannot always accurately portray the special circumstances and features of these vehicles.

No matter what method you use to value your vehicle, you want to be sure to obtain some written proof of the valuation you are claiming. This could be the actual appraisal if you go that route, or

simply a printout showing the online valuation calculator you used and on what date. In bankruptcy, a paper trail is a good thing. It shows you took the time and fully considered the valuation rather than just guessing. Surprisingly, vehicles often retain higher values than you might guess.

YOUR VEHICLE IN CHAPTER 7


Vehicle Exemption: When you file your bankruptcy case you are entitled to keep certain items of property up to certain values. These values vary greatly from state to state. But all vehicle exemptions consider only the equity that you have in your vehicle. That is the replacement value of your car (that you valued above) less any loans or liens you owe. If you do not owe any money on your car, your equity in the car is the actual value you list. To keep your vehicle, you must be able to exempt most or all of your equity. This means that the equity has to be less than the applicable exemption amount.

If you are unable to fully exempt the entire vehicle's equity, the trustee will determine how much of the value is nonexempt. Then, you can "buy" this portion of the vehicle back, or surrender the vehicle to the bankruptcy estate. The trustee will then liquidate (sell) the vehicle, pay off any loans or liens, pay you your equity, and use the balance of the proceeds to pay your unsecured creditors. If the trustee does liquidate the vehicle, the trustee must pay you the full amount of your exemption from the proceeds.

Example 1: Your vehicle is worth \$4,000 and your state allows you to exempt up to \$4,250 of equity in one motor vehicle. You do not have any loans against the car. In this example, your vehicle is fully exempt and you get to keep the vehicle.

Example 2: Your vehicle is worth \$12,000 and you have a loan against the car for \$5,000. The equity in your vehicle is \$7,000. Your state exemption allows you to exempt up to \$3,000 of equity in one motor vehicle. This leaves \$4,000 of unprotected equity in your car. In this case you may choose to pay that amount to the trustee and keep the car and then work with your lender to keep the car (see options below). Alternatively, the trustee can sell the car and pay the creditor the \$5,000 for the loan, pay you \$3,000 for the exemption amount, and use the rest (after deducting the cost of the sale) to repay your unsecured creditors.

Security Interests: One important factor affecting your vehicle in bankruptcy is whether you have clear title to it or you have a loan or have pledged your vehicle as security for a debt. Bankruptcy wipes out the obligation to pay most debts including vehicle loans. So, if you have a vehicle loan, and want to walk away from the vehicle, you can surrender the vehicle and never owe anything



If you do not owe any money on your car, your equity in the car is the actual value you list. To keep your vehicle, you must be able to exempt most or all of your equity.

additional on the loan, even if the vehicle is worth less than the remaining loan balance. However, if you are financing or leasing a vehicle that you want to keep, you will likely have the following four options when you file Chapter 7.

Reaffirmation: A reaffirmation agreement is a new contract between you and the vehicle creditor in which you agree to pay the balance owed on your vehicle note. Under this new agreement, you will still owe the balance on the loan after your bankruptcy. You will continue to make payments and the creditor promises that, as long as payments are made, it will not repossess the vehicle. When the vehicle is paid in full, the creditor must release the title.

There are pros and cons to reaffirming a vehicle loan and it is not something you should take lightly. It sometimes is the only way that a vehicle lender will allow you to keep the vehicle (not all lenders allow “retain and pay,” explained below). However, reaffirmation agreements are strictly voluntary. You are not required by bankruptcy law or any other law to reaffirm your vehicle loan.

If you do not make your vehicle payments after you reaffirm the vehicle loan, the vehicle lender can (and will) repossess the vehicle and sue you for any deficiency balance. A deficiency balance is a shortfall between what the vehicle finance company sells the vehicle for after repossessing it and what you owe. This is where the risk lies.

Before reaffirming a vehicle loan, make sure you understand the legal implications of taking on “new” debt and you can afford the payments. Be sure to have your attorney explain the details

to you and answer all your questions. A reaffirmation agreement requires either your attorney's signature or the court's approval. They need to make sure it is in your best interest.

Redemption: In Chapter 7, you have the right to purchase or redeem your vehicle from the creditor. You make a lump sum payment equal to the vehicle's fair market value and, in exchange, the creditor releases the lien. The Bankruptcy Code provides that you must pay the creditor the replacement retail cost of the vehicle. Then, the balance of the debt will be discharged.

For example, assume you own a vehicle worth \$5000.00, but owe the finance company \$10,000.00. In this circumstance, you could redeem the vehicle by paying the creditor \$5000.00 and the remaining balance will be discharged in your bankruptcy. This is the simplified version. Sometimes redemption involves a motion and hearing on the value of the collateral.

Redemption is a great option if your vehicle is worth significantly less than what you owe, you want to keep the vehicle, and you can come up with the necessary funds to pay the fair market value within a few weeks of your bankruptcy filing.

Surrender: If you cannot afford the monthly payments on your vehicle loan or if you determine that you owe more than the vehicle is worth, you can unload the vehicle and the debt in your Chapter 7 bankruptcy by surrendering the vehicle to the creditor. The debt will be forgiven in the bankruptcy like any other unsecured debt.

Retain and Pay: This is the unofficial option in bankruptcy. Here you propose to the creditor that you want to retain the vehicle and continue making payments. The advantage is that you eliminate the threat of being sued for a deficiency in the future should you default on the loan.

Here is how retain and pay differs from reaffirmation:

- First, in reaffirmation you sign a new contract for the loan, but in retain and pay you just keep making payments towards the loan and the lender accepts them. When the loan is paid off, the lender will release the lien.
- Second, with retain and pay, if you default on the loan, you will not owe for the balance of the loan. The debt (but not the lien) is wiped out in your bankruptcy, even though you continue to make payments. If you miss a payment, the lender can enforce its lien by repossessing the vehicle.
- Finally, retain and pay is completely dependent on the lender's willingness to allow it. Some lenders allow it, some do not. Given that lenders will usually get more money by continuing to accept payments than by repossessing, smarter lenders will typically allow retain and pay. But not all lenders make good financial decisions and these will try to repossess the vehicle if you do not either reaffirm or redeem.

Before reaffirming a vehicle loan, make sure you understand the legal implications of taking on “new” debt and you can afford the payments.

YOUR VEHICLE IN CHAPTER 13

In general, most of the same principles noted above apply to vehicles in Chapter 13. However, there are some special circumstances related to Chapter 13 that do not apply in Chapter 7.

Nonexempt Equity: In Chapter 7, if your vehicle has more equity than you have exemptions you will have to either pay the trustee the amount above the exemption or surrender your vehicle. In Chapter 13, if your equity exceeds the exemption amount, it is usually less of a problem. Essentially if your Chapter 13 payment plan proposes to pay the unsecured creditors as much as they would have gotten in a Chapter 7 liquidation, you can keep the vehicle and all its equity. (This is referred to as “the best interest of the creditor’s test”). In effect, you pay the non-exempt equity to your creditors over three to five years through your payment plan

Vehicle Loans in Chapter 13: If you have a loan on your vehicle, you can take a reasonable loan expense for the vehicle and budget it into your Chapter 13 plan. Your loan payment can be paid either directly to the creditor or through the Chapter 13 plan (where you pay the trustee the vehicle payment and the trustee then pays the creditor). Before plan confirmation, the plan will need to provide for “adequate protection payments” allowing the trustee to at least pay the vehicle lender the interest on the loan until your plan is confirmed by the bankruptcy court.

Cramming Down a Vehicle Loan: If your vehicle is worth less than you owe, or you are paying excessive interest, you might be able to propose a “cramdown” of your auto loan. This is a major

benefit available in Chapter 13 that is not available in Chapter 7 bankruptcy. Cramming down a car loan in Chapter 13 bankruptcy can reduce your balance, cut your interest rate, and slash your payment. In simple terms, if a vehicle loan is older than 910 days (the actual loan and not the age of vehicle), the court can give the borrower a prorated payment amount based on how much the vehicle is actually worth. In some cases, the interest rate can even be reduced.

Example: Karen has a car worth \$10,500, but the balance on her auto loan is \$16,000. Her payment is \$478 per month at 6% interest. In Chapter 13, Kim can cram down the loan balance to \$10,500, the amount the vehicle is actually worth. Therefore, her payments would be based on this new lower balance. The remaining \$5,500 becomes an unsecured debt, which will most likely be paid back at cents on the dollar through Kim's repayment plan. Kim's payments will be reduced to \$175 per month when paid through a 60-month Chapter 13 plan.