How Bankruptcy Can Avoid Foreclosure

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Many of today's homeowners have more than one mortgage on their home and, in this tough economic environment, they are struggling to pay multiple mortgages. In most cases, the value of the home is significantly less than the balance of the mortgages. Some people are simply walking away from their homes because they believe there is no alternative. What they may not realize is that in many cases, a second mortgage can be eliminated.

A second or junior mortgage can be eliminated in a Chapter 13 bankruptcy pursuant to the United States Bankruptcy Code if certain conditions are met. If the appraised value of your home is equal to or less than the balance of your first mortgage, then your second mortgage is deemed unsecured. Therefore, the second mortgage can be stripped off and then becomes unsecured debt, like a credit card or medical bill.

A Chapter 13 bankruptcy is often referred to as the "wage earner's plan," whereas a Chapter 7 bankruptcy is known as the liquidation bankruptcy. In a Chapter 13 bankruptcy, all of your debt is consolidated into one monthly payment, made directly to the Chapter 13 trustee assigned to your case. The trustee is responsible for distributing money to your creditors in accordance with your Chapter 13 plan. Usually, unsecured debts are paid at a percentage on the dollar, which is often a fraction of the original balance. Once you have successfully completed your Chapter 13 plan, your unsecured debts are discharged and you have no further legal obligation to pay them.

For example, if you have $25,000 of credit card debt, $5,000 in medical bills and a $70,000 second mortgage, the total amount of unsecured debt is $100,000. If your chapter 13 plan is approved and provides unsecured creditors with 10 percent of their claims, then you will be obligated to repay $10,000 of the unsecured debt. Instead of a $70,000 second mortgage that will take years to pay off, homeowners can see it stripped off in a Chapter 13 bankruptcy and paid at pennies on the dollar.

Eliminating a second mortgage allows many homeowners to keep their homes, avoiding foreclosures and monetary judgments. Sadly, many people turn to bankruptcy only after they have already lost their home and their finances are in ruins. A well-planned Chapter 13 bankruptcy can steer you away from this unfortunate scenario and can be filed even if you are not behind on your mortgage payments.

Although Chapter 13 bankruptcies are a great tool for managing debt and saving homes, they are not right for everyone. You must qualify for a Chapter 13 bankruptcy, which means you must have sufficient income to make the monthly payments for the term of the plan. If a Chapter 13 bankruptcy is not a viable option, a Chapter 7 bankruptcy can help a distressed homeowner get out from under massive debt and provide a fresh start. Bankruptcy can be an effective means to save your home, avoid foreclosure and give yourself a new financial start.

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