

What Is Bankruptcy and How Does It Affect My Credit History and Credit Score?

If you owe more than you can pay, and a disruption in your income means you can no longer keep up with your payments, you might want to consider filing for bankruptcy.

Bankruptcy is a legal process that allows you to get relief from the burden of unmanageable debt such as a mortgage or high credit card balances.

There are two types of bankruptcy for individuals: Chapter 7 and Chapter 13. Chapter 7 is known as liquidation; filers give up their assets in exchange for the discharge of their debts. It usually takes four to six months from the initial file date to the final discharge.

Chapter 13 is known as debt adjustment. It allows people to temporarily stop foreclosures or collection actions while they come up with a repayment plan for some or all of their debts over a three to five year period.

Filing for each type of bankruptcy requires that you appear in front of a judge, and fill out a raft of paperwork. That's why if you are considering filing for bankruptcy, you should find a good bankruptcy attorney who is familiar with the state and federal laws as well as the tax consequences.

The Repercussions of Filing for Bankruptcy

While a bankruptcy offers a fresh financial start in many cases, there are repercussions. Bankruptcy is the most serious negative mark you can have on your traditional credit history (what lenders look at to assess if you're a good credit risk). It will remain active on your credit history, affecting your traditional credit score, for up to ten years.

While you may be able to resume saving money without having to make payments for credit cards, medical bills and other obligations, you may not be able to get approved for credit or a loan at all during the first few years after filing for bankruptcy. Creditors will be less willing to loan you money if they see if you've filed for bankruptcy because they will be afraid you can't pay your bills.

Your credit history and credit score will definitely going to take a hit while you recover from your bankruptcy, but you will be able to re-establish good credit over time.

Know the Pros and Cons of Bankruptcy Before Filing

Bankruptcy is neither an easy way out of debt nor a quick fix. In addition to having to rebuild your credit rating, bear in mind that more employers are running credit history checks when making hiring decisions—and they are legally allowed to do so. Insurers may pull a copy of your credit history before determining what the price of your insurance policy will be.

Before you decide to file for bankruptcy, it is vital that you sit down and discuss the pros and cons with a reputable attorney or credit counselor. There may be alternatives to bankruptcy that you can try before you destroy your credit score in favor of a fresh start. You will also need to take a bankruptcy education class and receive a certificate before you will be allowed to file.

No one wants to end up in bankruptcy court a second time (you can file Chapter 7 bankruptcy once in six years). Be sure to start cultivating healthy money management habits like saving and budgeting, as this will help you avoid running into debt problems in the future.