



LEGAL BRIEF BANKRUPTCY

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Bankruptcy is a federal legal process designed to give debtors a financial "fresh start" by discharging burdensome debts or reorganizing them into a manageable repayment plan.

It should be a tool of last resort. A bankruptcy can stay on your credit report for up to 10 years, impacting your ability to acquire credit, housing, or certain jobs. Filing for bankruptcy does not automatically result in adverse administrative action or the loss of security clearance, but the underlying financial behavior that led to the bankruptcy will be scrutinized.

Once you start a bankruptcy case, it may be impossible to stop. It can affect your legal right to keep or use your property. Always consult with a civilian bankruptcy attorney before filing!

I. Overview

Filing for bankruptcy may be the only option for people who intend to pay their bills but simply cannot. The filing of a petition causes an "automatic stay," which prevents creditors from collecting debts. Most creditors cannot take any action during an open (unresolved) bankruptcy without the court's permission. This means that, once a bankruptcy petition is filed, it will temporarily stop bill collectors from calling, wage garnishments, pending civil court proceedings, foreclosures, and evictions.

Under the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA), individuals must complete an approved credit counseling course within 180 days before filing for bankruptcy. Additionally, a financial management or debtor education course must be completed after filing, but before receiving a final discharge.

Once a bankruptcy petition is completed, most of an individual's debt is permanently wiped, or "discharged," meaning creditors cannot legally collect on the debt. Legal Assistance attorneys provide limited advice and assistance on bankruptcy and generally can only refer you to resources. It is strongly suggested that you seek the advice of a civilian bankruptcy attorney if you are contemplating filing.

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II. Personal Bankruptcy

There are two primary types of personal bankruptcy: Chapter 7 and Chapter 13. Each must be filed in a federal bankruptcy court. There are filing fees associated with filing bankruptcy relief for both Chapter 7 and Chapter 13. If you hire a bankruptcy attorney to assist you through the process, the attorney fees are additional and can vary widely depending on the circumstances.

Chapter 7 (“Liquidating” Bankruptcy)

Chapter 7 cancels most ordinary consumer debt but allows the debtor to keep certain exempt property (see below). It is designed primarily to help eliminate overwhelming debt for those with few assets to protect.

To qualify for Chapter 7, your household income must be below the Nevada median income for your family size. If your income is higher, you must pass a strict “Means Test” calculation to prove you do not have enough disposable income to repay creditors. If you fail the Means Test, you may be forced to file Chapter 13 instead.

Chapter 13 (“Reorganization” Bankruptcy)

Chapter 13 allows an individual with a regular income to develop a plan to repay all or part of their debts through a 3-to-5-year repayment plan. Chapter 13 allows the debtor to keep some or all of their property, but they must make regular payments to a court-appointed trustee over the designated time period. The trustee then pays the creditors. The property the debtor is allowed to keep is protected as long as they continue making payments in accordance with the plan.

Waiting Periods for Repeat Filings

If you have filed for bankruptcy in the past and received a discharge, federal law dictates how long you must wait before filing again.

<i>Previous Chapter Filed</i>	<i>Seeking New Chapter 7</i>	<i>Seeking New Chapter 13</i>
<i>Chapter 7</i>	Wait 8 years	Wait 4 years
<i>Chapter 13</i>	Wait 6 years	Wait 2 years

Foreclosure and Vehicle Repossessions

Chapter 7 will *not* permanently stop a pending foreclosure or car repossession. To keep either your house or your car, you must continue to make your regular payments. However, Chapter 7 helps eliminate the deficiency balance due on your mortgage or car loan after the property is surrendered or foreclosed upon.

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Chapter 13 *can* stop a foreclosure or repossession. It allows debtors to catch up on missed mortgage or vehicle payments over the 3-to-5-year life of the repayment plan, provided they also maintain their regular ongoing payments.

Types of Debts

Bankruptcy does not discharge all debts. Several types of debts are protected by law and survive the bankruptcy process.

Dischargeable Debts	Non-Dischargeable Debts
Credit card balances	Child support & Spousal support
Medical bills	Most recent IRS taxes (*older income taxes may be dischargeable if specific criteria are met)
Payday loans & Personal loans	Court-ordered restitution & DUI injury/death judgments
Most civil court judgments	Debts incurred by fraud
Mortgages & Car Loans (*You must keep paying if you want to keep the property)	Student loans (*unless severe “undue hardship” is proven in an adversary proceeding)

(Federal) Student Loans and “Undue Hardship”

Bankruptcy courts use a three-part legal framework known as the *Brunner Test* to determine if repaying a student loan constitutes an undue hardship. November 2022, the Department of Justice (DOJ) and the Department of Education (DOE) issued new joint guidance that significantly streamlines the process for discharging *Federal* student loans. The DOJ/DOE guidance *does not* apply to private student loans (like those from Sallie Mae or SoFi). Debtors attempting to discharge private loans must still file an adversary proceeding and litigate against the private lender in court to prove the Brunner Test.

- **The Attestation Form:** The debtor must complete a 15-page sworn “Attestation Form” outlining their financial situation, efforts to repay, and future prospects.
- **Prong 1 Minimal Standard of Living:** The government now uses standardized IRS National and Local Collection Financial Standards for expenses like housing, food, and transportation. If a debtor’s expenses are within these IRS limits and their income still falls short of making loan payments, the first prong is met.
- **Prong 2 Persistence of Hardship:** The new guidance establishes explicit “presumptions” that a debtor’s hardship will continue. If the debtor meets any of the following, the government presumes their situation will not improve:
 - They are aged 65 or older.
 - They have a disability or chronic injury affecting income potential.
 - They have been unemployed for at least 5 of the last 10 years.
 - They failed to obtain the degree for which the loan was procured.

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- The loan has been in repayment status for at least 10 years.
- **Prong 3 Good Faith Effort:** The government now officially recognizes that navigating the student loan system is difficult. Good faith can be proven simply by showing the debtor contacted their servicer, applied for forbearance, or attempted to enroll in an Income-Driven Repayment (IDR) plan. Even if a debtor *didn't* enroll in an IDR, they won't be penalized if they have a valid reason (e.g., they were given bad advice by a servicer or feared the tax consequences of loan forgiveness).

It is vital to understand that a standard bankruptcy filing does not automatically trigger a student loan discharge, nor does the court automatically review the debtor's loans.

To seek a discharge, the debtor (or their attorney) must file an Adversary Proceeding. This is essentially a separate lawsuit filed within the bankruptcy case against the Department of Education or the private lender. The DOJ will review the Attestation Form. If the debtor meets the new guidelines, the DOJ will stipulate (agree) to the discharge, and the bankruptcy judge will typically sign off on it. If a debtor cannot prove that the entire loan balance constitutes an undue hardship, some bankruptcy courts (and the new DOJ guidance) may allow for a partial discharge.

III. Bankruptcy for Air Force Members

The Air Force position concerning bankruptcy petitions filed by military personnel is one of strict neutrality. Air Force members, like other private citizens, have a statutory right to invoke the procedures of the Bankruptcy Act. Accordingly, no adverse action may be taken against a member of the Air Force merely for filing a petition for bankruptcy or receiving a discharge.

Commanders may take adverse action against a member, however, if the underlying circumstances of a case involve mismanagement of personal affairs or a dishonorable failure to pay just debts. Neither the filing of a petition nor a discharge in bankruptcy can, by itself, be considered “mismanagement” or “dishonorable.”

Will Bankruptcy Affect My Security Clearance?

The status of your security clearance can be affected, but it is not automatic. The outcome depends on the circumstances that led to bankruptcy and several other factors, such as your job performance and relationship with your chain of command.

The security section will weigh whether the bankruptcy was caused primarily by an unexpected event (e.g., medical bills following a serious accident, divorce) or by financial irresponsibility. They may also consider recommendations from your chain of command. The amount of your unpaid debts, by itself, may jeopardize your clearance, even if you do not file for bankruptcy. In that sense, *not* filing for bankruptcy and ignoring debts may make you more of a security risk. Using a government-approved means of dealing with your debts (like bankruptcy) may be viewed as an indication of your level of financial responsibility.

IV. Protected Properties - State Exemption Statute

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In bankruptcy law, exemption categories are specific classes of property that the government protects from being seized and liquidated (sold) by a bankruptcy trustee. The underlying philosophy is that a debtor cannot achieve a true “fresh start” if they are stripped of the basic necessities required to live and work.

While the exact dollar amounts differ depending on whether you use Federal or State (e.g., Nevada) laws, the general categories of protected property remain consistent. Main exemption categories include Homestead Exemption (Real Property), Motor Vehicle Exemption, Household Goods and Furnishings (Personal Property), Tools of the Trade (Professional), Jewelry, Wildcard (Any Property).

That means that exempt property is not subject to the claims of unsecured creditors and may be kept by an individual, subject to the rights of secured creditors and lien holders. Nevada has “opted out” of the federal exemption scheme. Therefore, residents who file bankruptcy generally must use Nevada exemptions.

Nevada Exemptions: Domicile Test & The 180-Day Fallback Rule

Federal law dictates exactly which state’s exemptions a debtor is legally allowed to use based on a strict timeline of where they have lived. To use Nevada’s specific state exemptions (such as the protections for homesteads, vehicles, and tools of the trade outlined in NRS 21.090), a debtor must pass the 730-day domicile test.

The bankruptcy court looks strictly at the debtor's primary residence (domicile) during the two years immediately preceding the date the bankruptcy petition is filed. If the debtor has lived in Nevada continuously for that entire 730-day block, they are authorized to use Nevada exemptions.

If a debtor has not lived in Nevada for a continuous 730 days prior to filing, they cannot use Nevada exemptions. Instead, the bankruptcy court requires a specific calculation to determine which state's laws apply. The court looks backward to a specific 180-day window that occurred before the 730-day period. The court looks at the 180-day period immediately preceding the 730-day window (essentially days 731 through 910 before filing). The debtor must use the exemptions of the state where they lived the longest during that specific 180-day period.

These rules disproportionately affect military personnel due to frequent PCS moves. For service members considering bankruptcy, calculating this timeline is critical before filing a petition, as filing on the wrong day could mean the difference between keeping a home or having it liquidated by a bankruptcy trustee.

For example, if an Air Force member is stationed in Nevada but arrived only 18 months ago from a base in Texas, they cannot use Nevada’s bankruptcy exemptions. The court will look

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back to where they lived between 2 and 2.5 years ago (Texas) and attempt to apply Texas exemption laws to the property they currently own in Nevada.

The Federal “Safe Harbor” Provision

Many states write their exemption laws so that they only apply to *current* residents of that state. If a debtor recently moved to Nevada, the bankruptcy math might dictate they must use the exemption laws of their previous state (e.g., California). However, if California law states that only current California residents can use its exemptions, the debtor living in Nevada would theoretically be left with zero property protection.

To prevent this, the federal bankruptcy code includes a "Safe Harbor" provision, which apply when the 180-day rule directs the debtor to use a previous state's exemptions, but that state's laws prohibit non-residents from claiming them. In that case, the debtor is authorized to use the standard federal bankruptcy exemptions outlined in 11 U.S.C. § 522(d), regardless of the fact that Nevada is typically an "opt-out" state.

Exemptions Under the Nevada Exemption Statute

An individual must have an ownership interest in the property to claim it as exempt. Under Nevada Revised Statutes (NRS) Section 21.090, key property exempt from execution includes the following.

- Homestead: Protects up to \$605,000 in equity in primary residence.
- Vehicles: Protects up to \$15,000 in equity for one vehicle.
- Household Goods: Protects up to \$12,000 in necessary household goods, furnishings, and electronics.
- Tools of the Trade: Protects up to \$10,000 in professional equipment, inventory, and tools used for your primary occupation.
- Wages: Exempts 75% to 82% of disposable earnings from garnishment (or 50 times the federal minimum wage, whichever is greater).

V. References

- United States Courts - Bankruptcy Fees: Federal fee schedules for Chapter 7 and Chapter 13 bankruptcy filings. (Available at: [USCourts.gov](https://www.uscourts.gov))
- U.S. Bankruptcy Code (Title 11, United States Code):
 - 11 U.S.C. § 522(b): Exemptions and the 730-day domicile rule.
 - 11 U.S.C. § 707(b): The Chapter 7 "Means Test" requirements.
 - 11 U.S.C. § 109(h): Mandatory credit counseling requirements.
- Nevada Revised Statutes (NRS) Chapter 21 - Enforcement of Judgments:

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- *NRS 21.090*: Details the statutory caps for property exempt from execution in Nevada (Homestead, Vehicle, Household goods, etc.).
- Nevada Revised Statutes (NRS) Chapter 115 - Homesteads:
 - *NRS 115.010 - 115.050*: Rules regarding the declaration of homestead and the \$605,000 equity protection limit.
- Department of Defense (DoD) Adjudicative Guidelines: Guideline F (Financial Considerations) regarding how bankruptcy and unpaid debts impact security eligibility for access to classified information.

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