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WHAT IS A REAFFIRMATION AGREEMENT AND SHOULD I SIGN ONE?

A **reaffirmation agreement** is a contract in which a Chapter 7 debtor (the person who files a bankruptcy case) and a lender agree that personal liability for a debt will not be discharged in a Chapter 7 bankruptcy case. It is generally used for secured debt (e.g., cars and houses).

If the goal of a bankruptcy case is to eliminate (discharge) as much debt as possible, it may seem foolhardy for someone to agree that a debt will survive the bankruptcy. We very rarely recommend a client sign a reaffirmation agreement, but the creditors will always ask.

Reaffirming Secured Debt

Most reaffirmations are done to protect collateral on a secured debt. Secured loans, like car loans and home loans, are actually two agreements: the promise to pay borrowed money (the promissory note) and a promise to give up the collateral if the borrowed money is not repaid (the security agreement). In a bankruptcy case, only the promise to pay is discharged. The security agreement remains in force, and after the bankruptcy case is over, the secured creditor can still repossess or foreclose if you stop making the payments or keeping the property insured. If you sign a reaffirmation agreement, you are once again making a personal promise to pay the loan. By signing this new agreement, you are reestablishing your personal liability. We will generally not recommend this to any of our clients in Maryland no matter how hard the creditors beg.

Reaffirming Unsecured Debt

Sometimes you might choose to reaffirm an unsecured debt, like a personal loan or credit card. That happens much less frequently than with debts secured by collateral, most often to protect someone else who is also liable on the debt. Spouses are often jointly liable. Parents will often co-sign for children. If the co-debtor did not file a bankruptcy, the lender will look to the co-debtor for payment after your obligation is discharged. To protect the co-debtor, you could choose to reaffirm the account. But, again, we are not likely to recommend this.

What happens if you sign the reaffirmation agreement?

When you sign the reaffirmation agreement, the lender will file it with the court before the discharge is entered. Unless you have negotiated new terms for the loan, you will continue paying according to the same terms you had before the bankruptcy case was filed. After the Chapter 7 case is discharged, you can continue to work with the lender. The lender will send you statements and will report your payment status to the credit bureaus as if you had never filed a bankruptcy case. If you default on the loan, the creditor will be able to sue you personally for the debt in addition to repossessing the collateral (e.g., the car) or foreclosing. If this happens before you are eligible to file for bankruptcy again (usually 8 years), you will not be able to use bankruptcy to help you.

If the collateral is repossessed or you have an accident that is not covered by insurance, you will still be responsible for the debt that remains. This is called a deficiency balance.

What happens if you do not reaffirm the debt?

If you choose not to reaffirm the debt, it will be discharged at the end of your Chapter 7 case with your other dischargeable debts. You will no longer be personally obligated to pay the account, and the lender cannot actively try to collect the debt by demanding payment from you.

If you have collateral on the loan, the creditor will still have the right to repossess or foreclose on the collateral because the security agreement is not discharged in the Chapter 7 case. However, if you continue to make the scheduled payments and keep insurance on the property, the creditor will repossess or foreclose (absent extraordinary circumstances).

Should you sign the reaffirmation agreement?

Just because a creditor offers you a reaffirmation agreement, you are not obligated to sign it. It is your choice, but there are a number of factors you need to consider when you make that choice.

Can you afford the payments? As a part of the reaffirmation agreement, your attorney must certify to the court that you can afford the payments. If the attorney cannot certify to the court that you can afford the payments, the court may set a hearing and require that you testify about your ability to pay.

What is the collateral worth? If your collateral is underwater, meaning you owe more than the collateral is worth, signing a reaffirmation agreement might be a bad idea. This might be the best opportunity you will have to get out from under a burdensome debt.

Can you replace the collateral? If the collateral is something you need, like a car to get to work, it might be easier to replace than you might think. Your attorney can give you guidance on this, but there are many car dealers who specialize in financing for people just out of bankruptcy. It might cost you a little more in interest but save you money in the long run.

Do you have a co-debtor on the loan? If your co-debtor did not file bankruptcy, that co-debtor will continue to be responsible for the debt after your obligation is discharged. If that will cause a problem for you or for your co-debtor, signing the reaffirmation agreement might be a wise choice.

Reaffirming a debt is a serious matter. Your attorney understands the consequences and is in the best position to advise you on how a reaffirmation will affect your particular circumstances.