

## Bankruptcy: Automatic Stay And How It Protects You From Creditors

The moment that a petition for bankruptcy is filed, U.S. Bankruptcy Code imposes something called an automatic stay. The automatic stay will generally prevent the enforcement, commencement, or appeal of actions and judgments against a debtor from the creditors they owe money to who are trying to collect these debts incurred prior to the bankruptcy petition. The automatic stay also protects property of the bankruptcy estate itself from collection actions and proceedings.

If a creditor violates the automatic stay their actions are voided out. Any violation of the stay might cause the violating party to have damages assessed to them. But, like every complicated law, there are exceptions. A creditor might be allowed to take their collateral if they obtain permission from the court first. They'll get this by filing a motion for relief from the automatic stay.

After a petition is filed, the court will grant the motion or provide security to the creditor, which ensures that the value of their collateral won't decrease during the stay. Without the protection of the automatic stay creditors could hypothetically race to the courthouse in order to improve their positions against a debtor. If this happened, and let's say that a debtor's business was facing just a temporary crunch, it might not survive a "run" by creditors when their business could otherwise be salvaged. A run may also result in waste and it might be unfair to similar creditors that are owed money too.

There are three kinds of avoidance actions, and all of these are intended to limit the risk of the legal system prompting the downfall of a financially unstable debtor who hasn't yet declared bankruptcy. The bankruptcy system will generally reward creditors who continue extending financing to debtors and will discourage creditors from ramping up their debt collection efforts.

Despite the seemingly simple nature of these rules, a couple of exceptions exist in the context of each category of avoidance action.

### About the Author

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