

Tips from Consumer Action, Consumer Federation of America, Consumers Union and the National Consumer Law Center

Don't Get Caught in the Debt Settlement Trap

Having trouble paying your bills? You're not alone. Many people are struggling with their finances. You may be tempted by ads from companies offering to settle your debts for 50 cents on the dollar, but beware – it could be a trap that will leave you further in debt.

What you need to Know about Debt Settlement Services

Most debt settlement companies charge regardless of whether they ever settle your debts. They usually collect most or all the fee from you long before they have helped to eliminate your debts. You pay the fee whether your debts are settled or not.

Debt settlement services don't provide instant relief. Most debt settlement services require you to deposit a specific amount of money in a bank account each month until you have enough to make a reasonable settlement offer. While you are trying to save, the debt settlement company's fees are being deducted from your bank account. Saving enough for a settlement can take a year or more. If you have multiple debts, you will save for them one-at-a-time, so the whole process could take several years.

Debt settlement services can be very expensive. The charge is often based on a percentage of the total amount of debt that you want help with when you sign up for the service. A typical fee of 15 percent (some are even higher) on four credit card accounts totaling \$20,000 would be \$3,000. You would pay that amount regardless of how many of the accounts, if any, are actually settled.

Claims for success rates can be very misleading. Debt settlement companies advertise big savings but those claims often don't take into consideration the number of accounts that are never settled or the fees that customers pay. Industry figures show that the majority of debt settlement customers drop out of the programs within the first six months, after they have paid a large portion of the fees but before their debts are settled.

Debt settlement programs don't stop debt collection. Banks and debt collectors don't have to cooperate with debt settlement companies and they can keep trying to collect the money you owe. While you are saving for a settlement, your debt may increase because of interest and penalties, you may be hounded by collection agents, and you can be sued for the debt.

How to Get Real Debt Relief

Try to resolve debt problems with your creditors first. Call the creditor and ask if it's possible to change the terms of your debt to an amount you can afford by lowering your interest rate, forgiving late charges, and/or reducing your monthly payments.

Contact a nonprofit credit counseling service. There may be a small fee, though most nonprofit credit counseling services will provide advice even if you can't afford to pay. If your creditors agree to a plan allowing you to pay off your debts over a set period of time, the credit counseling service will charge you a small monthly fee for overseeing the payments. If you don't qualify for a debt management program, other options may be suggested. To find the nearest nonprofit credit counseling service, contact the National Foundation for Credit Counseling, www.nfcc.org, 1-800-388-2227, or the Association of Independent Consumer Credit Counseling Agencies, www.aiccca.org, 1-866-703-8787.

Know your rights. If you are considering debt settlement services, ask your Attorney General's Office if state law requires them to be licensed or registered and limits the amount and timing of fees (see the state government listings in your phone book or go to www.naag.org).

Read the fine print. You may find that the contract terms for debt settlement services are far different than – or even contradict – what the ads say. Read everything carefully and walk away from any contract that differs from what the ads or the salesperson promised to you.

Look for services that only charge based on success. Steer clear of debt settlement services that charge you fees whether or not your debts are ever eliminated. Look for services that charge most or all of the fees only when they succeed in reaching an acceptable agreement that will actually settle your debt.

Take immediate action if you can't make your mortgage or car payments. Debt settlement services usually don't address mortgages, car loans, or other debts "secured" by assets or property. Contact the lender or debt servicing company immediately if you are having trouble making your payments and try to work out new payment arrangements. For help regarding your mortgage, talk to a local housing counselor certified by the federal Department of Housing and Urban Development. To find one, call 1-800-569-4287 or go to <http://nhl.gov/offices/hsg/sfh/hcc/hcs.cfm>. Avoid services that ask you to pay a fee to stop a foreclosure or to try to get you a loan modification.

Consider bankruptcy. Some people who have too much debt need the fresh start that bankruptcy provides. Get legal advice to see if that is the right choice for you.