



CONSUMER CREDIT NATIONWIDE

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Helping you take control of your debt

Debt Settlement Companies - How they work

One approach to paying debts is called debt settlement. The idea is to get the creditor in a position where they think that collection of the entire amount you owe them is not likely and that their only choice is to accept something less than what you owe and cut their losses. Obviously, for someone who is 3 to 6 months (or more) behind in paying their creditors, the creditors may already be thinking that full collection is unlikely and MAY entertain accepting less than you owe. However, many people utilize a debt settlement company who are up to date and current with their creditor payments. Generally, barring some unusual situation, the creditors are not likely to consider a settlement when you are paying as agreed. Consequently, the debt settlement companies' first step in this situation is to ask you to stop making payments to the creditors and start making the payments to them instead. This allows the settlement company to accumulate a balance on hand that can be used to make a settlement offer. Creditors will normally want the entire amount paid at the time of settlement. They aren't willing to discount what you owe AND allow you to make payments over time. You can expect some increasingly aggressive collections activity if you are current with creditors and abruptly stop paying them so that you can pay the settlement company. The creditors know that with every day that passes the odds of them collecting will decrease. This means that they will utilize all their options to collect the money you owe including seeking judgment and garnishment of a paycheck. The settlement companies seem to do a good job of telling you how much they can save you, but give little explanation of what you have to go through to get the savings.

How does this impact your credit history? You may have a reasonable credit rating if you are current with the creditors at the time you start to deal with the debt settlement company. However, your credit rating must suffer significant decline in order to get the creditors to believe that they must accept settlement as a way to collect their debt. While you MAY indeed be able to save 50% or more by using the debt settlement company, the path to this savings can be lengthy and can not be guaranteed. Further, your debt savings will be reduced by the likely income tax you will have to pay since the reduction of the amount you owe is considered income by the IRS.

You should also be aware of the fees that may be charged by a debt settlement company. They typically have an upfront fee that will be covered by your first few months of payments to them. There may be other monthly charges that are incurred also. Certainly, these charges need to be taken into account when calculating any savings that are promised.

Debt settlement can be very useful for people who are significantly (1 year or more) behind in paying their creditors. While the debt companies are usually very willing to settle at this point, the problem is that most people will lack the means to come up with even a reduced amount to settle a debt all at one time.

Summing up, consumers need to be very careful when considering debt settlement as a way to pay debts.