Debt settlement companies may mislead you

August 14th, 2010, 4:01 pm

Recently, I have heard many Creditor rights and debt settlement companies making statements about bankruptcy that are at best inaccurate, and at worst an attempt to dissuade Debtors from filing bankruptcy in lieu of loosing their home and entering into long-term pay back plans with Creditors that are not in a Debtor's best interest. For example, I read one blog article, What No One Tells You About Bankruptcy, Foreclosure and Your Credit, that suggests filing bankruptcy will not always stop a foreclosure, or that your credit score will be harmed beyond repair for a decade by filing a Chapter 13 case.With all due respect to these positions on bankruptcy and its effect on credit, I would suggest that most homeowners facing foreclosure are already at the bottom of the credit score spectrum. Additionally, the only way to guarantee that a foreclosure is stopped is by filing a bankruptcy. Pursuant to section 362(a) of Title 11, once a bankruptcy case is filed, the foreclosure MUST be stopped, and the only way a creditor can continue is by filing a motion for relief from the automatic stay. In order for a creditor to do this, the homeowner must fail to make there subsequent payments.

I will grant you that many Chapter 13 cases do fail, but the reason for that are unrealistic plans, and underestimating a Debtor's expenses on schedule J, or an artificially inflated income on schedule I based upon untrue revenues from self employment.

What I have found in my practice is that a Debtor needs to take a hard look at there situation and determine if their house is (1) worth saving, and (2) if the homeowner has enough income to stay current and pay back their missed armaments over a 5 year period.

With respect to the contention that one's credit score will decrease with the filing of a bankruptcy and be harmed for up to 10 years, that is a very dangerous statement to make. In fact, it is actually possible for your FICO score to increase after your bankruptcy discharge. The reason for this is very simple, approximately 35% of your credit score is based upon the amount of debt. If you discharge thousands of dollars in debt, then that part of the calculation can only increase. Another approximately 35% of the FICO score is based upon your payment history. If by filing a bankruptcy, you no longer have debts to be in arrears on, then again you can only go up, over time as you make your chapter 13 plan payments. This is not to say that filing of a bankruptcy does not take a negative toll on your credit score, but it is balanced by the positives. In many situations, Debtors, especially those with a mortgage can rebuild their credit with in 24 – 30 months to the point of obtaining new secured debt loans. I do however, caution my clients to be careful not to fall into their old bad habits which created the need for the bankruptcy filing.

The bottom lines is that if you are facing a foreclosure or have a significant amount of unsecured debt, it is always a good idea to talk to a bankruptcy attorney or consumer debt advocate in your area before making any decision. Most of these attorneys such as me do not charge a consultation fee for the initial meeting and can provide you with a great deal of insight.