

## **Debt-Settlement Companies: Beware the Wolf in Sheep's Clothing**

With the economy continuing to suffer, more and more Mainers have fallen behind on their financial obligations. This can be incredibly stressful and most people feel totally helpless when their finances continue to spiral out of control, especially when they are getting continuous phone calls and mailings from debt collectors. It is no wonder that there are now so many professional debt-settlement companies offering up their services in Maine. Although there are legitimate credit counselors who are licensed by the State to consult with consumers to resolve their debt and credit issues, there are other companies operating in Maine, some of them illegally, which are in it solely for profit and often do more damage than good for consumers.

There are many different companies out there, but the pitch is pretty much the same: if you hire them, they will get your creditors off your back and will settle your debts for as little as 50% of what you owe. If this sounds too good to be true, that is because in most cases it is. There are things that debt-settlement companies will not tell you when you hire them about the risks and costs of their services. Before hiring a debt-settlement company, do some research on the company and consider the following risks that are pervasive in the industry:

**FEES:** Debt-settlement companies have various fee models. For example, some companies will charge a percentage (15-18%) of the total debt owed, others will charge a percentage of the debt savings, and others will charge a flat monthly fee. What usually happens is that the company tells you to stop paying on your debts and to send money to them instead, at which point the company will contact the creditors and negotiate settlements on your defaulted accounts. What they often do not tell you is that the money you send to the debt-settlement company goes towards their fee first, and only after the fees are paid do they start putting funds in an escrow account for settlement purposes. It can take two to three years for the initial fees to be paid; in the meantime the debt-settlement company is not doing anything to resolve your debts.

**LEGAL ACTION:** Once you sign a power of attorney for a debt-settlement company, they send notice to all of your creditors that they must cease and desist all further communications with you directly. Although this should get your phone to stop ringing, it can have other consequences as well. If a creditor cannot communicate with you directly, and your power of attorney (the debt-settlement company) is not negotiating any settlements because their fee has not yet been paid, the creditor's only other recourse is to sue you for the debt owed. Often the consumer is unaware that the debt is still owed until they are served by a sheriff with a Summons and Complaint!

**BAD CREDIT:** Creditors will not typically settle an account for less than what is owed unless the account is severely delinquent. This will be reflected on your credit bureau report and can obviously hinder your ability to borrow money in the future.

**TAX CONSEQUENCES:** When a creditor settles a debt, it is a taxable event for the consumer. Any amount of debt forgiveness over \$600 is considered income and the consumer must pay taxes on that income unless they are deemed insolvent by the IRS.

**THE GOOD NEWS:** Don't lose hope! As I stated earlier, there are legitimate, local companies who are licensed by the State to consult with consumers and help them to get out of debt and fix their credit. If you find yourself in a financial fix you may want to consult with an experienced attorney to discuss what options are available to you.