

The Dangers of Debt Settlement

Debt settlement companies advertise themselves as a fast fix for overwhelming debt. In reality, they rely on misleading promises, charge high fees, and fail to deliver meaningful relief, leaving people with damaged credit and even deeper financial distress.



What is Debt Settlement?

Debt settlement companies, also called debt relief or debt resolution companies, claim they can negotiate with creditors, so that you pay less than what you owe. While the idea sounds appealing, debt settlement comes with significant risks, including long-term harm to your credit and a heightened chance of being sued.

How debt settlement companies operate

1. They instruct you to STOP paying creditors, forcing your debt into default and immediately impacting your credit.
2. They tell you to START putting money in a special account for future settlements, knowing you will need about half of the amount you owe to settle.
3. Once you have saved half of what you owe plus ALL of their fee (up to 25% of the debt), then they call to negotiate a settlement.



The risks by the numbers

25%

of consumers are sued by at least one creditor, per a MD state report.

Source: Leslie Parrish, A Roll of the Dice: Debt Settlement Still a Risky Strategy for Debt-Burdened Households, 18 Cityscape 55, 59 (2016).



77%

of consumers don't complete debt settlement.

Source: Will S. Dobbie, Financial Outcomes for Debt Settlement Programs: Estimates for 2011-2020 (Jan. 15, 2021).

41%

of creditors do not work with debt settlement companies.

Source: InsideARM Debt Settlement Survey at 5 (Oct. 2011).



How debt settlement can hurt you

- When you stop making payments, your credit score can plummet.
- Creditors can continue to charge interest and fees after you stop making payments, adding to your overall debt burden.
- Creditors can sue for non-payment.
- A lawsuit against you can lead to wage garnishment, property liens or frozen bank accounts.
- Debt settlement companies might increase your debt by recommending new loans to finance their fees and settlements amounts — a practice known as “debt swapping.”

Alternatives to debt settlement companies

You have safer, more effective options:

- Negotiate directly with creditors. It's free and often works.
- Work with a nonprofit credit counseling agency to create a debt management plan.
- Develop a personal repayment plan with guidance from a certified financial counselor.

Debt settlement red flags

Be cautious if a company:

- Guarantees specific results, like cutting your debt in half.
- Pressures you to stop communicating with your creditors.
- Tells you to STOP paying creditors without clearly explaining the risks.
- Tells you to START paying into a special account for future settlements.

Get help from trusted sources:

The National Foundation for Credit Counseling: **NFCC.org**

Financial Counseling Association of America: **FCAA.org**

National Association of Consumer Bankruptcy Attorneys: **NACBA.org**