10-6-2010

Ways to Get Debt-Free — Safe or Not

Thomas A. Buckhoff

NEWSMAKERS, From 6

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Ways to get debt-free — safe or not

As of March 2010, total U.S. consumer debt reached $2.45 trillion, which equates to about $8,100 per person. The average household with credit card debt carries a balance of $16,007.

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Historically, consumers with excessive debt have employed two strategies for paying it off:

1. Home equity line of credit. With this strategy, debt-ridden consumers obtain loans secured by the equity in their homes. Since these are secured loans, such loans typically offer interest rates far lower than those offered by credit card companies.

2. Chapter 7 bankruptcy. In years past, many debt-ridden consumers have resorted to declaring bankruptcy in order to make a fresh, debt-free start. However, the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 made it more difficult for consumers to eliminate debt via Chapter 7 filings.

Since the above two strategies are now less accessible, consumers must look for other ways to deal with their excessive debt.

At present, consumers are confronted with an array of strategies for dealing with debt with varying degrees of legitimacy. A brief summary of some of the more prominent methods is as follows:

1. Debt consolidation. With this legitimate strategy the consumer consolidates a number of outstanding debts into one debt, usually a home equity loan.

This simplifies the monthly bill paying process and generally reduces the monthly debt payments. Since the debtor is paying back all debt obligations in full, the debtor's credit rating is positively affected by this strategy.

2. Debt settlement/negotiation. With this strategy, the consumer engages a third party (for a fee) to negotiate with creditors to pay back a lower amount than owed.

This strategy requires the debtor to stop making payments so the account goes into default status. The third party then convinces the creditor the debtor cannot pay back the full amount owed and negotiates with the creditor to forgive a substantial amount of the debt owed, usually about 50 percent.

Since the debtor is not paying back all debt obligations in full, the debtor's credit rating is negatively affected by this legal strategy.

3. Debt termination. With this strategy the consumer engages a third party who — for a fee ranging from $3,000 to $5,000 — will magically wipe away your debts forever with a few simple documents. Two common variations of this too-good-to-be-true scam include:

- The debt elimination letter. The third party provides you with a letter you show your creditors to get your debts voided. The letter explains that since many of the fees the credit cards charge are illegal, the entire debt is void.
- Credit card illegality claim. The third party provides you with a letter you show your creditors to get your debts voided. The letter explains that since you're borrowing your own money, the entire credit card system is illegal and, thus, the debt you owe is void.

Each of the above scams is based on the assumption it is cheaper for the creditors to write off the debt than to fight the debtors in court.

Although the third party will claim that creditors will not fight back, more and more creditors are choosing to do just that. Consequently, debtors ultimately end up with more, rather than less, debt.

Once again, the adage "if it sounds too good to be true, it is" proves to be wise counsel.

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