

Debt Settlement Companies Promise Relief. Here's What Actually Happens.

By Daniel Staeven, Esq.

For people behind on credit cards or personal loans, the ads for debt settlement companies sound tempting. They promise to negotiate with creditors and settle debt for less than people owe.

It sounds simple.

But a 2026 market study from TransUnion, one of the three major credit bureaus, looked closely at what actually happens to people who sign up — and the results raise some serious questions.

For those struggling financially and considering a debt-relief program, there may be other options, including potential bankruptcy protection. And it's not just personal credit card debt or bills. For those struggling with an unpaid tax bill and considering help from a debt settlement firm aggressively suggesting "pennies on the dollar" settlements through an IRS Offer in Compromise, there may be other ways to approach these issues with less cost.

The team at Frost Law can help with these situations. Schedule a free consultation by calling **(410) 497-5947**.

More People Are Signing Up, and Earlier Than You'd Think

According to the TransUnion study conducted in 2023, enrollment in third-party debt settlement programs jumped 41% in just one year. What's more surprising is when people signed up. More than half of enrollees, 53%, were still current on their payments when they joined. In other words, most people aren't waiting until they're deep in delinquency. They're enrolling while things still look manageable on paper.





Balances and Usage Climb Before Enrollment

The study tracked credit behavior for two years before people enrolled in debt settlement programs. For those current on payments during this period, average credit card balances more than doubled, rising from about \$7,100 to around \$14,500. Credit card utilization — meaning how much of the available credit is being used — climbed from about 51% to nearly 78%. Personal loan balances grew too, from around \$12,400 to almost \$20,000 over the same period.

In short, many people who ended up in debt settlement had been steadily taking on more debt for two years before they made that decision to seek help.

Credit Scores Take a Bigger Hit Than With Bankruptcy

For consumers, credit scores are key to a person's financial situation. Good credit scores can mean an array of things, making it easier to obtain home mortgages, reducing interest rates on car loans, and even affecting areas like renting housing and insurance rates.

Here's the statistic about credit scores that stands out most. Among people who were current on their bills when they enrolled in debt settlement, credit scores dropped by nearly 100 points during a six-month period, falling from a median of 645 to 549. Notably, during the next two years, these credit scores for enrollees recovered the slowest of any group in the study.

Compare that to people who filed for bankruptcy. Their median credit score dropped from 582 to 562 over the same six-month window, just a 20-point drop. That means the people who chose debt settlement while still current on

their bills lost nearly five times as many credit score points as the people who filed for bankruptcy.

This challenges a common assumption: Debt settlement is the softer, less damaging choice, and bankruptcy is the last resort. The data suggests the opposite may be true for many consumers.

Credit Cards Often Get Closed Along the Way

The study also found that about half of credit cards held by people in debt settlement programs were closed within six months of enrollment. The cards that got closed tended to have higher balances compared to their limits, meaning people had often maxed them out before the accounts were shut down. Losing access to that credit can be a real problem if an unexpected expense comes up while a settlement program, which can take years to resolve, is still in progress.

What Debt Settlement Doesn't Do

Debt settlement companies are not law firms, and enrolling in a debt settlement program generally does not stop creditors from suing people, garnishing wages, and continuing collection calls while debt negotiations take place.

By contrast, filing for bankruptcy triggers an automatic stay for creditors. The court order immediately stops most collection actions, lawsuits, and wage garnishments while the person's case is pending. These are different tools with different legal protections, and the right choice depends on the consumer's specific financial situation.

Why This Matters Before Signing Up for Anything



None of this means debt settlement is always the wrong choice, or that bankruptcy is always the right one. Every financial situation is different.

But the data makes one thing clear: Delinquency status alone doesn't tell the whole story, and neither does a debt settlement company's sales pitch. There are multiple reasons people should take a closer look before committing to a multi-year settlement program, including the steady rise in credit card balances before enrollment, the sharper credit score drops after enrollment, and the loss of available credit along the way. These are all real costs people shouldn't overlook.

Talk to a Bankruptcy Attorney Before You Decide

Before enrolling in a debt settlement program, it's worth talking to a bankruptcy attorney about your options. An attorney can review specific debts, income, and goals, and explain how Chapter 7 or Chapter 13 bankruptcy might resolve a person's financial situation faster, with stronger legal protections, and without the years-long uncertainty of a settlement program.

A short consultation can help people understand exactly what they're signing up for, as well as what might be given up, before making a decision that affects credit scores for years to come.

When it comes to debt and bankruptcy, Frost Law can help. People struggling with debt can contact the experienced bankruptcy attorneys at Frost Law at **(410) 497-5947** or **[schedule a free consultation](#)**.

Source data: TransUnion, "Identifying Third-Party Debt Settlement Risk Before It Surfaces" (market brief). Figures cited are from TransUnion's analysis of participating lenders' 2023 data and are not represented as industry wide.

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