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9 MISTAKES TO AVOID
WHEN YOU ARE HAVING MONEY PROBLEMS

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1. USING MONEY FROM YOUR IRA OR 401(K) TO PAY DEBTS.

This can be a costly error. Using retirement funds to pay off debts can hurt you in numerous ways.

- The vast majority of retirement accounts are exempt. This means your creditors cannot get at them and you won't lose them if you file for bankruptcy.
- Using retirement money to pay debts that can be discharged in bankruptcy, like credit card and medical debt, rarely makes sense. If you file for bankruptcy, you can eliminate the debt without spending any of your retirement.
- If your IRA or 401(k) balance isn't enough to get you out of your financial mess, you may end up needing to file for bankruptcy anyway, which means you will have completely wasted your retirement money.
- Using retirement funds to pay debt jeopardizes your future when you will be in more need of the funds due to lack of other income.
- The withdrawal from the IRA or 401(k) counts as income on which you will owe taxes and possibly even an early withdrawal penalty.
- Depending on how large the amount is, the added income could affect your ability to file Chapter 7 bankruptcy for a period of six months. During that period, you will be exposed to lawsuits and judgments from the creditors.

2. PAYING UNSECURED DEBTS LIKE MEDICAL BILLS, CREDIT CARDS, AND PERSONAL LOANS INSTEAD OF SECURED DEBTS LIKE MORTGAGES AND CAR LOANS.

Some creditors are so aggressive and sometimes predatory that they make you think that you must pay off their debts immediately or suffer severe consequences. Frightened by these tactics you may be tempted to pay their unsecured loans first and leave a secured loan unpaid. This creates multiple problems.

The two most common types of property subject to a security interest are probably the two most important things you own: your home and your car. A car loan creditor can repossess a car after one missed payment. If that occurs, you will lose your car and you will be responsible for any deficiency amount you still owe on your car note after the car is auctioned off usually for significantly less than it is worth.

While a mortgage company may not be able to foreclose as quickly, arrearages and late fees can significantly increase what you owe and make it very difficult to catch up. As a general rule, you should prefer to pay your secured creditors so you can keep your car and home, as opposed to paying unsecured creditors who don't have near the recourse that a secured creditor has.

In addition, if you decide to file for bankruptcy, the money paid to your unsecured creditor might as well have been thrown in the trash. Meanwhile, you will still have to catch up on your secured debts if you want to keep the property.

Finally, you might have to explain to the bankruptcy trustee why you were able to pay certain creditors, but not others, so close to filing. Such payments may be considered preferences that the trustee can force the creditor to return to the bankruptcy estate. It is always better to maintain your secured debts, even if you have to neglect the unsecured ones.

3. MAINTAINING ACCOUNTS AT A BANK OR FINANCIAL INSTITUTION WHERE YOU OWE MONEY.

Almost every bank and financial institution will require you to sign an agreement authorizing the bank to automatically garnish your account if you miss a payment owed to it. In other words, if you have your mortgage and a savings account at the same bank and you miss a mortgage payment, the bank can take it from your savings account. This is called a setoff. You should transfer your accounts to another institution where you don't owe money to avoid this situation.

4. USING A SECOND MORTGAGE OR HOME EQUITY LINE OF CREDIT TO PAY OFF CREDIT CARDS OR OTHER UNSECURED DEBT

As mentioned previously, credit card and other unsecured debt can be discharged in bankruptcy. If you don't make your mortgage payments, you could lose your home to foreclosure.

If the amount you borrow against your home doesn't get you out of debt, you may still end up in bankruptcy and now you will have wasted money that could have been used elsewhere. To make matters worse, you have allowed a second lien against your home, which increases your monthly expenses and the length of time before you are able to pay your home off. In addition, the second mortgage may not be dischargeable in either chapter of bankruptcy depending on the value of the home and amount owed on the first mortgage.

Don't fall for the advertisements that suggest you consolidate your debts with a home equity loan.

5. NOT PAYING YOUR INCOME TAXES.

Recent tax bills are not dischargeable in bankruptcy .If you do not pay your income tax and owe back taxes, there is a good chance you will continue to owe the back taxes after the conclusion of your bankruptcy. Interest and penalties will rapidly increase your tax debt, and the IRS has extraordinary collection powers. Keep your taxes current by withholding the proper amount from your income.

6. NOT FILING YOUR TAX RETURNS.

If you do not file your tax returns on time, you will have an issue if you file bankruptcy. Your case will not be closed and your debts will not be discharged until you file your return with the IRS and the court has a chance to review it. The IRS will not allow you to get through the bankruptcy without ensuring your returns have been filed and the bankruptcy trustee will not relinquish his or her role in your case until the trustee is able to view your last tax return. You also stand a better chance of losing your refund if you miss multiple returns, as between late fees and aggressive trustees, the likelihood that any part of that refund not exempt from earned income credit will be distributed to you is low.

7. TELLING A CREDITOR THAT YOU INTEND TO PAY.

It is always best not to say anything to a creditor than to promise the creditor that you will pay. Once you tell creditors to expect money, their harassment will grow every day they don't receive the promised money.

8. MAKING A WRITTEN PROMISE TO PAY OR MAKING A PARTIAL PAYMENT ON AN OLD DEBT.

Creditors are barred from collecting a debt once the statute of limitations has run. The limitations period on a particular debt depends on the state where it was incurred and the type of debt. State statutes of limitation on consumer collection actions are, generally, from 3 to 6 years. Making a written promise to pay or making a partial payment on the debt (no matter how small) may reset the clock on the creditor's ability to take legal action.

9. IGNORING PENDING LAWSUITS.

Ignoring pending lawsuits is a huge mistake as these lawsuits lead to judgments. Upon receiving a judgment, the creditor will be able to garnish your wages and freeze your bank accounts. In some situations, liens can be placed on your property and those are not automatically removed in bankruptcy. If you are sued on a debt, it's wise to at least consult an attorney. You may have legal defenses. It is normally best to file bankruptcy before the completion of a lawsuit against you.