Tarrytown-SleepyHollowPatch

BUSINESS, OPINION

How Consumers Manage High Credit Card Debt and Credit Scores in Difficult Times

Tracy Becker's advice on improving credit during the financial crunch.

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Credit card debts are going into default at record highs. With unemployment up, and home values dipping, creditors are having a very hard time getting paid.

Consumers are confused about how late payments affect their scores and what to do about making payments to creditors. We find that many good people are making the wrong decisions out of fear and misinformation.

When it comes to credit scores it doesn't matter whether you have a bankruptcy, judgment, late payment for $10 or $10,000, repossession, charge off or collection (when you don't pay a creditor at all for a length of time), settlement, or a foreclosure. Your score will drop anywhere from 60-100 points for your first derogatory mark. The higher your score the more it drops.

For example: If you have a 780 Fico score and you have a $10 late payment with Macys, your score will go down to a 680. If you have a 680 score it will drop down to around a 600 -620 for the same late payment. If you had a bankruptcy 3 years ago your score could be higher than the consumer who just had the new late payment.

The scores are more sensitive to new derogatory information. Since the score is evaluating your risk level as a consumer, for all types of financing, it is most concerned about who you are *now*! If you defaulted yesterday you are a much higher risk than the consumer who hasn't had a problem in 3 years. The older the late payment the less it affects your score and vice versa. All derogatory accounts stay on the report for at least 7 years, and bankruptcy 10 years. They can be removed earlier by credit restoration companies.

Besides late payments, what affects the score dramatically is balances. Balances that are over 10 percent of the limit on revolving credit have a greater impact on the scores. Revolving credit is any account on your credit report that you have the ability to charge the maximum and pay the minimum. The closer you are to your limit the more your score drops. Once you go over the limit , even by $1.00, your score will plummet. It can decrease 100 points from this alone. It is important to note that to keep your score high you must keep all your revolving credit balances lower. If one is high and 5 are low it will still hurt your score. You are better off paying them all down, as low as possible, rather than paying the larger balances down to the lowest dollar amount. It is the ratio of all your revolving credit balances to their limits that holds the most weight.

Now that we know all these facts it is clear why many consumers find their limits being dropped when they have carried high balances and incurred recent late payment. Over the past year or so creditors have been guarding against defaults by dropping limits and increasing interest on consumers that have paid late or carry high debt ratios. They don't care about who you were in the past only what you are doing now.

It has been the Wild West with the credit card companies. They have been able to hike up interest rates, sometimes 30 percent if they see any defaults, with no hesitation. They have used what is called "universal default". This is when a creditor, like Chase, watches your credit profile and sees you were late last month with a Capital One Visa card. Chase then hikes your interest rates (and or reduces your limits in some cases closes your account) as high as possible because of your history with another creditor. This will no longer be legal in July 2010 when the credit card rule changes go into effect.

You should be able to get a sense now of how things work. If you have had one or two late payments and are having trouble paying your bills your credit scores have already dropped dramatically. Many consumers, at this point, should be much more concerned about protecting themselves, not their creditors.

Juggling payments to creditors, paying them before yourself with concerns about your credit is not wise once your score has gone in a negative direction. When money is tight consumers should be responsible to unsecured creditors last. There are other choices to consider.

Debt settlement, debt consolidation, and bankruptcy are all good choices depending on your situation. If bankruptcy hurts your credit as much as a new late payment why would a consumer be so opposed to it? Many consumers are so afraid of what the word implies.

Bankruptcy was created to help consumers who, like many these days, have lost their jobs or have medical expenses that are too overwhelming to bear. Its whole purpose is to protect us as consumers. After you have gone to bankruptcy your credit can be cleaned up within two years. In most cases you can keep your primary residence if that is the only property you own.

Debt settlement means you can stop paying your creditors (credit card debt) and in time settle the accounts down to 20-50 % of what you owe. You will receive a 1099 on the saving and pay taxes after it is added to your income. Your credit can be cleaned up within a year or two after your accounts are paid off.

Debt consolidation can be used for people who can't go to bankruptcy and don't want to go into a debt settlement program. Consolidation is done by non-profit companies that pay your creditors, less than the minimum payment, and reduce interest rates down to 5 or 6%. You pay them one payment a month and they, for a small fee, pay your creditors for you. This also hurts your credit, and it can take a long time to finish paying off debt. Credit can always be improved once the financial picture has become stable.

It is also important to know that there are many different types of scoring systems.

The Fico score is the one that the mortgage banking industry uses. A good Fico score is a 720 to a 740. A great Fico score is a 740 and above. The Plus score is what you will find on sites like annualcreditreport.com, freecreditreport.com and truecredit.com, these sites are where consumers can go to buy scores direct. Plus scores are 40 points higher than Fico scores.

Vantage scores are yet another score variation offered online. Experian created the Vantage score a few years ago to compete with Fico. Vantage scores are usually 200 points higher than Fico and have letter grades as well. It is essential to know what score you have pulled and how it relates to the one you are being evaluated by. You can buy your Fico score at myfico.com (http://myfico.com/) but you will only be able to see your Trans Union and Equifax Fico score. Experian will not allow Fico to use their info to tabulate and sell the Fico score to consumers.

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Tracy Becker has appeared on nationally broadcast television and radio programs, delivering her down-to-earth message to consumers across the country. She is a popular writer of educational articles for realtors and bankers and has co-authored the: "The Credit Solutions Resource Kit." Tracy founded North Shore Advisory (http://www.northshoreadvisory.com/), Inc, a 20 year old Credit Restoration/Education Company located in Tarrytown. You can contact Tracy at: tracy@northshoreadvisory.com (mailto:tracy@northshoreadvisory.com).


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