

## Nine Debt Mistakes to Avoid

By Lita Epstein, credit and debt expert, WalletPop.com

Everyone mired in debt wishes for some type of magic spell that can make it disappear. Unfortunately there are no magic words to get rid of debt. You can only pay off debt with a disciplined plan of paying more on your accounts than the interest due.

As you search for that disciplined plan, you may find some tactics that make things worse rather than better. Here are some of the worst mistakes you can make:

- **Mistake No. 1:**

### **Signing Up With a Scam Artist for Debt Consolidation or Debt Negotiation**

Scam artists promise that they'll be able to negotiate with creditors to pay off your debt for pennies on the dollar. If you hear something that sounds too good to be true, it probably is.

Debt negotiation specialists can be a very risky choice and can have a long-term negative impact on your credit report. Fraudulent ones may pocket your cash and never pay your creditors. Before signing a contract, check with your state attorney general to be sure you understand the law and find out if there are any outstanding complaints against the firm which is offering you their services.

Debt consolidation specialists usually offer you loans that come with high fees and require you to put your house up as collateral. Before signing any contracts, be sure you understand the fees and the interest rate charged -- not only for the first year but for all future years as well.

- **Mistake No. 2:**

### **Playing the Teaser Interest Rate Game**

Don't you just love seeing those offers for zero percent interest for 12 months? It's tempting to try to take advantage of such deals. The credit card companies know it is and know you'll likely never pay off the card before the rate goes back up to 14 or 15 percent or more.

Some people are great at moving their debt year after year and finding new zero percent offers, but be careful. Eventually, you won't be able to qualify for the best rates anymore. That's because if you apply for credit too often, your credit score will fall. Or, as you keep moving your debt around, it will likely grow. Your credit utilization will go up and your score will fall -- knocking you out of qualification for the next round of needed teaser rate cards.

- **Mistake No. 3:**

**Using a Debt Repair Service**

Debt repair services do not offer a legitimate service and may actually encourage you to do things that are illegal. Many of these services offer to help you get a new identity, such as a new Social Security number. It's highly illegal and when caught, you could face federal fraud charges.

Others will promise to clean up your credit report and do the types of things you could do for free, such as order a credit report and correct the mistakes. Don't believe anyone who wants to charge you for debt repair services.

- **Mistake No. 4:**

**Using a Home Equity Line of Credit**

For years, when real estate prices were rising, many people paid off their credit cards with the proceeds from a home equity line of credit. Then they went out, bought what they wanted and maxed out their cards again. When the credit card payments got too high, they again took another loan against their house. Today, many of these people are at risk of losing their homes as the payments on their equity lines grew to levels they could no longer afford.

Remember, when you take an equity line you must put your house up as collateral, which means if you can't pay the bill, the bank can take your house. In contrast, credit cards are unsecured loans, which means there is no asset guaranteeing that loan. You can't lose your home if you can't pay back a credit card. For that reason, it's not smart to pay off unsecured credit card debt by taking a loan against your home.

- **Mistake No. 5:**

**Getting Caught Up In a House Payoff Scam**

If your house is at risk of foreclosure, the banks file notice with your local county clerk's office. House payoff scam artists use these lists to find potential targets. They'll approach you with fliers or post cards that say things like "stop your foreclosure," "save your home," or get "quick cash for your home." They could offer to buy your home, payoff your mortgage and then let you live in your home at a low rent until you can afford to buy back the home. Another common promise is that they'll pay your mortgage temporarily if you sign over your deed. They say they will let you continue to live in your house at a low rent until you can afford to pay your mortgage again.

But once you sign your deed over to these scam artists you'll never get it back.

Often they won't pay the mortgage, will pocket your rent checks and eventually the house will be foreclosed and you'll be left with nothing. Don't ever sign over the deed to your home to anyone other than a bank through a standard loan closing process.

- **Mistake No. 6:**

#### **Closing Paid Off Credit Cards**

When you pay off your credit cards, don't close them to celebrate. Instead let the cards sit with a \$0 balance and help to add to your total of available credit. That will help your credit score improve more quickly than closing them out.

Credit scoring companies look at what's called a credit utilization ratio. The people with the best credit scores have a utilization ratio of about 10 to 20 percent. For example, a person with total credit lines available of \$10,000 and a credit usage of \$2,000 would have a credit utilization ratio of 20 percent. Suppose that person paid off one of their cards with a credit line of \$5,000, closed the card and now has only a \$5,000 total credit line with \$1,500 in debt. His credit utilization ratio would go up to 30% and his credit score would likely go down.

- **Mistake No. 7:**

#### **Disputing a Charge and Not Paying a Creditor**

One of the best ways to destroy your credit score is to just stop paying a bill and ignore your creditor. The creditor can then report your non payment and your credit score could drop as much as 100 points. Even the first report of non payment can hurt you that much because the credit rating agencies see non payment as a sign that you're in trouble.

If you disagree with a charge, don't stop paying. Instead start a dispute process by putting in writing the reason you dispute the charge. Don't just make a phone call. You need written proof. If you fail and the dispute is only a minimal amount, say \$30, think about whether the fight is worth destroying your credit score. Sometimes it's better to pay the bill than destroy your credit. If it's a large amount and you feel it's worth your time, take the case to small claims court, but don't just stop paying and ignore the charge.

- **Mistake No. 8:**

#### **Lower Your Credit Limits**

You may think you will qualify for a bigger loan if you lower your credit limits and your credit report doesn't show you have as much available credit. But you get your best credit score when your debt utilization ratio is 10 to 20 percent. That

means if you have \$50,000 in available credit you can have up to \$10,000 of charges and still have access to the best mortgage rates because you have a debt utilization of 20 percent.

Let's say you decide you want to lower your credit limits because you think it will look better when you apply for a mortgage, so you ask two of your credit cards to lower your limit by \$5,000. Now you have \$40,000 in available credit, but you still have the same \$10,000 on credit credits. Your new credit utilization ratio would be 25 percent and you would no longer qualify for the best mortgage rates.

- **Mistake No. 9:**

### **Working With a For-Profit Credit Counseling Service**

You should never work with a for-profit credit counselor. You don't need to help a company make money while you're trying to pay off your debt. There are plenty of not-for-profit companies out there to help you lower credit card interest rates. Sometimes a credit counselor may advertise that they are non-profit, but still charge you high fees.

Find a non-profit near you at the National Foundation for Credit Counseling ([www.nfcc.org](http://www.nfcc.org)) or call 800-682-9832. A good non-profit credit counselor should do more than just help you pay the bills and negotiate lower interest rates with your creditors. They should offer you debt management plans and classes on money management.