One way you might be tempted pay off old debts is by increasing your credit card debt. This can be done directly by paying debt collectors using your credit card or by taking out a cash advance using the card. Some card issuers send you convenience checks which allow you to pay for your debts with the check. The hitch is that these checks come with high interest rates. Or you can pay for debts using the card indirectly by putting on your card necessities you usually pay in cash, freeing up cash to pay down your debts. If you have maxed out your card, this may involve taking out new credit cards.

One advantage of using a new credit card debt to pay off old debt is that it typically does not take your home or other property as security. You can avoid default by making the minimum payment each month, and even if you default completely, your income, bank accounts, and assets are not at risk until you are successfully sued on the debt. Even then your income, bank accounts, and assets may be partially or fully exempt from seizure. See Chapter 21[1].

Another advantage of using credit card debt, as opposed to taking out a loan with your home as security, is that you can eliminate the debt in bankruptcy. Nevertheless, this may not be the case if you run up big bills on your credit card or take cash advances just before filing. Creditors have argued with some success that if you use a credit card at a time when you did not have the ability to repay, you have committed a fraud which prevents the debt from being eliminated in the bankruptcy process.

The downside of adding charges to credit cards is that cards have interest rates over 20% plus late charges and other fees. The more you put on your card, the harder it will be to pay off your card. When you max out your card, you will not be able to use it in emergencies, and may have to resort to even more expensive forms of credit.

Definitely do not put medical debt on a credit card if you cannot pay off the card right away. As explained in Chapter 11[2], medical debt will have lower interest rates than credit cards, will have less of an immediate impact on your credit score, and you are more likely to find ways to reduce or delay payment of medical debt compared to credit card debt. Chapter 23[3] also explains that you should similarly not put debts owed to the IRS on your credit card.

Other of your debts, even high priority debts, can often be handled in a smarter way than putting the full amount on your credit card. Before using your card to pay down real estate taxes, federal student loans, or home mortgages, refer to the relevant chapters in this book about ways to reduce, delay, or even eliminate payments on those debts.

On the other hand, using your credit card is clearly better than taking out a payday, auto title, or similar high-interest small loan. In addition, use your card if that is the only way to pay for necessities or to pay high priority debt that cannot be otherwise delayed or paid out in installments.

Credit Cards to Avoid. Whatever the merits of using a credit card to pay off debts, you should definitely avoid certain cards that will just get you into trouble. Subprime credit cards, often advertised as helping those with “bad credit” generally come with very high interest rates, expensive fees often loaded onto your balance on card opening, and low credit limits.

It may make sense when it is time to build up your credit record to take on a secured credit card that allows you a credit limit up to the amount you have on deposit in a particular bank account. But such a secured card makes no sense if you are looking to borrow additional funds. If you are going to use the card to pay down your debts, it makes more sense to just take the money in your bank account and pay down the debt.

Avoid any credit card that takes your home as security. The more you put on your card, the more your home is at risk of foreclosure.

Credit cards offering zero interest should also be used with caution. No interest is charged during the promotional period, but the full balance must be paid off by the end of that period. If you do not pay the full balance by the end of the period, you are retroactively charged interest at a high rate for the whole promotional period. Suddenly you owe not only the remaining balance, but as much as an extra $1,000 or $2,000 on top of it.

No matter the type of card, also steer away from any card that charges high interest rates or high fees—late fees, over-the-limit fees, annual fees, membership fees, cash advance fees, balance transfer fees, even fees for buying lottery tickets with a card. No matter what card you have, make sure your monthly charges do not automatically include junk purchases, such as credit protection, credit report monitoring, travel clubs, and other similar offers. They will cost you a lot, but provide little benefit.
Source: National Consumer Law Center, Surviving Debt [50th NCLC Anniversary Edition], updated at www.nclc.org/library
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