10/17/2007

Debt Consolidation Can Affect Your Credit Score

Debt is a part of everyday life for most Americans these days. While some may only carry debt in the form of a monthly mortgage payment, many others have student loan debts, car payments, and most often credit card debt. Consumer credit has become so readily available that many people have gone hog-wild and overspent themselves. When there seem to be no more credit lines to tap, the answer is often to turn to debt consolidation agencies. In the long run, a debt consolidation loan and debt reduction program will likely be a great help to your credit score. In the first few months, however, you may see your credit score drop. Here’s why that happens:

The Short Term

Debt consolidation programs and debt management programs generally try to work with your creditors to create new payments plans to help you avoid bankruptcy. While these negotiations take place, your open balances might be suspended by your creditors, but they can sometimes be recorded on your credit report as late payments if the creditor does not provide the credit agencies with the correct information. You may be able to get some creditors to report the payment suspension, but others may require three on-time monthly payments before readjusting the status of the account. This means that your credit score could fall a little or it could fall dramatically for the first few months as you continue to have late payments recorded. If you need financing for a new home or auto loan in the near future, you should wait on the debt reducing program until after you secure the funds you are seeking.

The Long Term

It will take at least six months generally, before you see a correction of your credit score after you start into the debt consolidation program. At that point your accounts should all be back on track, with several months of timely payments on record. This will positively affect your score because it reflects more financial responsibility on your part.

Your score should also go up in the long run because most debt management programs teach you fiscal tips that will help you develop healthy money management habits. You will hopefully learn to consistently make on-time payments as well as keep your credit balances down to a manageable level. All of this will push your credit score upward over time.

Be Careful

If part of your debt reduction plan includes getting your creditors to settle for less money than your owe them, you will definitely see a negative impact on your credit score. This action shows that you failed to keep your end of a financial bargain. Your credit trustworthiness is called into question and your score will be lowered. Only time and better financial habits will be able to correct that sort of credit blemish.

Overall, choosing a good debt management program will be a great boon to your credit score as you mend your fiscal ways and deal more responsibly with money lent to you. Just be prepared for a dip in your credit score as you participate in and finish the program.