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7 things not to do when you've maxed out your credit cards

Yes, you're deep in debt. And yes, missteps can make things worse



By Amy E. Buttell

With unemployment rising and credit card companies [slamming the door on new credit and slashing credit limits](#), consumers may find themselves moving ever closer to maxing out their cards. For some, it can happen suddenly; for others, being maxed out comes about more slowly.

Regardless of how you arrived to your maxed-out circumstances, it's important to have a plan to get out of them. In this case, the best thing to do first may be to figure out what you shouldn't do. Here's what experts say:

1. [Don't miss any payments or make any late payments](#)
2. [Don't get a payday loan](#)
3. [Don't borrow from your 401\(k\) plan](#)
4. [Don't get more credit](#)
5. [Don't buy new stuff](#)
6. [Don't go it alone](#)
7. [Don't cut out all the extras](#)

1. Don't miss any payments or make any late payments. When times are tough, even a [minimum payment](#) on a couple of credit cards can seem like too much, especially when there are stacks of other bills to be paid. Still, it's vital to pay all your bills -- not just your credit cards -- because if you fail to make the [minimum payment](#) by the due date on any bill, that can have a domino effect on your overall credit, raising [interest rates](#) and increasing your minimum payments going forward.

"What we are seeing, in many cases, is that credit card companies are reviewing everyone's credit, so that if you have a misstep even with another creditor, other creditors are raising your rates," says Kim Cole, a senior counselor with Novadebt, a nonprofit credit counseling agency in Freehold, N.J.

This is called [universal default](#), and it has been outlawed by the [sweeping credit card reforms](#) that were enacted in December 2008. However, issuers aren't required to comply until the summer of 2010, so it remains an issue of which to be wary.

2. Don't get a payday loan. Payday loans are just about the worst type of available credit because borrowers are saddled with sky-high interest rates at a time when they're already struggling to make ends meet.

"With these high levels of interest, a \$200 payday loan will grow to a \$1,000 balance within a year,"



says Ken Clark, a financial planner and author of the "Complete Idiot's Guide to Getting Out of Debt." "You are using next month's paycheck to pay back last month's loan, so when the next month comes around, you have the same problem, plus you have to pay the interest."

Cole agrees, saying, "I've seen interest rates as high as 300 percent in some places. And because the rates are so high, consumers are not able to pay the loans back, so they take out more loans, and the balance just continues to build."

What we are seeing, in many cases, is that credit card companies are reviewing everyone's credit, so that if you have a misstep even with another creditor, other creditors are raising your rates.

*-- Kim Cole
Credit counselor*

money as collateral," says Clyde Wyatt III, managing director with Navigation Financial Group in Dallas. "Should you get laid off or terminated -- which we are seeing a lot of lately -- the loan must be repaid within 90 days. If the funds are not repaid, they are then reported to the IRS as a premature distribution and could be subject to taxes and penalties that could add up to more than one-third of the proceeds."

In the long term, by borrowing from your 401(k), you are decreasing your overall balance and limiting the impact of compounding returns, including interest and dividends. While it may not seem like \$5,000 or \$10,000 will make that much difference in your overall retirement plans, it can. Also, should you have to file for bankruptcy at some point in the future, retirement funds are out of bounds to your creditors, so they are one asset that you can keep when you emerge from bankruptcy.

4. Don't get more credit. As Americans became more addicted to credit, many have thought the answer to a cash flow problem was simply to get more credit. While it is easy to think that one more loan or credit card can solve your problems, experts strongly recommend that you resist the urge. "At this point in time, I am not suggesting to anyone that they obtain new credit unless they are in fantastic financial shape, which so few are," says Cole. "The temptation is there to get more credit because many don't have the same disposable income as we had last year."

Specialized credit cards, such as [department store cards](#), should especially be avoided, says Avi Karnani, CEO of Thrive, a New York City-based financial planning firm. "Store credit cards are among the worst kinds of cards out there," says Karnani. "They have higher interest rates and fees than other cards and are almost overwhelmingly designed to entice you to buy stuff that you don't actually need. You can't buy Pampers with a Banana Republic card."

[Store credit cards] are almost overwhelmingly designed to entice you to buy stuff that you don't actually need. You can't buy Pampers with a Banana Republic card.

*-- Avi Karnani
Financial planner*

Home equity lines of credit aren't a great choice either. In many cases, banks are also lowering or cutting off these lines of credit, so even if you have funds to tap, they might not be there for long. In any case, when you use funds from your home equity line of credit, you are eroding any equity you may have in your house, which is a bad idea in times of plummeting home values and high

unemployment.

5. Don't buy new stuff. With eBay, thrift shops, garage sales and even exchanges with friends and neighbors, there is often no need to buy items that are brand new. If you really need something, any of the above are good options, as are [Craigslist](#) and [Freecycle](#).

Bartering is another option to access goods and services without laying out cash or taking on more debt, says Hugh Simpson, author of the e-book "BarterWealth." "I have been bartering for more than 25 years and have bartered close to \$250,000 in products and services," he says. You can barter your skills or trade with someone else for access to their skills. For instance, a hairdresser could trade haircuts for accounting services or a contractor could barter remodeling a bathroom for a new Web site with a Web designer.

With [payday loans'] high levels of interest, a \$200 payday loan will grow to a \$1,000 balance within a year. You are using next month's paycheck to pay back last month's loan, so when the next month comes around, you have the same problem.

*-- Ken Clark
Financial planner*

Be sure to report any bartering exchanges on your tax return, as bartering is not tax-exempt. For example, if you bartered \$500 of landscaping services in return for \$500 worth of dental work, you need to report that \$500 as income, as does the person who performed the dental work for you.

6. Don't go it alone. In tough times, relying on your relatives and friends for moral support can make a big difference. Karnani is seeing a trend of relatives and friends forming budget

clubs to share cost-saving ideas and support each other when tough decisions have to be made. "We saw a group of women recently who are in their mid-20s and who get together once a week or so over a potluck dinner and talk about where they recently spent money and what they bought," he says. "When the group decides that spending on something was excessive or not needed, they would kind of resolve together that those items should be taken back."

Even if you don't call it a budget club, getting together with friends over a potluck dinner or coffee pot can save money that would otherwise be spent on expensive dinners. "Doing things like potlucks requires a bit of a mindset change because, at the end of the day, you are doing stuff with your friends and the people who matter to you, and it almost doesn't matter what you are doing," says Karnani. "You don't need to go out and spend money on drinks and restaurants to have fun."

7. Don't cut out all the extras. When you're in financial trouble, cutting out all the extras may bring your spending in line with your income, but it is also a surefire way to torpedo any budgeting or spending plan, says Cole. "You want to start by tracking expenses, writing down everything that you are spending for two weeks to a month because that will give you a clear picture of what you are spending. As consumers, we have a tendency to spend money that we don't even realize we are spending," Cole says.

"Once you have an idea of what you are spending, my suggestion is to make adjustments on what you want, but in the beginning, don't cut everything out," she continues. "We have a tendency to cut everything out, but that is where a lot of people fail in their budgeting because they think they are going to be able to remove every extra and leave themselves with the bare bones. Make simple adjustments, like instead of stopping for coffee on the way to work every day, do it twice a week. If you have every cable channel, cut the extra movie channels rather than dropping cable altogether."

See related: [Tapping a 401\(k\) makes little financial sense](#), [Regulators finalize sweeping credit card reforms](#), [Understanding how minimum payments work](#), [Glossary of common credit card terms](#)

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