

Proceed With Caution When Closing a Credit Account

It's easy enough to apply for a credit card today only to forget about it over the next year or so. However, that account still remains open and active on your credit report. Consequently, this can have an affect on your overall credit rating since having too many credit lines open could make you look like a worse credit risk in the eyes of lenders. They might be wary that you'll be overextending yourself.

In addition, if you have several accounts open, there's a greater chance that you will forget about an account you opened awhile back and you could unintentionally stop making payments on it. Therefore, it might be a good idea to maintain open accounts for some of your accounts, even if you plan on paying them off. In fact, you should keep at least 2 or 3 accounts open regardless of how much you use them because otherwise, there won't be anything for lenders to use to determine your credit history on. In this case, accounts are not just limited to credit cards, but can also include personal loans, mortgages, student loans, etc.

How Closing an Account Can Affect Your Credit Report

It's also important to understand that once you close an account, the record of the closed account remains on your credit report and can affect your credit score for a while. In fact, closing unused credit accounts may actually cause your credit score to drop in the short term, as you will have higher account balances compared to a smaller available credit.

For example, let's say you have four accounts, each with available credit lines of \$1000 (so \$4000 in available credit). And let's say you owe \$500 on two of the cards and the other two are cards you want to close (so you owe \$1000 total and have \$4000 in available credit). Well, since lenders factor in how much you owe vs. how much credit you have available, if you close those two cards, you go from owing 25% of your available credit (\$1000 out of a possible \$4000 available credit) to owing 50% of your available credit (\$1000 out of only \$2000 available credit). This might actually cause your credit score to drop, at least in the short term. In the long term, though, not having extra temptation to charge and not having credit you don't need is much more of a benefit.

The Importance of Monitoring Your Credit Report

It's a good idea to monitor your credit report from time to time, especially if you're making significant changes like applying for new credit or closing older accounts. That way, as you gradually pay off your debts and streamline the number of accounts you have, you'll also be aware of any potential negative impact your actions might be making, either short term or long term. You'll also be able to watch your score increase over time and there's nothing like positive feedback to keep you on track with your goals.

By following these tips, you can avoid some of the common pitfalls consumers face when paying off their credit accounts. Now that you are aware of these concepts, you can ensure that you're making the best decisions in terms of your credit and put yourself on the fast track to being debt free.

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About the Author

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