CARE Program

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Top 20 Mistakes Made by People Who Have Filed for Bankruptcy

(some of these tips are included in Mar/Apr 2005 issue of NextStep Magazine)

In the articles that I have written on behalf of the CARE Program for *NextStep Magazine* over the last several years, I detailed many reasons to avoid credit card debt and a number of important lessons, tactics and techniques, including an article on how to develop a realistic college budget, in order to help students prepare for and live a credit card debt-free college life. In this article I want to share with you some of the common mistakes that have been made by many of the bankrupts that I have seen in my Court, those who by their own admission were overspenders and credit card abusers, so that you can avoid making the same mistakes, not just during your college years but throughout your life.

These many bankrupts:

1. Seldom had a detailed and periodically updated budget, developed with a realistic view of what they "needed" versus what they "wanted" and could afford. Even if they had some form of a budget, they seldom kept to it. As a result, they never knew what their disposable income was, what they could actually afford without going into debt or what they could realistically borrow and pay back within a reasonable period of time.
2. Accepted "Myth One" of our competitive consumptive debt-is-ok society, which is that many things that are mere "wants" are in fact "needs." They were persuaded that they "needed" cable television, a cell phone, to go out to dinner on weekends as a reward for a hard week's work, an annual Disney World vacation and so much more. Just because so many Americans have or do these and similar things, does not make them needs, and it is not necessary to go into debt for them.
3. Actually believed that if a bank solicited them and approved them for a credit card, it had determined that they could borrow up to the credit limit and pay it back within a reasonable period of time, even with annual interest rates of as high as 24%. In fact no such determination was ever made. At most, the bank determined that it was reasonably likely that they would make at least the minimum payments.

4. Accepted "Myth Two," which is that they could afford credit card debt if they could make the minimum payments, even though doing that is the worse thing you can do. So many debtors with $30,000 and more of credit card debt that they could never have realistically paid back, and who were paying thousands of dollars in interest every year, incredibly have said to me, "I paid all my bills" until such and such happened, for example, "My overtime hours were cut back." Just because you can maintain debt doesn't mean that you can afford it. Being able to afford debt is being able to repay all of it within a reasonable period of time. When you have "paid your bills," you owe nothing.
5. Had no idea how much of their credit card debt was accumulated interest or that for years they had been paying interest on interest, so that they were paying double or triple for everything they were buying and doing. Since in many cases the minimum payment required on a credit card account doesn't even cover the accrued interest for that month, the next month you are charged interest on last month's unpaid interest.
6. Instead of having one credit card, so that every month they could see how much they charged, and if they were carrying a balance, how much debt they had actually incurred, the unpaid interest that was accruing, and that their balance was increasing, not reducing, they had as many as twenty-five credit card and store charge accounts. As a result, it became too difficult of a task for them to monitor their accounts, so they never even added up their balances to find out their total debt until they filed for bankruptcy.
7. Went into credit card debt to do things for others, like buying more expensive Christmas gifts for more family members than they would have if they actually had to pay cash for those gifts or taking children and grandchildren on expensive vacations they really couldn't afford.
8. Did not have savings for either reasonably anticipated future expenses or unexpected but inevitable emergencies. They never even thought or planned for these expenses, or if they did, they expected to use credit cards for them. If you have a ten-year-old hot water heater or a fifteen-year-old roof, you know that eventually you are going to have to replace them. These are things that you should have savings for. In this time of less job security, you should have six to eight months of salary saved in case you lose your job. How many people actually do that today? Chances are that you or a family member are going to have some uninsured medical expenses like co-pays, dental work or other medical treatments that are not covered by insurance. You may also have auto or home losses that your insurance will cover but you will have to pay a deductible. You need to have the money saved for these things. Resorting to high interest rate credit cards to pay them makes no sense.
9. Went into credit card debt to weather hard times, rather than cutting expenses and doing anything and everything possible to raise or increase income, without ever analyzing whether when the hard times

were over they were going to be able to repay the debt that they incurred to get over those hard times. Credit cards are not middle-class welfare, although many have referred to them as such.

10. When the amount of their credit card debt became significant, they never put a plan in place to stop charging, cut their discretionary spending and repay their credit card debt within a reasonable period of time.

11. Didn't even realize that something was wrong when they were "maxed out" on many of their credit cards and couldn't make the payments on one credit card account without borrowing from another account. Perhaps they were just in denial.

12. Never fully read and understood many of their financial contracts, such as their cell phone contract with hefty termination fees for changing plans or cancelling their service, their automobile lease or their credit card agreements. As a result, they paid many hundreds of dollars in unnecessary fees and had the interest on their credit cards increased to the highest possible rate.

13. Did financially illogical other things such as, while having $40,000 of credit card debt at 20% interest, saved $2,000 in the bank earning 1% interest in case they had an emergency, or contributed $200 per month into an IRA at work. The first thing most financial planners tell you is to pay off your high interest debt before you consider making any investments. In order to be in control of your finances you have to have a plan and "connect all the dots."

14. Admitted that they really didn't have anything to show for all of the credit card debt they incurred and could not even remember what most of the debt was incurred for.

15. Could not believe how addictive overspending and living above their means with credit cards really was.

16. Were embarrassed that they had been so financially irresponsible. In looking back, they realized that they never paid attention to their finances or the spending and buying choices they made. They were not in control, they were being controlled.

17. Indicated that after what they learned the hard way, they had cut up their credit cards and told their friends, family members, children and grandchildren to stay away from credit card debt. Many of them have said that they wished they never had a credit card.

18. Never thought that the bank would be as nasty as it was when they went into default on their credit card accounts, because the bank had been so nice when it solicited them originally, making them feel like they were "important" for qualifying for the card and even offering them attractive low teaser interest rates when they opened the account.

19. Waited too long to go on a "financial diet" or to get help with their excessive debt and overspending, so that bankruptcy became their only alternative.

20. Never realized how stressful and embarrassing it would be to go bankrupt.