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THE COLOR OF MONEY

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Retail Credit Cards May Cost You More Than the Discount

In my younger and more foolish days, I used to sign up for retail credit cards the way some restaurant patrons grab peppermint candies at the hostess stand.

I just couldn't resist getting the 10 percent discount that retailers dangled in exchange for signing up for their signature credit cards. I would never use the cards again. I just wanted the discount.

Then I became a lot smarter about how I use credit. Now, when shopping, I easily pass up all those delicious discount offers.

You too should say "No, thank you" to such offers, because it's important to limit your credit usage to optimize your all-important credit score. High credit scores often translate into better rates on the money you borrow.

I'm telling you this now because during the holidays, the pressure is on to push credit on shoppers. In addition, as you shop for big-ticket items, you will be enticed by those "take it home now and worry about paying us later" plans.

"Stores bring out their big guns this time of year with tempting credit offers, but shoppers need to know what the end result will be if they take them up on those offers," says Stephen Snyder, the author of a book due out in January called "How to Increase Your Credit Scores."

The average consumer can save $250 to $300 a month off their typical payments (auto, home, education, credit card, etc.) by improving their credit score, Snyder said.

So, if you want a higher credit score, digest what Snyder had to say when I asked him some questions about credit and credit scores.

As people are holiday shopping, should they spread their charges out on multiple cards or load up one credit card account?

People with high credit scores tend not to have many credit accounts, maybe three or four, and they work to manage these few accounts well over a long period of time. The best thing is to manage your debt among a few credit cards and keep the balance below 50 percent of each credit card limit. (So, if your credit limit is $5,000, you should have less than $2,500 in charges on the card).

If someone takes advantage of those offers to open a retail credit account just for the 10 percent discount, what impact can those open lines of credit have on their credit score?

It's credit you don't need. Opening an account triggers a credit inquiry to a credit bureau. A credit inquiry is simply a record that a lender has looked at your credit report. Credit inquiries can lower your credit scores up to 12 points per inquiry, on average. This can play havoc with your pocketbook—especially if you are in the market to buy a new house, refinance a current one, purchase a new car or make another major credit purchase.

For instance, a credit score that's five points lower could increase a home-mortgage down payment from no money down to 5 percent down.

And don't think that you can simply open the account, get the quick discount and close it. Closing credit accounts can also reduce your credit score. If you're going to open the account, it's best to keep the credit line open and pay as agreed for a long time after you open it.

How do those "buy now, pay later" offers impact someone's credit score?

It depends. You will most likely receive a credit inquiry—which, by the way, remains on your credit reports for 24 months but lowers your score for only 12 months. If you pay off the amount on or before the time allowed, you only suffer a credit inquiry.

Here's one more thing Snyder said you should be aware of: Check to see if a finance company, not a bank, is backing the retail credit card or that "buy now, pay later" plan.

It used to be that credit obtained from a finance company could make a huge (negative) difference in your credit score, Snyder said. That's because it was generally viewed that folks who needed to use a finance company instead of a bank were a higher credit risk.

However, the credit-scoring models have been changed so that credit obtained from a finance company isn't scored much differently from bank credit, said Ryan Sjoblad, a spokesman for Fair, Isaac and Co., which developed the widely used FICO credit-scoring model.

But there is a caveat. If your credit score is borderline—meaning you're just below a higher credit-score level that would help you qualify for a lower interest rate—getting credit from a finance company could keep your score slightly depressed.

Ultimately, if you want a "ho ho" holiday in years to come, say "no, no" to more credit.

Michelle Singletary discusses personal finance Tuesdays on NPR's program "Day to Day" program and online at www.npr.org. Readers can write to her in care of The Washington Post, 1150 15th St. NW, Washington, D.C. 20071 or by e-mail at singletarym@washpost.com.