



Authorized-user credit card plans can be useful, and abused

"Authorized user" sounds like a term you'd find on the warning label of a heavy-duty power tool. (*Authorized users only! All other users risk injury or death.*)

But in the world of credit reports, an "authorized user" is someone who is allowed to use another individual's credit card without being responsible for the bill.

That sounds like a sweet deal for the authorized user. But millions of people with good credit use this strategy to help their children or spouses build a solid credit history. Thanks to a recent turnaround by Fair Isaac, developer of the widely used FICO score, this avenue to good credit will continue to be available.

First, some background: When a credit card holder designates a child, spouse or other individual as an authorized user, the card holder's payment history appears on the authorized user's credit report. If the card holder has stellar credit, it will boost the authorized user's credit score. More than 50 million consumers are listed as authorized users on another person's credit card, according to Fair Isaac.

But in recent years, some credit-repair outfits have exploited authorized-user accounts in ways that Fair Isaac never intended. These companies arrange for people with good credit to "rent" their histories to strangers with tarnished credit.

"Some consumers were paying thousands of dollars to be added to someone's account to get a short-term increase in their credit rating," says Tom Quinn, vice president of scoring solutions for Fair Isaac. Fair Isaac officials were concerned that the practice, known as piggybacking, allowed consumers with bad credit to artificially inflate their scores.

In an effort to stop this practice, Fair Isaac announced last year that its new scoring formula, known as FICO 08, wouldn't recognize authorized-user accounts. Critics said the change would lower credit scores for millions of consumers, forcing them to pay more for everything from mortgages to car loans.

About 1% of consumers would no longer have enough of a credit history to get a score at all, according to a survey by Credit.com, a consumer website. Without a credit score, it's very difficult to qualify for a loan.

Lenders, meanwhile, raised a regulatory concern. They told Fair Isaac that they used FICO scores to comply with the Equal Credit Opportunity Act, which requires lenders to consider a spouse's credit history when weighing a potential borrower's credit risk. If Fair Isaac stopped



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recognizing authorized users, lenders said they wouldn't be able to use FICO scores to meet that requirement.

In response, Fair Isaac sent its scoring model back to the laboratory. Company analysts came up with a new version of FICO 08 that will continue to recognize authorized-user accounts but make it more difficult for credit-repair agencies to manipulate credit scores, Quinn says. Fair Isaac declined to provide details on how its new formula will close the piggybacking loophole. The company says it's working with the three credit-reporting agencies to get FICO 08 adopted as quickly as possible.

"This is great news," says John Ulzheimer, president of educational services for Credit.com, an outspoken critic of the original proposal. "I'm thrilled with Fair Isaac's willingness to take a second look at this."

A credit-building tool

Ulzheimer believes the authorized-user designation offers a valuable way for parents to help children learn how to manage credit without giving them their own credit card. "It's like a credit card with training wheels," he says.

There's no downside for the child, because an authorized user has no liability for the account, Ulzheimer says. If the parent falls behind on payments, the child can ask to have the authorized-user designation removed from his or her credit report.

"When you have someone as an authorized user on a credit card, you give them an escape route," Ulzheimer says. "If you lose your job or get into a horrible financial mess, you're not dragging them down with you."

Still, credit cards, like power tools, can cause a lot of havoc if they're handled improperly. For that reason, Quinn says, parents who name children as authorized users should set clear limits on how the card should be used.

"When I went to college, I was listed on my dad's credit card as an authorized user, but I was strictly told it could only be used for emergency purposes and not to buy a round of beer for everybody," he says. "When it's done in a family environment where the practices of sound credit are taught, it's very beneficial."

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