



Solving the Mystery of Credit Scores

By Victoria Fillet

Some of you are about to embark on your first career, while others will launch a different career. Whether you're new to the workforce or returning to it, it's never too soon to think about your financial foothold.

With that in mind, do you know the difference between your credit report and your credit score?

I like to think of the differences this way: Most people have bills that are due each month, and the timeliness of how well each person pays his or her bills is recorded by the three credit reporting agencies. These agencies create annual reports showing the payment history for each person's accounts. This recorded payment history is drawn from the three agencies and used to produce a credit score.

Credit Reports

Credit reports start with the three credit bureaus – Experian, Equifax and TransUnion – that each produce a credit report using information reported by lenders and creditors. Each bureau formats and reports your information differently, but each report basically contains the same categories of information, such as personal identifiable information, credit accounts, credit inquiries, and public records and collections.

Be sure all reported credit information is accurate and correct any errors you might find.

Personal identifiable information consists of your name, address, Social Security number, date of birth and employment information.

Credit accounts comprise lenders – mortgage, credit cards, auto, etc. – that report your

account information to all three bureaus, including your payment history.

Credit inquiries occur every time you apply for any type of loan or credit card. The lender will ask for a credit report from each agency, called a “hard” inquiry. “Soft” inquiries happen when potential lenders order a report and offer you pre-approved credit in the mail. Only “hard” inquiries affect your credit score.

Public records and collections result from the public record information the credit bureaus collect from state and local courts, including bankruptcies.

Each agency will produce a credit report detailing all four categories and listing your payment history on all of your credit accounts and loans. All late payments are highlighted.

You are entitled to a free report from each agency once a year. It's best to space your requests to each agency about four months apart to make sure you can always obtain an up-to-date view of your accounts. This is also a great opportunity for you to make sure all reported information is accurate and correct any errors you might find.

Credit Scores

Fair, Isaac and Company created an industry-standard credit score in 1956 that included a consistent credit-scoring algorithm. Today, this is known as your FICO score and is used, along with other details in your credit report, to assess your credit risk.

According to *myfico.com*: “To keep up with consumer trends and the evolving needs of lenders, FICO periodically updates its scoring models.” As a result, there are multiple FICO scores.

If you wish, you can dive deeper into the calculations and simulations used to make up the various scores, but for the purpose of this article, FICO provides a composite FICO score. While FICO is tight-lipped about exactly how the scores are calculated, it does provide the weights of the various criteria it uses:

Payment History: 35% Your payment history is the most important factor in your FICO score and has the most impact. Your payment history is carefully considered, and late payments have a negative impact. Making on-time payments can improve and maintain your score.

Amount Owed: 30% This number is the total amount you owe to lenders. Your overall credit utilization, or the percentage of your available credit used, is key here and is the second-most important factor in your score.

Although FICO does not release this information, it is believed that using no more than 30% of your available credit limit is preferred. For example, if you have a \$10,000 limit on

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your credit card, you should charge no more than a maximum of \$3,000 each month to maintain your credit score. Of course, that amount must be fully paid each month, on time, to maintain the score. If you need to charge more, it would be helpful to have the credit institution increase your credit limit.

Length of Credit History: 15% Those oldies are good-ies! The longer your credit history, the better because there is more data and payment history for financial institutions to use as a guide. Thus, if you currently have old credit cards you do not use, it's best to keep them (provided they do not charge fees) since canceling them will reduce the length of your credit history.

Types of Credit Used: 10% Credit mix is the assortment of different types of accounts and loans on record. It is the combination of mortgage loans, auto loans, credit cards and other loans. FICO ranks these types of loans in its calculations.

New Credit: 10% Every new application for a loan or credit card is added to your history. Too many requests, especially over a short period of time, could lower your score.

What Is a Good Credit Score?

Your FICO score will be checked when you apply for a mortgage, buy a car, rent an apartment, apply for a credit card and even when you interview for a new job.

What is a good credit score? According to *myfico.com*, a score of 850 to 750 is considered excellent, 749 to 700 is considered good, and 699-650 is categorized as fair. The higher the score, the better! Individuals with the highest scores will receive the lowest interest rates and best terms for financing; as the score drops, interest rates will go up and financing becomes more difficult to acquire.

How to Improve Your Score

We all would like to have a FICO score of 800 or higher, and there are ways to get there:

Pay down credit card debt This might seem obvious, and sometimes it's not easy, but start by not incurring additional debt. Pay off cards with highest interest rates first. Remember, the amount owed makes up 30% of your credit score.

Schedule payments Make your payments automatic so you will never incur a late charge. Also, credit card issuers report your card balance at the statement closing date, not the payment due date. Find your statement closing date and pay the card off at least one day before. If you do this, the balance will show as zero on your report.

Ask for a credit limit increase Lenders are willing to

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increase your limit, and this increase will reduce your utilization rate.

Do not apply for any new credit cards Seeking a new card triggers a "hard" inquiry and will temporarily lower your score.

Remove incorrect information Look for inaccurate information on your report, such as a late payment. If you have a conversation with your credit card issuer, it may remove it.

Give it time The length of your credit history is worth 15% of your FICO score, so negative information has a lower impact as it gets older.

Protect Your Identity

Identity theft is the fraudulent use of a person's identifying information, such as credit card and bank information, for the purpose of obtaining financial gain for themselves. Detecting and correcting this type of theft is time consuming and costly.

Monitoring your credit report is the single best way to spot evidence of identity theft; you can place a fraud alert on your file as soon as you suspect you might be a victim.

Credit freezes go even further than either credit monitoring or alerts by making credit reports inaccessible to lenders and others who might have a fraudulent interest in viewing your credit history.

Each of the three major credit bureaus offer a credit lock for a fee or a credit freeze for free. A credit lock might be easier to unlock when needed, but a freeze might provide additional legal protection.

You can temporarily or permanently remove a lock or freeze at any time to allow a credit agency to review your file. For example: If you plan to buy a new car and want the dealer to access your file for loan approval, you need only contact the credit agencies and have the lock or freeze temporarily lifted. It can then be reinstated at your request. You must contact each agency separately to place a lock or freeze on your report. Submit a request on each agency website or call each directly.

Obtaining Credit Reports and FICO Score There are many sites that advertise free credit reports and FICO scores, but the only one authorized by federal law is *annualcreditreport.com*. Most credit card companies now make your credit score available for free on a monthly basis. Since credit scores are widely used today for almost everything involving personal finance, it's imperative we make sure our information is accurate!

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