



## Credit FAQs

### **What is credit scoring?**

Credit scoring is a system financial institutions use to help determine whether to give you credit. Information about you and your credit experiences, such as your bill-paying history, the number and type of accounts you have, late payments, collection actions, outstanding debt, and the age of your accounts, is collected from your credit application and your credit report. Using a statistical program, creditors compare this information to the credit performance of consumers with similar profiles. A credit scoring system awards points for each factor that helps predict who is most likely to repay a debt. A total number of points, a credit score, helps predict how creditworthy you are or how likely it is that you will repay a loan when due. Your credit score changes over time with your credit patterns.

### **What looks bad on my credit report?**

There are basically 10 things that look the worst on your credit report: credit inquiries, credit rejections, late payments, past due and unpaid payments, court judgments, collections, loan defaults, repossession, foreclosure, and bankruptcy.

### **How does a lender decide that I am creditworthy?**

When you apply for credit by filling out an application, you normally give permission to the lender to get your credit report from a credit bureau. Lenders use this credit report to work a short-term debt-to-income ratio, where they calculate your present short-term debt payments (excluding your mortgage), and divide the total by your total annual income. Lenders will refuse you credit if your short-term debt is more than 20% of your annual income. The second method lenders use is to add up your monthly bills (not including rent or mortgage and utilities) and divide the total by your gross income (before taxes). With this method, lenders are looking for a ratio of under 35%.

### **How does a lender qualify me for credit?**

Most lenders look at the number of years you have worked at your present job, the number and nature of negative entries in your credit report, the amount of credit you currently have, savings and or checking accounts with the lender, length of time at your present address, or if you own your home.

## How do I Improve My Credit Score?

Most people can significantly improve their credit in as little as one or two years, if they are willing to work on it.

- **Know what's on your credit report** Get your credit report from all three major credit bureaus (see below). Dispute any information that is wrong and take care of any accounts currently behind. For example, if you have unpaid collection accounts, negotiate settlements so you can get them paid off.
- **Pay your bills consistently and on time** Make sure you at least pay the minimum monthly balances on your credit cards. If you do this monthly, your credit score will slowly begin to rise. Credit bureaus weigh the events on your credit record from the last two years more heavily than events further in the past. For example, the fact that you paid your car bill late four years ago will matter less than the fact that you've paid the bills on time since then. Events dating back seven years or more are dropped from your record.
- **Maintain only a reasonable amount of unused credit** While it's good to have a cushion of credit available, having ready access to thousands of dollars of debt makes you a poorer credit risk.
- **Have less debt** Having less debt will improve your credit rating and make it easier for you to make monthly payments. One rule of thumb: for a good credit score, your account balances should be below 75% of your available credit. For example, if you have a \$2000 credit limit, you should have a balance of no more than \$1500.
- **Avoid too many inquiries** Inquiries are interpreted as a sign that you have been actively seeking credit, and may be in financial difficulties or in the process of overextending yourself.
- **Pay off as much as you can from your savings account** You're paying your debtors much more than you're earning on interest

To get rid of credit card debt, pay off the card with the highest rate first, while paying the minimum on the rest—and then cancel that card. Then, move on to the card with the next highest rate. Consider consolidating to a low-rate card, but be careful of low "teaser" rates that will shoot up later. Sometimes, if you call or write your creditors and tell them why you are having trouble staying on top of things, they'll lower your rate.

### **Some debt is good.**

Borrowing for a home or college usually makes good sense. Just make sure you don't borrow more than you can afford to pay back, and shop around for the best rates.

### **How do I obtain a Credit Report?**

You can get a free credit report yearly from the Annual Credit Report website or by calling 1-877-322-8228 where you will go through a simple verification process over the phone.

It is important that you obtain and review a copy of your credit report once a year to make sure your information is accurate.