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WEEKLY COLUMN

The Ins and Outs of Credit Card Scores Money Matters

By Martin Brown, updated 5/22/2008 at 3:03:39 PM



By now, just about all of us have heard the phrase "credit score." Today, the common term for credit scores is FICO. That's because while there are separate agencies that produce credit reports on each and everyone of us, Experian, TransUnion, and Equifax; they all use programming software developed by Fair Issacs and Company, therefore the acronym, FICO.

But what are the key factors that create your FICO score? And what can you do to improve that score if you don't like it?

Credit scores are created by software that analyzes your credit history using five principle areas. The percentage placed next to each of these five criteria is the amount of value it represents in determining your overall score:

1. Payment History: 35% of your score.

This is gathered from account payment information on specific types of accounts (credit cards, retail accounts, installment loans, finance company accounts, mortgage, etc. Additionally there is the presence of adverse public records (bankruptcy, judgments, suits, liens, wage attachments, etc.), collection items, and/or delinquency (past due items). There are additional mitigating circumstances that include the severity of delinquency, the number of past due delinquent accounts or collection items, and the number of accounts paid as per the agreed terms.

2. Amounts Owed: 30% of your score.

Here what's reviewed is:
- The amount owing on all accounts, and the specific types of accounts.
- The number of accounts with balances outstanding, and the proportion of credit lines used, in other words the balances of total credit limits on certain types of revolving accounts.
- The last area of amounts owed is a review of the proportion of installment loan amounts still owing. (This is the balance to the original loan amount on particular types of installment loans.)

3. Length of Credit History: 15% of your score.

This include the time that has lapsed since your accounts were opened; the specific type of account; and the time since account activity began.

4. New Credit: 10% of your score.

This is determined by:
- The proportion of accounts that are recently opened, and by the type of account.
- Your total number of recent credit card, and various other loan inquiries.
- How much time has passed since recent account opening(s), by type of account; and
- The time elapsed since re-establishment of a positive credit history following past payment problems

5. Types of Credit Used: 10% of your score.

This is the number of various types of accounts (credit cards, retail accounts, installment loans, mortgage, consumer finance accounts, etc.)

This is the raw numbers and basic facts that go into making up your score. At the beginning of 2008, some changes were instituted to reward consumers for what Money Magazine aptly called "Good Borrowing Behavior." These changes included giving you a bump in your ratings if you have installment loans, as well as credit cards that are maintained at a low balance; and if you make regular and timely payments on those accounts. Conversely, your score can take a hit if you have only credit cards and keep the balances at or near the maximum.

Also, the system has been adjusted to not ding you for making a number of credit inquiries in a short period of time. For example, if, in the recent past, you were having a problem securing a new credit card and you applied to three different institutions to see if any would accept you, each one of those inquiries would take your score down a notch.

Nothing is more valuable in improving your score than paying your credit cards and loan installments on time. And, if you are behind on any of those, do your best to bring them current.

One thing I did several years ago to improve my on-time performance is that I ended credit cards that went off in the mail and limited my accounts to banks in my immediate area. Now that's not going to help you if you live in rural Montana, but if, like most of us, you live in cities or suburban communities where you have a Bank of America, Citibank, Chase, Wells Fargo, or other major institution down the road, there's a lot more peace of mind in dropping off a payment at the bank branch and seeing that it is credited that day.

You would think you could do the same with electronic bill pay, right? Wrong. Often that takes a number of days to be credited to your account, especially if it's a transaction between banks—and on occasion, outrageous as this is, within the same banking institution. So if you want to do your best to maintain a pristine record, take the extra few minutes and make a payment at the bank's local branch.

Another tip: It is a good idea to pull your free credit report once every 12 months. You can get it easily by going to www.annualcreditreport.com. You are also entitled to see your report when and if you have been rejected for a loan. In addition to recognizing the possibility of identity theft, accounts opened in your name, or credit inquiries made that you yourself did not make, it's wise to periodically check your credit score.

Most times the system works reasonably well. But there are times when accounts that have been paid mistakenly get reported as delinquent, and you are not even aware of that. It is also possible that someone by the same name has a delinquent account that was mistakenly filed by the reporting agent as being assigned to you when you never knew the account existed. I experienced that personally when I went through a loan application and the report came back that there was \$75 outstanding on my Pier One retail credit card. Only problem: I'd never opened a Pier One credit card. My doppelganger came to light when it was acknowledged that the Social Security number was not mine.

I know none of this is fun, but in a world where Big Brother is watching 24/7, you have a choice: live a life that never involves loans or credit cards—which is virtually impossible— or keep a clean record.

If you want to keep it simple as possible use just one credit card, and NEVER accept retail cards,

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such as Macys, Target, or Nordstrom. They'll lure you in with "Ten percent off today's purchase," but you'll regret you ever said "yes." First, remember that you'll ding your credit score each time you open a new account; and second but most importantly, you'll increase your chances with each additional card that a payment will get misplaced, you'll forget to put it in the mail, or something. It's just not worth the hassle. Particularly when the ten percent you saved on that pretty blouse has to be paid back, ten-fold, in the interest you'll be hit with, on the one account you'll never use.

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