The Magic Three-Digit Number: Your Credit Score

By Robyn M. Young

A credit score is a number lenders use to decide whether to give you credit. Landlords, utility companies, and employers all use credit scores to determine your reliability and trustworthiness.

Credit scores impact whether you can get a loan. They have a bearing on your interest rates and credit limits. They may be a factor in whether you get the job or the apartment you want. They may help determine the amount of your deposit for electricity, telephone, or natural gas service. In short, your credit score tells lenders and others how much of a risk you are.

The FICO® score, developed by Fair Isaac Corporation in Minneapolis, is the most commonly used credit scoring system. Each of the major credit reporting agencies, Equifax, Experian, and TransUnion, use your credit reports to calculate your FICO score. Whereas a credit score is a number, a credit report details your identification information, public record information, credit information, payment history, and inquiries for information from companies that want to offer you credit.

Because each credit reporting agency has a slightly different credit history about you, your score will vary among them. Each agency sells your credit score to lenders and other businesses extending credit.

The FICO score ranges from 300 to 850. Most consumers score in the 600s and 700s. Many lenders consider a score in the 700s to be good. To qualify for the lowest interest rates, you need a score of 780 or higher. A score below 660 indicates that a person is a significant credit risk, and, if he or she even qualifies for a loan, will pay high interest rates.

These scores are up from before the recession when a score of 720 qualified consumers for the lowest interest rates, and a score below 600 meant that they were a credit risk.

Your FICO score is comprised of five factors:

- 35% of your score is based on your payment history. Do you pay on time, all the time?
- 30% of your score is based on your “utilization ratio.” This is the amount you owe as a percentage of the amount of credit available to you. You want a low ratio.
- 15% of your score is your length of credit history. The longer your credit history, the higher your score.
- 10% of your score is new credit. How much new credit have you applied for? If it looks like you are taking on more debt than you can handle, your score will drop.
- 10% of your score is the type of credit you are using. A mix, such as mortgages, auto loans, credit cards, and personal lines of credit, will raise your score.

Your credit score continually changes. When your information changes, so will your score. This means that you can improve your score.

To raise your credit score, financial experts recommend:

- Pay on time. Payment history is the most important factor.
- Pay off debt. Don’t move it between credit cards.
- Keep the balance on your credit cards below 25% of your credit limit. Below 20% is better.
- Check your credit report regularly. Take immediate steps to correct any inaccuracies.
- Don’t close old credit accounts. Closing an old credit card reduces your total credit line. If the total you owe remains the same or increases, your credit utilization ratio will increase and depress your score.
- Did I mention, pay on time? The longer you make your payments on time, the better your credit score.

You can obtain your credit score for a fee. If you search for “credit score” on the internet, several websites will appear offering credit reports and credit scores for free. Be careful from whom you order your information. You may end up inadvertently signing up for services that you don’t need, such as credit monitoring, for a monthly fee. The recommended outlets for obtaining your FICO credit score are:

- Annual Credit Report Service at www.annualcreditreport.com. Congress established this service to make it easier for consumers to get their credit reports and credit scores from Equifax, Experian, and TransUnion. Be certain that you are on the correct site; verify the web address. And, as of this writing, this website does not have advertisements.
- Myfico.com at www.myfico.com. This is the consumer site of the Fair Isaac Corporation that developed the FICO score.
- The individual credit reporting agencies:
    - Equifax at www.equifax.com
    - Experian at www.experian.com
    - TransUnion at www.TransUnion.com

Keep in mind that, even though you are paying, you may be receiving only an estimated credit score which is different from what a lender actually sees. Lenders can purchase specialized FICO scores. Many mortgage lenders buy FICO Mortgage Scores. Credit card and automobile finance companies may use proprietary Industry Option FICO scores. These scores are customized to the needs of the lender and produce different results from the score that you can buy.

Although these scores may be similar to what you can get, consider whether it is worth the fee. You may be better off to regularly monitor your credit report. This you can do for free. You can request your credit report on line, by phone or through the mail at www.annualcreditreport.com. (See my related story below.)

Lenders and other businesses put a lot of weight on your credit score. If you are using credit or plan to in the future, it is worth the effort to take steps to keep your score as high as possible and regularly monitor your credit reports.