Your Credit Reports and Scores: UNDERSTAND TO IMPROVE

Christian Credit
COUNSELORS®
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Getting Started: Does Credit Repair Really Work?

Today, it's difficult to know who to trust and where you can find accurate information on managing your credit reports and credit scores. Many companies advertise that they can quickly "repair" your credit and help you eliminate your debt. In the case of your credit, the old saying stands true: "if it's too good to be true, then it probably is." Building and improving your credit takes time. Unfortunately, there is no quick fix once you have overextended your financial obligations. Despite this, there are still actions you can take to help yourself get back on track. First, you need to understand how credit reporting and scoring works. Whether you want to improve, build, or just manage your finances more efficiently, this eBook is a great first step in helping you achieve your goal(s). With this eBook, you will gain a basic understanding of how credit works, how credit is reported, and how scores are formulated. You will learn how to pull your free annual credit reports and how to review them. Once you have done that, you can make an action plan based on your goal(s). You will also learn some actions that you can take to prevent identity theft. Credit repair and financial help doesn't have to cost hundreds of dollars. By educating yourself, you can improve your credit for free.

Christian Credit Counselors (CCC) continues to provide our clients with the most up-to-date information regarding their finances. We understand that with all of the information out there today, it is difficult to know what is accurate and who to trust with your personal financial situation. CCC has taken the most current and useful information from a variety of sources to help you understand how credit reporting and scoring works. Ultimately, it's our goal that this eBook will arm you with the tools and information that you need to review and understand your current financial situation, and set goals to improve and/or manage your credit wisely.

Your Credit Report Explained

Once you begin to understand how credit reporting works and how crucial a positive credit history is to your ability to borrow and obtain financial security, the more important it will be to keep your credit in good standing.
First of all, it is extremely important to check your credit reports at least once a year so that you are not only fully aware of your financial situation, but also to check for any inaccurate information that may be negatively affecting your credit. The FBI has reported that identity theft is currently the fastest growing crime in the United States. Pulling and reviewing your credit report is essential to build and improve your credit report and score as well as for your own financial protection. Do not waste money on identity blockers or credit report monitoring scams. By law, you are allowed to pull one free copy of each of your three credit reports once a year from www.annualcreditreport.com.

The three main credit reporting agencies are Equifax, Experian, and TransUnion. These agencies compile each report which contains both financial and personal information about you. Each agency compiles a separate credit report for you but most often, the information amongst the three is very similar. You should expect to see the following information on your credit reports: your name, address and/or previous addresses, phone number, social security number, date of birth, current and previous employers, and any companies that have issued credit to you (i.e. credit cards, personal or student loans, car loans, mortgages, home equity loans, etc.).

Whenever you hear the term "Credit Reporting Agency" or "Credit Bureau," this refers to one of the three agencies mentioned above (Experian, Equifax, and TransUnion). The purpose of the agencies is to supply creditors with the most accurate financial information about individual consumers. Based on this information in your credit reports, the creditors can decide if an individual qualifies for credit or not. Within a credit report, there are four main sections: Public Record Information, Credit Account Information, Inquiry Information, and Personal Identification Information.

Key Elements of Your Credit Report Explained

- Public Record Information

In this section, you can expect to find listings such as bankruptcies or unpaid tax liens. This is also where lawsuits, judgments and any court proceedings will be recorded. It is important to note that a bankruptcy will appear on your credit for up to 10 years and tax liens can remain on your credit report for up to 15 years. All other delinquent and public record information can stay on your credit report for up to 7 years from the date of last activity.

- Credit Information

Here you will find a record of all the loans and credit you have been granted in the past and present. For each account listed, you will find details about the balance (as of the last reported date), the minimum payment, your credit limit, the date the account was opened and/or closed, whether it is an individual or joint account, as well as whether or not you are a cosigner or authorized user on the account.

Remember, you should never co-sign unless you are prepared to fully pay the debt yourself. For each account, your payment history/pattern is also listed. This will show if you have ever been late on a payment. Typically the credit report will show if the consumer is 30, 60, or 90+ days delinquent and if the account has been charged off or is with a collection agency. Each lender decides the point of delinquency at which an account is charged off. Typically an account is charged off between 90 and 150 days of delinquency.

- Inquiry Information (Requests by Others to View Your Credit History)

The Fair Credit Reporting Act allows credit grantors with permissible purpose to inquire about your credit information without your prior consent. These are called "soft inquiries." All of these inquiries remain listed on your credit report for up to two years and do not negatively harm your credit report or score. In this section, "hard" credit inquiries are also listed. These are the inquiries made by creditors with your permission as you are applying for credit such as credit cards, loans, or a mortgage. As you will see in the credit score section, too many of these hard inquiries within a short period of time can be harmful to your credit score. The exception to this rule would be rate shopping for a personal or auto loan. Creditors understand that these are not multiple attempts for credit and you, the consumer, are trying to get the best rate.

- Personal Identification Information

Your personal details such as your name, current and previous addresses, telephone numbers, current and previous employers, social security number, and date of birth are all listed here.

Delinquent items which are more than 7 years old as well as bankruptcies and tax liens more than 10 or 15 years old will not be listed on your credit report and will not negatively affect your report or score. Any checking/savings, 401K or other retirement accounts will not show up on your credit report. Typically utility bills are not reported to the credit bureaus but if they are delinquent and the company forwards the debt to a collection company, it may be reported and will negatively affect your report and score. This is another reason why it is important to set a monthly budget. It will ensure that all of your monthly bills are paid on time and that you do not overextend yourself financially.

Your Credit Score Explained

Now that you understand the sections of a credit report and what they mean, you are probably asking yourself: "How is my credit score formulated?" You do not just have one credit score. You have several that change all the time. They are based on the information on your credit report such as your balances, available credit, and length of credit history.

Your credit scores are designed to provide a snapshot of your credit picture. As creditors add and delete information from your report, your score will change. That can be good or bad depending on the information that is changing. An ever-changing credit report can be a good thing. If you currently have a low credit score, you are not stuck with it forever.

There are many credit scoring models used by creditors. However, we will focus on the FICO (Fair Isaac Corp.) scoring system because it is the industry leader and is used by 90% of lenders. Credit scoring models are designed for the lenders, not the consumers. This means that the exact formulas used to calculate scores are closely guarded. Even more reason to get a basic understanding of how to maintain and improve your score.

The FICO score is calculated based on an algorithm which changes due to evolving trends. The exact formula is unknown but, as trends emerge, research shows that the FICO score algorithm is adjusted. One example of this is in regards to rate shopping for mortgages and auto loans. Another example has to do with credit counseling agencies. In the past, this reporting counted negatively against the FICO score but now it does not. It is encouraged for people to seek financial help when it is needed.

Remember, you have to use credit to build credit. Without recent reporting on your credit report, FICO will not have the information to grant an accurate score. It is also important to note that many times, the credit score isn't the only information that the lender will consider. When you are in the process of qualifying for a mortgage, the lender will also look at your employment history, income, and the total debt payments monthly in comparison to your total income. Paying cash all the time does not build credit.

The average American has a credit score of about 700. If your credit score is at least 700 you will be setting yourself up for prime rates. The graph below will give you an idea of where you stand in the world of credit scores. A variety of life events and circumstances influence our credit situation. A hardship can make you feel financially out of control and it can be difficult to know how to get back on track. Despite this, improving your credit situation can be done with time and planning. If you understand the key portions of your credit report and how they affect your credit score, you can take actions towards improvement.

FICO Credit Scoring National Averages

FICO Credit Score:	300-499	500-549	550-599	600-649	650-699	700-749	750-799	800-850
Percent with score:	2%	5%	8%	12%	15%	18%	27%	13%

Payment History

Your payment history makes up approximately 35% of your FICO score. Any collection accounts, judgments, bankruptcies, foreclosures, or other adverse reporting such as late credit card payments will affect this portion of your score. Late payments and negative accounts are not something that will just go away but the longer it has been since the delinquency has been reported, the better. To improve this section of your report and score, you will need to begin building an ongoing history of on-time payments. The longer the history of consistent, timely payments, the more this section of your credit report and score will improve. For example, if you have a 30-day late payment reported on your credit report from April of last year and since then every payment has been made and reported as on time, this will help you. One late payment followed by a history of 24 on time payments is far better than several ongoing or sporadic late payments which would look risky to a credit grantor.

You will need to make sure that going forward, the account is paid on time each month to establish that current on-time payment history. You will also want to make sure that any adverse accounts such as collection accounts are paid in full. The negative account will still show up and affect your report and score but a "paid-in-full" collection account looks far better than one that is not paid in full.

Unfortunately, in order to pay collection or other delinquent accounts, you may need to speak with a collection agent or attorney. This can be scary, but making a payment arrangement on these accounts is your best bet, especially if they are threatening further action against you such as a judgment or wage garnishment. If you end up having to go to court then making payments toward the balance will only help you. You can offer to settle the account for less than the full balance but make sure you get the agreement in writing first and remember that you will be taxed on any forgiven amount more than six hundred dollars. Also, be very cautious of debt settlement because it can have a huge negative impact on your credit.

Amounts Owed

The amounts that you owe on your accounts make up approximately 30% of your FICO score. More specifically, this section deals with how much available credit you have compared to your total balances owed and the amount you still owe on any installment loans or other types of loans. Quite simply, as you pay down debt, this portion of your credit report and your score will improve. Some people think that they are improving their credit by closing zero balance accounts that they are not using. This is NOT the case. By closing those accounts you are decreasing your amount of available credit and this can hurt your credit score, especially if that account also happens to be an older one which contributes to your credit history. Paying off your credit card and line of credit accounts in full each month will keep this portion of your report in good standing and significantly help your credit.

If you are finding that your balances are too high at this point to do so, you will want to budget in a specific amount per month to pay down the cards. Once they are paid in full then you can begin charging and paying the full amount you charge each month.
If you find yourself in a hardship and cannot make the minimum monthly payments, you may want to contact a credit counseling agency. They will be able to assess your budget and help you get on track to pay off your accounts over time. It is important to understand your debt-to-income ratio. Your credit might be good but if you owe more to your creditors than you make monthly, that is a red flag.

Length of Credit History

How long you have had credit makes up approximately 15% of your FICO score. Compared to the first two sections, this one and the two following are far less significant but they still matter. This section will look at the age of your oldest account(s) and the average age of your accounts. This section will improve with time. One thing that you can do to improve this section is to leave your old accounts open even if you don't use them. If you only have newer accounts open it will hurt your credit because it does affect the average age of your accounts, which only looks at open accounts.

New Credit

This section makes up approximately 10% of your FICO score. Opening new accounts can negatively affect this portion of your credit score, especially if you are attempting to open numerous credit accounts within a short time or you don't have a long credit history. The average American hasn't opened an account in 20 months so if you are continually opening credit, beware because it may be affecting your score.

To maximize your score in this section, you will want to be mindful of how many accounts you have opened recently, how many of them are new, and how much time has passed since you applied and opened new credit. Throughout the years, research has shown that consumers now spend about 45 days rate shopping for auto loans and mortgages. Due to this, multiple inquiries only count as one on the credit report and do not negatively impact your FICO score. Remember, if you are rate shopping for one loan, your credit will not be negatively impacted but it will if you are continuing to open new credit accounts.

Types of Credit

Approximately 10% of your FICO score is determined by your "healthy mix" of credit accounts. This doesn't mean you should go out and apply for credit so that you have one of each kind (i.e. credit card, auto loan, mortgage, installment/personal loan, department store card). If you have a car loan that is paid off but still on your credit report, meaning it was open within the last 7 years, it still counts as a type of credit. This is the same as a personal loan or mortgage that is paid off but still reporting. A healthy mix of credit comes with time and opening different accounts all at once just to make sure that you have some of every kind is not a good idea because you are increasing your monthly payments and balances and this should be done over time.

It is also helpful to learn other ways in which credit can be categorized. Most credit can basically be obtained in two forms: secured credit and unsecured credit. Secured credit requires that you provide something of value to guarantee that you will repay your debt. It is usually used for installment loans. If you fail to repay, the lender takes your item as repayment. Personal valuables, such as a car, are often used for secured loans. On the other hand, unsecured credit such as credit cards, medical bills, or utility bills has nothing securing it, thus, it is a higher risk for lenders because they have no collateral if someone fails to repay it.

Within these categories, you will also hear about the following types of credit:

Revolving Credit - Allows you to borrow money any time up to the set limit. As you pay the borrowed money back, it becomes available for use again. The lender allows for monthly minimum payments or lump sum payments. If you pay back the debt over time, you are charged a fee each month on the amount that is owed. The fee is called interest. The most common types of revolving credit are credit cards, such as VISA or MasterCard, department store cards, and gasoline cards. It is important to understand what type of revolving credit you have, what the interest rate is, and how it is charged.

Installment Credit - Allows you to borrow a specific amount of money at one time for a defined purpose. You establish a payment plan with your lender to repay the loan on a regular basis over a period of time. The total amount of interest paid is determined in advance and is calculated into your set monthly payments. This type of credit is common for large purchases such as a home, car, or education.

Non-installment or Service Credit - Allows you to pay for a used service at a later date. Some businesses and utility companies offer this type of credit. Often, if you pay the total sum owed within 30-60 days, you do not have to pay any interest or fees. If you are unable to make the payment within the specified time, there is usually a penalty charge that will be added to your debt.

Steps to Do-It-Yourself Credit Repair

- Pull and review your three free credit reports from www.annualcreditreport.com at least once a year. Correct any inaccuracies and make a list of your debt. Use that list and this eBook to help create a plan for repayment.
- ALWAYS make your payments on time. Most lenders look for at least two years of consistent on-time payments.
- Avoid overextending yourself. Strive to pay your credit card balances in full each month.
- If you cannot pay your balances in full each month, take note of the minimum payment required on your monthly credit card statement. You must pay at least the amount listed to keep your account current.
- If you are not in the position to pay off your balances in full each month, look at your debt-to-income ratio and evaluate your balances and how you can lower them to a more manageable level.

What Now?

Once you understand your credit reports and scores in terms of these sections and their value, it is easier to evaluate your current situation and create an action plan. Now that you know how credit reports and scores "work," you will have a better idea of how to start improving them. With this knowledge, you want to set up your budget so that you can pay for your necessities and send extra funds to accounts with the highest balance and interest. Once you are "debt free," you will still want to use your credit but, instead of allowing credit balances to carry over month after month, you should only be spending what you can pay off in full each month. Paying off your full balances each month is the key to improving and maintaining your credit.

Still want more information or help with your finances? Christian Credit Counselors Inc. is a nonprofit 501(c)(3) credit counseling agency. We can help you avoid bankruptcy, debt settlement scams, and quick fixes through our debt management program. Over the last 25 years, we have helped over 300,000 Americans get out of debt and onto the path of financial freedom. Give us a call today to see how we can help you get out of debt up to 80% faster than you could by making minimum monthly payments on your own.

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