Credit Score

A person's credit score is one of the factors that lenders consider when they extend a line of credit or loan (e.g., auto loans, mortgage loans or personal loans). Lenders often use the number to determine rates, terms and risk. FICO and Vantagescore are the most widely used credit scores and range between 300 and 850. From a lender's perspective, a higher score equates to lower risk, which often translates to more favorable credit terms and better rates.

The following factors account for a consumer's credit score:

- **Payment history** – Shows whether or not you pay your bills on time. A single late payment will be included and can negatively affect your score.
- **Credit utilization rate** – Measures how much credit you use in relation to your credit limits. For instance, if you have two credit cards with a combined limit of 10,000, and a combined balance of 4,000, your credit utilization ratio is 40%. The lower the ratio, the better your credit score.
- **Length of credit history** – Having credit for longer has a positive impact on your credit score.
- **Type of credit** – Accessing different types of credit—such as mortgage loans, credit cards and student loans—indicates how well you manage your credit. A more diversified pool of credit is better for your score.
- **New credit** – Opening a number of new accounts in a short period of time has a negative effect on your credit score. Lenders examine how often you apply for credit and look at the number of "hard inquiries" on your account. When you access your own credit report, it does not impact your score.

Improve Your Credit Score

The first step to improving your credit score is reviewing your credit report. You can obtain a free copy of your report once a year at AnnualCreditReport.com or 1 (877) 322-8228. Your credit report includes the following information:

- **Credit history** – The number and types of credit opened both active and closed accounts), age of your accounts, your account balances and payment history.
- **Credit inquiries** – How often you have applied for credit. These "hard inquiries" will show up on your credit report for up to two years.
- **Collections** – Unpaid or overdue debts, such as foreclosures, bankruptcies or liens.

Once you access your report, determine if there are any errors. If you find any mistakes, you have a right to dispute the information, and can do so by contacting the three credit reporting bureaus: Equifax, Experian, TransUnion.

In addition to correcting any erroneous data, check what you need to improve. Typically, you will want to focus on:

- **Payments** – Even if you cannot pay off a loan immediately, always ensure that you make on-time minimum payments. Consider automatic payments or calendar reminders to make payments on time. Note that paying off a collection account will not automatically remove it from your credit report. It will remain for seven years, so it's important not to reach that point.
- **Keeping low balances** – Your credit utilization is an important factor in calculating your score. Lenders prefer seeing rates below 30%, so do not max out your credit cards.
- **Applying for new credit only as needed** – Too many hard inquiries that result from applying for new credit will lower your score.
- **Maintaining your accounts** – Don't close your credit card accounts even when you stop using them. If you do, you may hurt your credit score by unintentionally raising your credit utilization ratio. Consider the following scenario where you have two cards with a balance of $3,000 and a combined credit limit of $10,000.
    - Credit Card A – balance of $3,000 and credit limit of $6,000
    - Credit Card B – zero balance and $4,000 credit limit

When you maintain both cards, you have a credit utilization ratio of 30% ($0+$3,000/($6,000+$4,000). If you close the account with $4,000, your credit utilization ratio increases to 50% ($3,000/$6,000).

If you need assistance, contact a professional credit counselor at the National Foundation for Credit Counseling.