Solving The Credit Puzzle

Everything you need
to understand about your credit...
and then some.

EXPRESS VERSION

PRESENTS

The Express Version of the Credit Repair Magic Reference Guide *Solving the Credit Repair Puzzle.* This Express Version is provided for those who don't want to invest the time reading the entire 130-page Reference Guide

CHAPTER 2

What Is Credit And How Does It Work?

What Is "Bad Credit?"

A consumer to be denied the best credit terms. Many people find out the hard way that as Bad credit is defined as a credit report with any information (or lack of it) that may cause little as one late payment can bring credit denials or higher rates at every turn. It is a myth that lots of good credit can outweigh a little bit of negative credit. Any negative credit at all can be a major credit obstacle for most people.

Types Of Credit

In general, there are two types of credit you can obtain; secured and unsecured. **Secured credit** means that the loan is secured by the merchandise purchased with that loan. If you buy a car, that is a secured credit transaction because the lender can repossess the car if you do not repay the loan in a timely manner. **Unsecured credit** means that you were loaned money on the strength of your signature. This is sometimes called a signature loan. There is no specific merchandise backing the loan, just the lender's belief that you will repay the money. Unsecured credit generally requires a much higher credit rating on the part of the borrower.

Credit And Employment

One surprising place you may find your credit history being scrutinized is as part of an employment application. The law allows potential employers to examine your credit report as part of your employment interview process. In fact, many companies now routinely run a credit check on a person before making an employment offer. They feel this gives them some insight into the character of the applicant

Fair Credit Reporting Act

To address this issue, and provide a remedy to consumers for poor record keeping on the part of the credit-reporting agencies, the U.S. Congress first passed the Fair Credit Reporting Act (FCRA) in 1971. A summary of the law is included in the *Consumer Rights and Credit Laws* section of this publication.

The FCRA has been revised and refined several times. The laws established by this act require the credit bureaus to remove all obsolete, inaccurate, irrelevant, outdated, misidentifying, incomplete, incorrect, erroneous, or misleading information from their credit reports.

Specifically, if the completeness or accuracy of any item in a consumer's file at a credit bureau is disputed, the agency shall reinvestigate free of charge and record the current status of the disputed information, or delete the item, before the end of the 30-day period beginning on the date on which the agency receives the notice of dispute (the courts have allowed up to 45 days in some cases).

Further, the credit bureau shall promptly provide notification of any dispute to anyone who provided any item of information in dispute (that is, the creditor or collection agency).

If an item is found to be inaccurate or incomplete or cannot be verified, the credit bureau shall promptly delete the item, or modify the item, as appropriate, and notify the consumer no later than five business days after the completion of the reinvestigation

Defending Your Credit

You must develop an effective self-defense credit strategy, including periodically checking your credit reports and aggressively working on solving any and all credit problems you discover. This process should be done at least once a year. There are even some excellent services available that will provide you with unlimited copies of your credit reports for a small annual fee. These services will also enable you to access your credit report online and easily track any changes.

CHAPTER 3

Credit Bureaus And Credit Reporting

The Credit Bureaus

The credit reporting system is a business relationship between two parties: independent agencies that collect credit information (the credit bureaus) and merchants who pay for a copy of this credit information on an as-needed basis. Notice that the consumer is *not* a party to the transaction.

Credit bureaus refer to these merchants who pay a fee for their service as “subscribers.” As with any business, the main focus of the bureaus is to meet the needs of their customers, who are the merchant subscribers (and definitely *not* you).

Most banks, savings and loans, finance companies, credit card companies, and even some retail stores, employers, and apartment complexes will use a credit bureau's service, so they can be more aware of the financial risk they will be taking by extending the consumer credit. They are the same ones who report back to the credit bureau if that risk failed.

When you apply for any type of credit or financing, the creditor (merchant/subscriber) “pulls” your credit report, which contains information from at least one of the three major credit bureaus (Experian, Equifax and TransUnion). This helps the merchant evaluate the risks in extending credit to you.

The bureau itself doesn't actually approve or deny you credit, but rather supplies the merchant with your payment history as reported by other subscribers with whom you have received credit.

However, the bureau does use a closely guarded “secret formula” to assign a credit score to each individual based on the information in the file. This formula is a mathematical algorithm which is so complex it wouldn’t do you much good to know it even if it were available.

The information on your credit report (your credit history and current debt situation) is the most significant factor in the merchant's decision regarding your ability and willingness to meet your future financial obligations. The merchant is counting on the credit bureau's information to serve as a filter to help separate good credit risks from poor risks.

The shortfall of this system is that the product being sold (you) has little influence in this relationship. The merchant's primary motivation is to avoid bad credit risks, and the bureau makes a profit by charging the merchant for helping her do that. Consumers don't make money for the bureaus (except indirectly, as a product), so they are out of the loop (but yet the loop still dangles around their necks).

Every credit bureau desires to maintain as accurate information as financially feasible, but at the same time they realize that if they do err, it is better to err on the negative side rather than the positive in order to serve their subscribers' best interest. Although they want to develop as truthful a portrait of your credit history as possible, human nature compels them to give highest priority to recording negative items that might keep their customer base from entering into a risky credit arrangement.

The three major credit bureaus do not all contain the same information, nor is any one credit bureau likely to have the entire credit history of any one particular consumer.

There are also hundreds of smaller credit bureaus around the country, but most of them obtain their credit from the "Big Three"—Experian, Equifax, and Transunion. When you apply for a mortgage, for instance, the lender will almost always pull credit from one of these regional credit-reporting agencies because they have the ability to access all three bureaus in one report. The information on these "three-in-one" or "tri-merge" reports is almost always identical to that in the major bureau files.

A credit bureau collects and maintains information on the majority of Americans, but they are not affiliated with the government in any way. The credit bureaus are for-profit corporations and they sell your personal information for money. How much money? To give you an idea, Experian's annual sales exceed $2 billion.

The credit bureaus make money by gathering your credit information from credit grantors, listing the information in your credit file, then selling it to other credit grantors who want to see your credit history before they decide to lend you money. If you have shown any tendency to pay late or to default on paying your financial commitments, many credit grantors' computers are programmed to immediately reject your application.

How Credit Bureaus Get Their Information

Whenever you provide information about yourself on a credit application with a creditor that information usually will end up in a credit bureau's file. Credit data from millions of Americans is continually maintained and updated by credit bureaus.

Credit bureaus get your personal information from the same lenders who grant you credit. They have agreements that require the credit grantor to inform the credit bureau of everything that occurs in your relationship with the credit grantor. For example, if you are late with a payment, this fact is quickly reported to at least one of the major credit bureaus and is added to your credit history. Credit reports not only show how you are currently managing your credit, they are also histories of everything you have done in the past as far as your credit is concerned.

Not all companies report to credit bureaus, however. Many people who think they have a good credit report from various creditors are surprised to learn that oil credit card companies, hospitals, credit unions, and checking account information are not generally reported. In the case of checking accounts, if every overdraft that occurred was reported, it would be too time consuming, and credit bureaus could easily become overloaded.

Credit bureaus also get their credit information by searching public records. What they are most interested in are liens, judgments, bankruptcy actions, and wage attachments.

What Exactly Is A Credit Report?

Your credit report contains a list of your creditors, how much you owe on each account, when you opened the account, what your monthly payments are, your payment history, the current status of your credit, and other personal and important information.

What Kind Of Information Appears On Credit Reports?

Identifying Information Items such as your name, any aliases, current and previous addresses, social security number, and possibly marital status.

Merchant Trade Lines or Credit Lines These include all regular installment or revolving credit accounts such as department store cards, auto loans, mortgages, and credit cards. If you have any history of late payment or if the credit account was included in a bankruptcy, charged off, or put into repossession, the listing will be considered negative or derogatory by all credit grantors.

Not all credit accounts may be listed on your credit report since not every credit grantor reports to the same credit bureaus. In addition, not all credit grantors report every credit account to the credit bureaus. For a thorough review of your credit file, you should look at information from all three major credit bureaus.

Collection Accounts When any credit account is referred to a collection agency or the collections department of a credit grantor because of delinquency, non-payment, or other reason, it shows on the credit report as a collection account. Collection accounts can appear as paid or unpaid accounts. Any account that shows as a collection account (whether paid or not) is considered very negative by credit grantors.

Court Records Court records include bankruptcies, judgments, satisfied judgments, liens, satisfied liens, and divorce. Most court records, including satisfied liens and/or judgments, are considered very negative by credit grantors.

Inquiries Each time you apply for credit and a potential credit grantor looks at your credit file, an "inquiry" appears on at least one of your credit bureau files. Inquiries can also appear when an existing credit grantor reviews your credit periodically (to increase your credit line, etc.)

These requests for your credit report are noted as part of your credit history file and can actually lower your credit score by a few points because it may indicate your desire to increase the amount of your credit.

What's Not Included Your credit report will not include information about your race, salary history, religion, checking or savings accounts, stocks and bonds, medical history, personal assets, criminal record or personal background and lifestyle.

The Truth About Credit Reporting

Myth: The information on a credit report cannot be changed.

Fact: Exactly the opposite is true. The Fair Credit Reporting Act requires that items be removed if they are not 100% accurate or cannot be verified within 30 to 45 days. Read it for yourself—the FCRA is summarized in this publication in the *Consumer Rights and Credit Laws* section.

Myth: When I pay off a delinquent account such as a charge-off or collection account, it will stop hurting my credit, because it will then be shown as "Paid."

Fact: As hard as it might be to believe, sometimes paying off a debt can actually harm you. Most collection accounts are allowed to stay on your credit for a maximum of seven years. Paying them off without knowing what you're doing can unwittingly restart this clock.

However, this does not mean that you should never pay these debts. Elsewhere in this publication, you will learn the best way to pay off debts and improve your credit in the process.

Myth: Credit-reporting agencies are empowered with government authority.

Fact: Credit bureaus are like any other for-profit business. They exist for one reason: to make money. No special authority exists. Rather, they must adhere to government laws and abide by the Fair Credit Reporting Act and numerous other laws.

Myth: Bankruptcy is a "fresh start."

Fact: Unfortunately, many attorneys don't clearly explain the devastating effects to one's credit when filing bankruptcy. This goes for all types of bankruptcy including Chapter 13 (the Wage Earner Plan).

Bankruptcy is not a clean slate. Every account included in the bankruptcy will be so noted in your credit file. Additionally, there will be a court record generated that will also be added. Avoid bankruptcy if at all possible.

Although you can often re-establish credit after bankruptcy, the time table and the odds of completing credit restoration are greatly extended due to the number of negative entries that are associated with such filings.

Myth: Some types of credit information (such as bankruptcies, judgments, and foreclosures) are impossible to remove.

Fact: Although it is true that some types of information can be more difficult than others to remove, each of these types of entries have been removed hundreds of thousands of times, using numerous methods.

Myth: Credit repair is too complicated for consumers. It is necessary to hire an attorney.

Fact: An attorney well-versed in the intricacies of the Fair Credit Reporting Act can help with clarifying the finer points of your state's laws and provide information about the possibility of filing a lawsuit. However, you can accomplish most if not all of the legal and negotiation-based methods in this publication yourself by becoming familiar with your federally given rights and how to enforce them.

Myth: It is illegal to have truthful information removed from a credit report.

Fact: Congress has already set the precedent by making special provisions for the removal of correct information from individuals' credit files which fulfill certain criteria. Congress realizes that dangling that carrot in front of college students, for instance, encourages repayment of defaulted student loans. It should come as no surprise that creditors in other financial markets are familiar with this practice.

If you need more proof, read section 609(c)(2)(E) of the NEW Fair Credit Reporting Act that President Clinton signed in September of 1996, which reads, in part:

"...a consumer reporting agency is not required to remove accurate derogatory information from a consumer's file, unless the information is outdated under section 605 or cannot be verified."

Notice the wording above: "is not required to remove." It is very interesting that the law does not say that accurate information "cannot" be removed, but only that credit bureau is not required to remove it.

Congress has repeatedly validated this fact. One shining example is the area of student loans, where the law specifically allows repayment of a defaulted student loan to trigger *the removal of all indicators of past debt from one's credit file*. This program, labeled by congress as "rehabilitation," is an undeniable precedent of accurate information being deleted after the debtor fulfills a predetermined payment plan.

Now, there *is* law that says a creditor cannot knowingly add wrong information to someone's file, but the subject of removing accurate information is mysteriously avoided. The truth is the FTC and the bureaus themselves spend a lot of money trying to convince consumers otherwise.

Why? Powerful lobbies and money, of course. Verifying mistakes on credit reports creates more work for the credit bureaus, thus increasing their labor costs. Bureaus save millions of dollars a year by convincing us that the consumer is virtually powerless. But Congress deliberately worded things to leave the door wide open, and in at least one case drafted law specifically allowing for the removal of accurate but damaging items.

Many creditors have an agreement with the credit bureaus that they will not allow a negative listing to be deleted upon settlement. Larger creditors, such as huge credit cards or banks will require more pressure before they will agree to delete a negative listing, but virtually every creditor will give in with the right amount of convincing.

Every creditor who reports to the credit bureaus can also change any of the information they report. In most credit organizations, there are dozens of people with the authority to make changes on the credit report. The bottom line is that anything a creditor is responsible for reporting and confirming, a creditor can change.

Why Should I Regularly Review My Credit Report?

Identity Theft/Fraud: With identity theft on the rise in the United States, the number one reason to review your credit report at least once a year is to detect and stop fraud—before you need your credit.

Buying a Home or Car: Know ahead of time what appears on your report to help you shop for the best rate and take care of inaccuracies or past due balances.

Divorce: You'll need to evaluate your financial position with your attorney. Make sure you check to see if there have been any accounts opened that you might not have known about.

For How Long Does Negative Information Appear On My Credit Report?

The Fair Credit Reporting Act (FCRA) requires that most negative credit items be deleted from your credit bureau file after seven years. Exceptions include bankruptcy, which can be reported for up to ten years. Inquiries usually remain in your credit file for 24 months.

The credit grantor or credit bureau has the right to remove negative credit information whenever they please. There is no law stating that accurate information must remain in your credit file for any length of time, only that certain items cannot stay on file for more than seven years.

All of these limits represent what is *supposed* to happen. The reality is that many credit items will not be automatically deleted unless you demand it using the proper procedure. Also, every time you make a payment or other arrangement with a creditor, the clock is reset to zero, so accounts opened 15 years ago can still be legally reported on your file. Use the information in this publication to ensure that this doesn’t happen.

Who Can Look At My Credit Report?

If you rent, you have probably already been through a credit check to determine your worthiness as a renter. Anyone who can prove a valid business purpose (and has your permission) can view your credit file. The Fair Credit Reporting Act (See the *Consumer Rights and Laws* section) has specific details.

Most credit grantors are not allowed by the credit bureaus to show you your own credit report. However, credit bureaus and other companies do allow you to purchase your personal credit report for a fee or provide one for free if that particular bureau's report has been used to deny you credit.

What Is Credit Scoring?

There are two types of credit scores. The most-commonly referred to are the generic credit scores (generated by the credit bureaus). Each credit bureau generates its own credit score, such as Experian's FICO credit score and Equifax's Beacon score. The bureau-based credit scores draw on statistics from a large number of consumers across a variety of accounts.

Custom scores are generated by individual lenders who rely on credit reports, but also other information (such as account history) from their own portfolios. Scores are not just used to rate the creditworthiness of consumers. Lenders also use scores to predict consumer response to offers sent in the mail, the likelihood that account holders will file for bankruptcy or that a consumer will move their account to another lender.

Credit scoring is a grading system creditors use to help determine whether to extend 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 and a "secret formula" computer program called an algorithm; 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, that is, how likely it is that you will repay a loan and make the payments when due.

The score is also commonly referred to as a FICO score (named after Fair, Isaac Corporation), although now each bureau uses their own scoring system:

Experian: FICO

Equifax: Beacon

TransUnion: Empirica

Each score will be different, sometimes dramatically so. But if the same credit history shows up on all three bureau files, their scores should be very close.

Your credit score is a fluid number, and it changes as the elements in your credit report change. For example, payment updates or a new account could cause your score to fluctuate. There are many different credit scores used in the financial service industry. Your score may be different from lender to lender (or from car loan to mortgage loan), depending on the type of credit scoring model that was used.

Range Of Credit Scores

Your score will be between 340 and 850 points. A higher score indicates a better candidate for credit. There are three general categories of borrower:

Prime If your credit score is above 660, you are considered a "prime borrower" and should have few problems obtaining a good interest rate on your home loan, car loan, or credit card. For purposes of a home loan, many banks consider 660 or even 640 to be acceptable, enabling you to qualify for the best rates and lowest down payments.

Sub-prime If your credit score is between 580 and 660, you may be considered a "sub prime" borrower and will likely pay a higher interest rate on your loan and require a higher down payment on a home.

Forgetaboutit If you're credit score is below 580, you can forget about getting reasonable rates or terms on credit. You can still get a credit card but you will likely be hit with a security deposit or high acquisition fee. In addition to that, your interest rate will likely be 22 to 23%. You can forget about most home loans and the majority of new car loans at this score. Below 580 is no-man's land. You will pay much, much higher interest and unnecessary fees. You may even pay more for insurance rates. A very low score can even prevent you from getting a job with many companies.

Following is a quick summary of credit categories:

720+ Excellent credit; you will get the best rates and terms on all loans.

660-719 Good credit; you will likely get the best rates on most mortgages, but some credit grantors may take a closer look at your file.

580-659 Higher risk; you may not be eligible for the best rates and products. Some credit items may not be available.

Below 580 Credit options will be limited or not available. Lender will need to consider other information in your application.

How Is A Credit Score Calculated?

Although each credit bureau has its own unique system for compiling a credit score, the scoring models have been normalized so that a numerical score at one bureau is the equivalent of the same numerical score at another. Thus, a score of 700 from Equifax will be equal to a score of 700 from TransUnion or Experian, even though the calculations used to determine those scores are different at each bureau.

Your credit score is generated by a computer analysis of relevant information from your credit report, such as how much money is owed and whether payments have been made on time. Then that score is compared to the credit performance of consumers with similar profiles.

The scoring system awards points for each factor that helps predict who is most likely to repay a debt. Your points are totaled to arrive at a credit score, which ultimately helps predict how likely it is that you will repay a loan and make payments on time.

The score is calculated based on a mathematical model using up to 33 different factors about your history. The formulas are proprietary and the companies will not release them. In fact, there's more than one formula. Different credit-reporting agencies and lenders have customized variations. So you don't really have just one score, you have many scores.

What goes into the score? The different factors fall into five groups. The first is your **payment history**: how good you've been about keeping up with your payments. A bankruptcy would be considered here. Any late payments or charge-offs are also considered. Remember that this isn't an all-or-nothing proposition. So one missed payment doesn't doom you to a low score. But a pattern of late charges will certainly hurt.

Next, the model will consider your **outstanding debt**—how many accounts are open and how much debt you have. The model will give you the highest score if you have some credit, but not too much. Having one or two open accounts that are fully paid off each month will actually help your score.

The model also considers your **credit history**. You get more points if you've had an account for a longer period of time. The theory is that if you've been consistent over a number of years, you're more likely to continue responsible behavior. The pursuit of new credit can be a potential minefield to your score. The model considers how many new accounts you've opened. But, more than that, it also looks at how many times you've asked for credit.

Now this is where it can get interesting. The model doesn't always know why new requests for credit are coming in under your name. Suppose you're out shopping for a new car and visit a number of dealers and ask each of them to find the best rate for a car loan. Depending on how they get the information, it's possible that they can generate a number of **new queries** on your credit. All those queries can actually lower your score by making it look like you're out there trying to get a bunch of new credit.

Finally, the formula includes the **types of credit** in use. You'll receive a different rating for home and auto loans than for bank and store credit cards. And installment loans will likely count against you.

Now that we know a little about what goes into the formula, let's look at the primary factors that can cause a low score. In no particular order they are:

1. Delinquency on accounts.
2. Total owed on accounts too high.
3. Too many or too few bank revolving accounts.

Other negative issues are having too many open accounts with balances and having loans from consumer finance accounts (companies that loan to people with credit challenges). These are only a few possibilities. Remember, the calculation includes up to 33 factors.

What Constitutes A Good Score?

A credit score is not like a grade you might receive in school where 100 is the best possible score and anything less means that you answered a question incorrectly. Certain elements on your credit report raise your score and certain elements lower your score.

The negative factors (usually isolated on your credit reports) illustrate what is hurting your score the most. Just because you don't have any items significantly hurting your score doesn't mean you receive the maximum points for the elements helping your score. For example, if two individuals had exactly the same credit report except for the length of credit history, the person with the longer credit history would still receive a higher score, even if neither one had any negative information.

Only 3% of the U.S. population has a score of 770 or higher. As stated previously, each of the three credit bureaus creates its own score based on their own formula. The scores can range from 340 to 850 with a higher score indicating lower risk (technically, they can go higher than that, but almost nobody achieves higher than 850).

The magic number among credit scores is 770. With a credit score at or above this, you can qualify for just about any type of credit at the most favorable rates, although 720 or above is sufficient for most credit. For good rates on home loans, a score of 660 or better is usually required. Anything below this is often considered "sub-prime" and will have higher interest rates and require other compensating factors like higher down payments.

Why Is Credit Scoring Used?

Lenders look at many things when making a credit decision, including your income and the kind of credit you are applying for. However, your credit score does not reflect these facts as it only evaluates the information retained by the credit bureau.

Why do lenders use your credit score in their lending decisions? Because they discovered that there is a direct correlation between credit scoring and the odds of your becoming delinquent on your monthly mortgage payments.

How Is A Credit-Scoring Model Developed?

Remember, there are two types of credit score: bureau generated and lender generated (custom). Some lenders use the bureau score exclusively, but most consider the other factors (employment, length of time at residence, income) along with the credit report, since these items do not appear on the bureau reports.

To develop a **custom credit-scoring model**, a creditor (NOT the credit bureaus) selects a random sample of its customers or a sample of similar customers if their sample is not large enough, and analyzes it statistically to identify characteristics that relate to creditworthiness. Then, each of these factors is assigned a weight based on how strong a predictor it is of who would be a good credit risk. Each creditor may use its own credit scoring model, different scoring models for different types of credit, or a generic model developed by the credit bureaus.

Lender-based credit scoring models use information from credit reports, but it is not as simple as having a high enough credit score. Your credit score is only one of the factors they consider. For instance, mortgage companies often insist that you have a certain number of credit items (or "trade lines"). Creditors also look for length of credit history and other items that give them an idea of your credit worthiness. Each creditor develops their own scoring model, which is why you may get approved for a Macy's card, but not a Sears’s card.

How Can I Improve My Score?

Do’s

1. **Pay your bills consistently and on time.** Payment history typically is a significant factor. It is likely that your score will be affected negatively if you have paid bills late, had an account referred to collections, or declared bankruptcy, if that history is reflected on your credit report.

2. **Maintain a consistent and long credit history.** Generally, models consider the length of your credit track record. An insufficient credit history may have an effect on your score, but that can be offset by other factors, such as timely payments and low balances.

3. **Check your credit report for errors and have them removed.** The best way to do this is with the credit monitoring services available from each credit bureau. Each bureau charges about $60 a year for this service, but that usually includes unlimited credit reports and lots of other services. It never affects your score or counts as an inquiry to request and check your own credit report.

4. **Keep your debt to reasonable levels.** The scoring models want you to have balances of less than 75% of your available credit limits. The formula considers a balance above 75% as a warning sign of impending trouble. Carrying a zero monthly balance is the wisest use of your money.

5. **Keep unused credit limits at a reasonably low level.** If you carry a dozen cards, each with $3,000 in available credit, the model assumes that you could go on a buying spree. You know

that you won't do that, but the scoring model doesn't. If you find that you can't bear to close some of the accounts, at least call and have the credit limits reduced.

6. **Keep balances low** on credit cards and other "revolving credit." High outstanding debt can affect a score.

Don'ts

1. **Don't pay your bills late.** Also, be careful of automatic debit programs that pay your bills directly. If there is a mistake of any kind, you are still responsible for ensuring that the bills are paid.

2. **Don't open accounts just to have a better credit mix**—it probably won't raise your score. Apply for and open new credit accounts only as needed.

3. **Don't just move debt around.** Pay it off instead. Also don't close unused cards as a short-term strategy to raise your score. Owing on the same number of cards, but having fewer of them open may actually lower your score.

4. **Don't get lazy about your credit.** Pay attention. Your credit is one of the most important assets you possess.

5. **Don't co-sign on other people's loans.** This is a terrible idea, even for family. If you do co-sign, insist that they pay you directly. Then, pay the bill yourself so that you can ensure its prompt payment.

6. **Don't apply for too much credit at one time.** Sometimes the computer models have a hard time telling the difference between someone shopping for a new car and a borrower who's desperately trying to find money to avoid bankruptcy. If you have applied for too many new accounts recently that may negatively affect your score. However, not all inquiries are counted. Inquiries by the consumer (like when you order your own credit reports) or by creditors who are monitoring your account or looking at credit reports to make "prescreened" credit offers are not counted. Other inquiries can cost several points each, which could be enough to disqualify you from the credit you want.

How Will A Specific Action Affect My Score?

Simply closing two accounts not only lowers the number of open installment accounts (which generally will improve your score) but it also lowers the total number of all open accounts (which generally lowers your score).

Furthermore, such an action will affect the average age of all accounts that could either raise or lower your score. As you can see, one seemingly simple change actually affects a large number of items on the credit report. Therefore, it is impossible to provide a completely 100% accurate assessment of how one specific action will affect a person’s credit score.

What Factors Affect My Credit Score?

There are basically ten negative things that look the worst on your credit report, listed from the best to the worst:

1. Credit inquiries.
2. Credit rejections.
3. Late payments.
4. Past due and unpaid payments.
5. Court judgments.
6. Collections.
7. Loan defaults/debt consolidation.
8. Repossession.
9. Foreclosure.
10. Bankruptcy.

Previous Credit Performance / Payment History (35%)

The more recent the late payments, the lower your credit score. In fact a 30-day late payment on your credit report today may hurt more than a bankruptcy seven years ago. The last 18 months are the most important to consider.

Then there are the derogatory items that really hurt like: collections, charge-offs, judgments, liens, repossession, bankruptcy and foreclosure. Following are items considered in evaluating credit performance:

Payment history on your accounts. These include credit cards, retail accounts (department store credit cards), installment loans, finance company accounts and mortgage loans.

Collection items and public records. This includes judgments, bankruptcies, suits, liens, collection items and wage attachments. Most of these are considered quite serious, although older items count less than recent ones.

Negative information and late payments are determined using four factors:

Recency How long ago was the last delinquency? A 30-day late payment made just a month ago will affect your score far more than a 90-day late payment from years ago.

Prevalence How many credit obligations have been delinquent?

Severity What level of delinquency did the item reach? How late was the payment made? 30 days? 60 days? 90 days? Or worst of all, is it still outstanding?

The number of negative items as compared to your total amount of available credit. For instance, five accounts with a total three late payments are much worse than twelve accounts with a total of three late payments. One of the important considerations is how many accounts show no late payments. A good track record on most of your credit accounts will increase your over all credit score substantially.

Credit Utilization / Amount Owed (30%)

Having credit accounts and owing money on them does not mean you are a high-risk borrower with a low score. However, owing a great deal of money on many accounts can indicate that a person is overextended, and is more likely to make some payments late or not at all.

Part of the science of scoring is determining how much is too much for a given credit profile. Having available credit can actually help your debt-to-credit ratio. Your total indebtedness includes the following considerations:

Total amount owed on all open accounts. Paying off your credit cards completely every month doesn't mean that those accounts won’t show a balance on your report. Your total balance on your last statement is usually the amount that will show in your credit report.

Number of accounts you have open and how many of them have balances.

A high number of open accounts, even with small balances, can indicate higher risk of over-extension. This is considered in your credit score but most lenders leave it to their discretion, as they have access to your income amount. It is generally good not to have too many credit card accounts. About three is right.

Percentage of the total credit available to you that you are using. Are you close to maxing out your limits? For example, if you have a credit card with an available credit line of $1,000 and you have a current balance of $850 or more, then you are nearly “maxed out.” Having several credit cards or other debts with balances approaching the credit limit will affect your score negatively, even if you have always made your payments on time. Your credit score will factor your overall ratio of debt to your overall limits.

The table below demonstrates a Total Debt Ratio calculation.

Total Debt Ratio			
Account	**Amount owed**	**Limit/Loan amount**	**Percentage**
Visa	$800	$1000	80%
MasterCard	$150	$1000	15%
Car loan	$20,000	$25,000	80%
Home loan	$80,000	$200,000	40%
Total	**$100,950**	**$227,000**	**44%**

Amount Of Time Credit Has Been In Use / Credit History (15%)

Generally speaking, the longer the credit history you have, the better your score. However, this factor only makes up 15% of your total score, so even young people, students or others with short credit histories can still score high as long as the other areas are strong as well.

Here are the considerations for length of credit history:

How long your credit accounts have been in the credit bureau's file.

The age of your oldest account and the average age of all your accounts.

How long it has been since you used certain credit accounts, as well as the mix of older and newer trade lines.

Applying For New Credit (10%)

The credit bureaus have changed some of their calculations to account for these new trends. Specifically, they now treat a group of inquiries—which probably represents a search for the best rate on a single loan—as though it was a single inquiry (note: this only applies to auto or mortgage loan inquiries.) For example, auto loan inquires that are within 14 days of each other should only count as one inquiry.

Your score takes into account the following regarding applying for new credit:

How many new credit obligations have recently been assumed? Opening several credit card accounts at the same time can look bad. What the bureau's scoring models look for is "To what extent is this consumer trying to open new credit accounts?"

How long it has been since you opened a new account? Primary consideration is given to:

1. Number of inquiries in last six months
2. Number of accounts opened in last year
3. Number of months since most recent inquiry

There are no good inquiries. Inquiries are typically seen as a request for credit and thus are factored as if you are searching for credit. Every time you fill out one of those credit card applications to get a free gift, you are also getting a free inquiry. Every time you fill out an online application for a credit card, or other type of loan, you are getting an inquiry. Too many inquiries looks bad. While there are no good inquires, there are neutral inquiries. These inquiries are most often known as:

1. **Consumer initiated.** A request for your own credit report shows as a consumer inquiry (provided you don't have a friend in the mortgage business pull your report).

2. **Pre-Approval.** If a potential lender has viewed your credit reports without your prior consent in order to determine whether they want to offer you a loan, this is not factored into your score. However, once you fill out a credit application, your full report will be reviewed and a "bad" inquiry will appear on your reports.

3. **Periodic Review**. Many lenders will periodically review the credit reports of their current customers to see if there have been any major changes to their credit reports. If the lender discovers that your credit score is now too low for their standards, they may close your account. These inquiries created as a result of the periodic reviews are not supposed to be factored into your credit score.

Types Of Credit (10%)

The final 10% takes into account how many credit items are reported for large installment bank or credit union loans versus finance companies versus travel and entertainment cards or department store cards, etc. A healthy mix of different types of credit (installment loans, retail accounts, credit cards, and mortgage) is not a key factor in determining your score but it *can* help, especially if your credit report doesn't have a lot of other information on which to base a score. It's not a good idea to open different types of accounts just to improve this factor because it will reduce your score overall. You should never open accounts you don't intend to use.

What type of accounts you have, and how many, can make a big difference. The optimal ratio of installment versus revolving accounts depends on your profile and differs from person to person. One factor that seems to have significant influence is the percentage of open installment loans (such as automobile loans). Too many can lower this portion of your score.

How Long Does It Take To Rebuild A Score?

Of course, **just because something is supposed to come off your credit report after a certain period of time doesn't mean that it will.** The system is desperately flawed and you may have to take action to remove items that should have already been removed automatically.

CHAPTER 4

Credit Improvement

There are three ways to improve your credit:

1. Remove negative credit items from your credit report.
2. Add positive items to your credit report.
3. Improve other aspects of your credit profile.

It is possible to do all of these things, but before discussing these options, it is important to understand the significance of improving credit.

Removing Negative And Erroneous Items From Your Credit Report

Your particular problems may be serious or they may just be annoying, but the bottom line is: if you've got negative and erroneous items on your credit report, then you are suffering. **Each derogatory credit item can deduct 20 to 50 points from your credit score**, with the most recent items representing the most harmful.

The good news is: there is a way to remove these items from your credit report. Federal law requires that upon receiving a dispute, the credit bureau must investigate the item. **If a disputed item cannot be verified as correct within a reasonable period, it is automatically removed from the report.**

Generally, creditors will only maintain credit account information for two years. **If you challenge an account that is more than two years old, chances are the records won't be available for verification.**

Self-Directed Credit Improvement - The Best Approach

The ideal credit-improvement strategy is a self-directed one. The difference between self-directed and do-it-yourself is the amount of work you have to do yourself. Doing it yourself means that you have to write all the letters to the credit bureaus and that you rely on dubious instruction from unreliable sources.

Self-directed credit improvement means that you have received a program that enables you to greatly simplify the process. This kind of program usually does not require that you write any letters and provides simple, professional instruction that takes into account all appropriate laws.

How To Get A Copy Of Your Credit Report

Fortunately, the bureaus have made it easier to obtain your credit reports via the World Wide Web.

You can also find many companies licensed to sell you copies of your credit report, usually at a reasonable fee. In addition, these companies usually have good customer service, offer immediate online delivery, and often offer a "three-in-one" report that contains information from all three major credit bureaus in one report. Be aware, however, that it may be difficult to use these "three-in-one" reports in the dispute process. The Bureaus prefer their own unique report.

In addition, you are entitled to a free credit report if a credit grantor used that report (from that particular credit bureau) to determine you unworthy of credit, employment or insurance. You have 60 days after being declined to obtain your free report. You can also get a free copy if you are unemployed or think you are a victim of credit fraud. Otherwise, you will have to purchase one for around $10 each.

How To Order Your Credit Reports

Step 1: You will be able to obtain your reports by calling the three credit bureaus directly or going to their web site:

Experian 1-888-397-3742 www.experian.com

TransUnion 1-800-888-4213 www.transunion.com

Equifax (call 1-800-555-1212 for latest number) www.equifax.com

Follow the automated prompts and answer every question. Often, the system will ask you to verify your identity by answering questions about existing credit accounts. For that reason, make sure you have your bills nearby in case you need some information from them. There is a fee to order reports via the automated telephone or online systems.

Step 2: If you are unable to obtain your credit report by phone or web, address an envelope to each of the bureaus and put your return address on them. The address for each bureau is available by calling the bureau's toll-free number above or by going to their web site and clicking on Contact Us at the top of the page. The credit bureaus frequently change their mailing addresses in order to make it difficult for consumers to order their reports, so please call and verify the addresses before mailing out the forms.

Step 3: Make four copies of your driver's license (if your license doesn't have your current address on it, also copy something else that shows your address, like a utility bill in your name, etc.) and your social security card (or anything with your social security number on it, like a pay stub). You can copy these items on the same sheet of paper. Keep one of the copies for yourself.

Step 4: On the front of the copies from step 3, write "Please send my credit report to this address:_____. I have enclosed the appropriate dollar amount."

Step 5: Place the appropriate money order and copy of driver's license and social security card.

in the envelope matching the bureau. Make sure that the money orders are made out to the credit bureau and that they match the envelope.

How To Read A Credit Report

yourself. If not, your reporting agency is required to answer any and all questions to help explain your report. Remember, you have the right to know. Also, please remember the information on your report is based on how it was given to the bureau by the subscriber/ lender.

All of the above items will fall under one of the five sections contained in a credit report:

1. Personal information.
2. Public record information.
3. Collection agency account information.
4. Credit account information.
5. Inquiries.

All of the sections are easy to read and understand with the exception of two: the credit account

Credit Account Information

M = Mortgage

C = Check credit (line of credit)

Therefore, based on the above, you could quickly go down the relevant column in your credit file and **the following alphanumeric combinations would be indications you have an excellent payment history: O1, R1 or I1. Of course, you don't want to find anything that ends in 2, 3, 4, 5, 7, 8 or 9.**

Inquiry Section

Credit bureaus sometimes use coding in the inquiry section (section where those who have pulled your credit file are listed). For example, Equifax uses the following abbreviations:

PRM = Your name and address were given to a credit grantor, but nothing else. For example, a credit card company might offer you a "pre-approved" credit card based on this information. Any item marked with PRM will not count against you as an inquiry.

Review Your Credit Report

Now that you have the credit reports in hand, review them very carefully. Understanding your credit report is very important. Every bureau uses different codes and abbreviations, so don't feel intimidated. **After you have received your report and have decoded the information, review it carefully. Are there any:**

Errors and/or inaccuracies

After reading the laws included in this publication, you may see other reasons to dispute your credit report, but, for now, concentrate on finding obsolete, incorrect, or misleading information.

Some reports are easier to read than others. Experian puts an asterisk next to all negative items. TransUnion lists all negative entries under one section and all positive entries under another section. Equifax does not indicate an entry as negative or positive—you must determine an account's status by viewing each entry.

Once you have noted each questionable item, you should rank them. Rank the most damaging information first, followed by the next most damaging, etc., and finally those items which are neutral. Do this for each credit report, as they may not all have the same questionable information on them.

The following ordered list should give you an idea of the significance of derogatory information. From most damaging (1) to least damaging (10):

1. Bankruptcy
2. Foreclosure
3. Loan default (charge backs)
4. Repossession
5. Court judgments
6. Collections
7. Past due payments

8. Late payments

9. Credit rejections

10. Credit inquiries

Also, look carefully for the following items:

1. If you have paid off an account but it is still listed, make sure the report lists a zero balance. In particular look for:

2. Incorrect or incomplete name, address or phone number

3. Incorrect social security number or birth date.

4. Incorrect, missing, or outdated employment information

5. Incorrect marital status—a former spouse listed as your current spouse.

6. Bankruptcies older than 10 years or not identified by the specific chapter of the bankruptcy code.

7. Lawsuits or judgments older than seven years.

8. Paid tax liens older than seven years, delinquent account older than seven years or that omit the date of the delinquency.

9. Credit application inquiries older than two years.

10. Unauthorized credit (not promotional) inquiries—credit-reporting agencies usually do not remove these at a consumer's request, but it never hurts to ask.

11. Commingled accounts—credit histories for someone with the same name or similar social security number.

12. Duplicate accounts—this may occur when the creditor reports the account as both installment and revolving, or when you move and your account is transferred to a different location. Collection accounts may also appear from the original creditor and the collection agency. It is better to dispute them both for inaccuracy than for duplication.

13. Premarital debts of your current spouse attributed to you.

14. Lawsuits you were not involved in.

15. Incorrect account histories—such as a late payment notation when you paid on time or a debt shown as past due when it was discharged in bankruptcy.

16. Paid tax, judgment, mechanic's or other liens listed as unpaid.

17. A missing notation when you disputed a charge on a credit bill.

18. Closed accounts incorrectly listed as open.

19. Accounts you closed that that don't indicate, "closed by consumer."

20. Incorrect aliases.

21. Incorrect balances. If a balance is listed too high, you should correct it. The balance

reported is the balance on the date the creditor reported the information. If the balance is correct as of the date shown, it is not necessary to dispute the item.

22. Accounts that have been paid off can still be listed on your report, although they should indicate that you've paid them off.

23. If you've been through bankruptcy, both the public record information about the fact that you've been through bankruptcy can be listed and the individual accounts that were discharged may also have a notation that they were discharged may also have a notation that they were included in your bankruptcy.

Disputing Your Credit Report

As you proceed through the following steps, keep copies and records of all correspondence you send and receive. If possible, when corresponding with these agencies, send everything by certified mail, return-receipt requested. Make sure you obtain a cash receipt and retain a copy of the certified mail receipt. These will serve as your proof of mailing. If information that was removed from your credit report should reappear later, you will have the documentation to force the credit agency to permanently delete this entry.

Here are the steps required to restore your good credit:

1. Obtain Your Credit Reports
2. Review Your Credit Reports
3. Request Correction

Enclose any documentation you have that will support your claim. It is best to make copies of such documentation and keep the original yourself. Use words like "detrimental" or "damaging," and stress how the information could jeopardize your future creditworthiness. This is very effective if used correctly.

Below is a list of statements you should make and shouldn't make when disputing your credit items:

Good Reasons to Dispute:

This account is not mine. Please remove it.

This account was never paid late. Please update it to show "Paid in Full, Never Late."

This item is listed late due to a bank error. Please remove or update this entry.

This information is inaccurate. Please remove this item from my report.

I did not authorize this inquiry. Please remove it.

Bad Reasons to Dispute:

The collection agency said this wouldn't be listed on my report.

I got laid off and the bank said I didn't have to make a payment for a couple of months.

The bureaus may attempt to bully you into believing that your request is frivolous, or even unlawful. But the credit-reporting agencies are required to assume that all disputes are bona fide, unless there is clear and convincing evidence that it is not. A blanket dispute (i.e. all information is challenged) may be considered evidence that the dispute is frivolous, if you fail to provide any allegations concerning specific items in your file.

You will now write a letter to each credit bureau, requesting an investigation to verify the status of the most damaging item reported by any of the agencies, and asking that they correct the information.

Removing Inquiries

Too many recent (within the last six months) inquiries indicate to a potential credit grantor that your debt-to-income ratio may be much higher than you say. Most creditors disregard inquiries once they have been on your credit report for one year or more. This may not help your situation if you need credit right away or if applying to a creditor who looks at all of your inquiries.

Add New Positive Credit References

Some creditors such as gasoline companies, furniture stores, and finance companies will not report to credit bureaus unless you become a couple of months delinquent. If you would like them to report on a monthly basis then you can request this of them.

Landlords and other people who you pay on a monthly basis can also report to the credit bureaus. Some people have been know to request that their landlord report their prompt payments to the major credit bureaus on a monthly basis. The fee (around $10 a month) for doing this is usually.

How To Put Your Positive Credit Items On Your Credit Report

You can write to the credit bureaus or a creditor and ask that certain accounts be added to your credit file. The credit bureaus do charge a small fee to add information to your credit file, but it should not cost you more than $10.00.

Unconventional Credit Improvement Strategies

Below are unconventional methods you can use to improve your credit. These are powerful strategies when used correctly.

Do a credit audit. Under the Fair Credit Reporting Act you have the right to ask tough creditors (not just the credit bureaus) for proof that you were late, didn't pay, etc. Write them a letter giving them 10 days to give you proof you were late, including all cancelled checks and backs of checks, etc. Tell them they must remove the derogatory item if they cannot provide proof. If they do not provide proof, write them another letter telling them they must delete the item (send all letters with mailing receipt). Then send a copy of your letters to the credit bureaus saying they.

The safest way to close a credit card account is by sending a certified letter to the customer service department of the card issuer. Ask the card issuer to close your account and to report your account to credit bureaus as "closed by consumer." In approximately 10 days, the card issuer should send you a letter confirming that your account is "closed by the consumer." If you don't receive the confirmation letter, follow up by calling the card issuer to make sure it closed your card and is reporting it properly to the credit bureaus. You may even want to get another copy of your credit report to make sure it is reported correctly.

CHAPTER 5

Applying For Loans And Credit Cards

Be Complete On Your Applications

If you call the creditor you want to apply to and ask them what credit bureau they subscribe to, you can then order a copy of that credit report, see what accounts are listed on it and then you can make sure you have the same accounts listed on your application.

Observe The 30-45 Rule For Approval

Many creditors (and all mortgage lenders) will examine how much debt you have in comparison to your income. Here is how it works: Add up your monthly payments on all your bills except your rent/mortgage and utilities. Divide your gross (before tax) monthly income by your monthly debts. You will get a percentage.

To obtain your monthly income, don't just multiply your weekly income by four or your bi-weekly income by two. This is because there are an average of 4.35 weeks in a month, not just four. Instead, multiply weekly income by 4.35 or bi-weekly income by 2.175.

For example: If your total monthly payments are **$1,400** and your weekly pre-tax income is **$800**:

$800 X 4.35 = $3,480 monthly income

$1,400 divided by **$3,480** = .40 (which is **40%**--your debt ratio)

Here are the ranges you need to know:

If your debt ratio is **30% or less**, you should have no trouble getting credit cards or other additional loans.

If your debt ratio is **31% to 44%**, your bills are on the high side and you might have some trouble getting additional credit.

If your debt ratio is **45%** or more, you will probably not get approved for any more credit.

There are some ways to lower monthly debt to get the necessary approvals. You can combine monthly credit card payments into one payment at a lower interest rate. You can also negotiate lower monthly payments with your existing creditors.

What Creditors Look For (in order of importance to them when evaluating your credit request):

1. A positive, up-to-date credit report with a high score.
2. A Master Card or Visa card with a perfect payment history.
3. A home with a mortgage and up to date payments.
4. An American Express and/or Diners Club card.
5. A job you have had for more than one year.
6. An address you have resided at for at least one year (if it's in your name, even better).
7. A current or paid off bank loan.
8. A department store credit card.
9. A telephone/utility bill in your name.

How Do Creditors Decide Whether To Extend Credit?

Understanding your credit report is an important step to obtaining an approval from a lender. They will be looking at the same things most common to loan approval. **It is important to order a copy of your credit report before you apply for a loan, credit card, or mortgage.** You will want to check it over very carefully looking for errors, erroneous information, outdated information, and to add any new information that may be helpful to you.

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%.

What Happens If You Are Denied Credit Or Don't Get The Terms You Want?

Rejection letters are sometimes called "adverse action letters." Two important pieces of information must be included in the rejection letter:

1. The reason why you were turned down for credit, which must be specific.
2. The credit bureau's name and address that was used for the credit decision.

If you are denied credit, the Equal Credit Opportunity Act requires that the creditor give you a notice that tells you the specific reasons your application was rejected and that you have the right to learn the reasons if you ask within 60 days. Indefinite and vague reasons for denial are illegal, so ask the creditor to be specific.

Acceptable reasons include: "Your income was too low" or "You haven't been employed long enough." Unacceptable reasons include: "You didn't meet our minimum standards" or "You didn't receive enough points on our credit scoring system."

Sometimes you can be denied credit because of information from a credit report. If so, the Fair Credit Reporting Act requires the creditor to give you the name, address and phone number of the credit bureau that supplied the information.

You should contact that agency to find out what your report said. This information is free if you request it within 60 days of being turned down for credit. The credit bureau can tell you what's in your report, but only the creditor can tell you the specific reasons why your application was denied.

Cosigning

You can use a friend or family member to cosign with you. It is best that they have very good credit or you may both be turned down. Cosigning is a big risk for the person who is doing the cosigning, so make sure you make them feel as comfortable as possible about cosigning with you. Show them your ability to repay the loan. Remember: if you fail to repay the debt and the cosigner has to step in and repay it and they can't, then you both will have ruined your credit history.

How Credit Card Companies Play "Gotcha"

Even if you pay your account in full there are still ways that the banks can manipulate the grace period to their advantage. Some have shortened the **grace period** from 25 to 20 days. If your company does this, give their customer service number a call and ask for the standard 25-day grace period. Many companies will change back just by being asked.

Another credit card company practice involves offering a very low rate, prompting many to transfer high balances. The problem is, if you are ever late on a payment, even once, the rate will jump to the highest rate allowed by law. Then you are stuck with a high balance AND a high rate. And with that recent late payment on your credit record, you aren't likely to qualify for another low interest rate card.

Beating The Credit Card Companies At Their Game

Credit card companies are required by law to post your payment to your account on the day it is received. But they often use some sly tricks to avoid doing that, legally. Here are some ways you can outwit the credit tricks, and make sure you don't fall prey to losing your low interest rate and/or having to pay a late fee.

1. **Be sure you write as neatly as possible.** Credit card companies are legally allowed to hold for five days and re-route all "illegible" payments to another department, and thus your payment will be "late" before it is posted.

2. **Never include an additional note about anything in with your payment.** If you are adding additional money in your payment for the principle, (i.e. making more than the minimum payment due), do NOT add an extra note with your check, and do NOT write on your payment stub. All payments received with extra notes are also legally allowed to be held and routed to a different department, and thus your payment will be "late" before it is posted.

3. **Make your payment twice every month, instead of just once.** If you break your payment in half, and send it in twice each month, making sure that both payments are received well before the final due date, you eliminate some of the interest which accrues. This may not be a huge amount per month, or may not seem like very much when you do this for just one credit card. But if you have multiple credit card debt, and you can afford to only make the minimum payments required, using this method will save you a significant amount of money when added up over time, and you won't have to spend any more money to pay your bill than you already are now.

Mortgages And Credit Scores

The most important reason to increase your credit score as high as you possibly can is that it can influence the interest rate you must pay. If your credit score is higher than 725, some lenders will reward you by lowering your interest rate by about $1/4^{th}$ of a percent. This translates into $12,000 savings on a $200,000 mortgage and a lower monthly payment. If it is between 700 and 724, it could be lowered by $1/8^{th}$ of a percent.

Other lenders might not reward those with good credit scores, but add on interest points for those with bad ones. In any event, it pays to have a high credit score because you will have a lower monthly payment and save thousands in added finance charges.

Keep in mind that a credit score of, say 500, is going to result in paying an interest rate that is 2 or more points higher than that offered to those with excellent credit. This doesn't sound like a big deal until you realize that it will result in a $400 or more higher monthly payment on the typical $200,000, 30-year mortgage loan. That's at least $144,000 more you're going to pay for your house!

General Rules To Determine Your Mortgage Credit Grade And Creditworthiness:

A credit score of 660 or higher usually means you have "good" credit.

A debt-to-income ratio greater than 36% usually lowers your credit grade.

Note: An example of an installment loan is a car payment. An example of revolving credit is a credit card.

A rating *[Credit score 660 or higher]*

Debt to income ratio: Range of 28% to 36%.

Mortgage: You have not been late with a payment in the last 24 months.

Installment loan: You have been 30 days late making payments 0 or 1 time within the last 12 to 24 months.

Revolving credit: You have been 30 or 60 days late with a payment 0 or 1 time in the last 12 to 24 months.

Additional requirements: Good/excellent credit during the last 2 to 5 years; no bankruptcy within the last 2 to 10 years.

Loan-to-Value Considered: 90 to 100%.

B rating [Minimum credit score 620]

Debt to income ratio: Around 50%.

Mortgage: You have been 30 days late with a payment 2 or 3 times in the last 12 months.

Installment Loan: You have been 30 days late with a payment 2 to 4 times during the last 12 months.

Revolving credit: You have been 30 days late with a payment 0 to 2 times in the last 12 months.

Additional requirements: You have no 60-day late mortgage payments; if filed bankruptcy, it must be discharged 2 to 4 years ago.

Loan-to-Value Considered: 85 to 95%.

C rating [Minimum credit score 580]

Debt to income ratio: Around 55%.

Mortgage: You have been 30 days late with a payment 3 or 4 times in the last 12 months.

Installment Loan: You have been 30 days late with a payment 4 to 6 times during the last 12 months.

Revolving credit: You have been 60 days late with a payment 2 to 4 times in the last 12 months.

Additional requirements: If you filed bankruptcy, it was discharged 1 or 2 years ago.

Loan-to-Value Considered: 75 to 85%.

D rating *[Minimum credit score 550]*

Debt to income ratio: Around 60%.

Mortgage: You have been 30 days late with a payment 2 to 6 times in the last 12 months; and 60 days late 1 to 2 times during the last 12 months.

Installment Loan: You have a few 90 and 120 day late payments during the last 12 months.

Revolving credit: You have a few 90 and 120 day late payments during the last 12 months.

Additional requirements: If you filed bankruptcy, was discharged within last 12 months.

Loan-to-Value Considered: 65 to 75%.

E rating [Credit score under 550]

Debt to income ratio: Around 65%.

Mortgage: You have a pattern of 20, 60, 90 and/or 120 day late payments.

Installment Loan: You have a pattern of 20, 60, 90 and/or 120 day late payments.

Revolving credit: You have a pattern of 20, 60, 90 and/or 120 day late payments.

Additional requirements: You may have a current bankruptcy or foreclosure.

Loan-to-Value Considered: 50 to 70%

Qualifying For A Home Mortgage With Bad Credit

Each mortgage broker uses one or more lenders to fund the home loans that come to her. The mortgage broker's job is to match you with the appropriate lender. For this service, you or the home seller may pay the mortgage broker **"points."** These points are equal to percentage points of the loan amount. If you are paying your broker "2½ points" on a $120,000 home loan, that will come to a $3,000 payment to the broker. Many brokers charge no points for very qualified buyers.

Some mortgage brokers will look at your less-than-perfect credit and suggest that you accept a "B", "C", or "D" paper mortgage. This means that the loan will require a larger down payment, a higher interest rate, better debt to income ration, and, of course, more points for the mortgage broker.

When a mortgage broker prepares your file for the underwriter (the lender), he or she will use a **Standard Factual Report (also called a "tri-merge")** to check your credit. The Standard Factual company is a business that compiles all three bureaus into one report. This company can aid in the deletion of negative credit listings.

CHAPTER 6

Credit Problems

Individual Or Joint Account?

Individual Account: Your personal income, assets, and credit history only are considered by the creditor. Whether you are married or single, you alone are responsible for paying off the debt. The account will appear on your credit report, and may appear on the credit report of any "authorized user." However, if you live in a community property state (Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, or Wisconsin), you and your spouse may be responsible for debts incurred during the marriage, and the individual debts of one spouse may appear on the credit report of the other.

Joint Account: Your income, financial assets, and credit history (and your spouse's) are considerations for a joint account. No matter who handles the household bills, you and your spouse are responsible for seeing that debts are paid. A creditor who reports the credit history of a joint account to credit bureaus must report it in both names (if the account was opened after June 1, 1977).

Unfortunately, there is no easy way to clear up an account that was supposed to be paid by a former spouse, but is now showing up on your credit report as delinquent. You can pay off the debt and collect from your ex, or you can dispute the item with the credit bureaus. However, you will not be able to merely say "my ex was supposed to pay this." They don't care. **It is 100% your responsibility and 100% theirs. If you don't like this outcome, it's best to avoid joint accounts.**

Authorized Users: If you open an individual account, you may authorize another person to use it. If you name your spouse as the authorized user, a creditor who reports the credit history to a credit bureau must report it in your spouse's name as well as in yours (if the account was opened after June 1, 1977). A creditor also may report the credit history in the name of any other authorized user.

How To Avoid Being A Victim Of Identity Theft.

Sign-up for credit monitoring services. Right now, about the only way to fight identity theft is to participate in the credit monitoring services now being offered by the credit reporting agencies (CRAs) and other commercial services. So far, these services are receiving good marks from consumer groups. A credit monitoring service works by notifying you immediately every time your credit file is pulled or something in your credit file changes. This way you are alerted to unauthorized activity and can address the problem when it first begins. You can catch the thief when he tries to open that first account in your name.

The fee for credit monitoring is about $60 to 80 per year, but it is fast becoming a necessity since there are 700,000 victims of identity theft each year in the United States and the number is climbing at an alarming rate. Think of it as insurance. Would you rather pay $80 per year for prevention or $1,000 or more, plus many stressful hours of your time to clean up the mess?

Check your credit file at least once a year. If you aren't interested in credit monitoring services, you should check your credit file with all three major credit bureaus at least once a year. Why? Because someone might obtain credit or a loan in your name at any time.