

# *Credit Scoring - How it Works*

Credit scoring is a statistical method that lenders use to quickly and objectively assess the credit risk of a loan applicant. The score is a number that rates the likelihood you will pay back a loan. **Scores range from 350 (high risk) to 950 (low risk).** There are a few types of credit scores; the most widely used are FICO® scores, which were developed by Fair Isaac & Company, Inc. for each of the credit reporting agencies.

Credit scores only consider the information contained in a credit profile. They do not consider income, savings, down payment amount, or demographic factors like gender, race, nationality or marital status. Past delinquencies, derogatory payment behavior, current debt level, length of credit history, types of credit and number of inquiries are all considered in credit scores. The score considers both positive and negative information in the credit report. **Late payments will lower the score, but establishing or re-establishing a good track record of making payments on time will raise the score.**

**Different portions of a credit file are given different weights:**

- **35% - Previous credit performance (specific to payment history)**
- **30% - Current level of indebtedness (current balance compared to high credit)**
- **15% - Time credit has been in use (opening date)**
- **15% - Types of credit available (installment loans, revolving and debit accounts)**
- **5% - Pursuit of new credit (number of inquiries)**

**The most important factor for a good credit score is paying bills on time.** Even if the debt owed is a small amount, it is crucial to make payments on time. In addition, try to: keep balances low on credit cards and other "revolving credit;" apply for and open new credit accounts only as needed; and pay off debt rather than moving it around. Also don't close unused cards as a short-term strategy to raise your score. Owing the same amount but having fewer open accounts may lower the credit score.

Recent changes minimize the negative effects that rate shopping can have on a mortgage applicant. If there is a consumer originated inquiry within the past 365 days from mortgage or auto related industries, these inquiries are ignored for scoring purposes for the first 30 calendar days; then, multiple inquiries within the next 14 days are counted as one. Each inquiry will still appear on the credit report.

**Every score is accompanied by a maximum of four reason codes.** Reason codes identify the most significant reason that you did not score higher. The reason codes can help a lender describe the reasons for higher than expected rates or loan denial. Scores are not part of the credit profile and are not covered by the Fair Credit Reporting Act.

**The credit report must contain at least one account which has been open for six months or greater, and at least one account that has been updated in the past six months for in order to get a credit score.** This ensures that there is enough information in your report to generate an accurate score. If one does not meet the minimum criteria for getting a score, they may need to establish a credit history prior to applying for a mortgage.