Understanding Your Credit Score

1. What is a "Credit Score"?

- A "numerical tool" that calculates the likelihood of you making your payments on time and in full. It is a non-discriminatory score since it is based on information in your credit file (see categories below) and does not consider race, gender, age, marital status, salary, occupation, etc.)
- The most common credit score is the "FICO"* score, which ranges from 300 – 850 points. The higher the score -- the lower the risk. Nationally, a score under **600** is considered high risk; a score of **723** is considered average risk; and a credit score of **760** or higher is considered low risk.
- For more information on the FICO score –go to: **www.myfico.com**

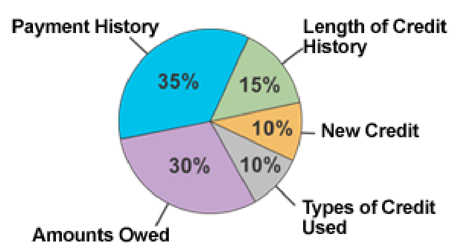
2. Why is my Credit Score important?

- Historically, over 86% of all lenders' decisions were based, in part, on credit scores.
- Employers sometimes use credit scores for evaluating job applicants.
- Landlords may use credit scores in selecting tenants.
- Insurance Companies may use credit scores to evaluate your risk.
- Utility companies may use credit scores to determine deposit requirements.
- A low credit score will cost you thousands of dollars in additional interest. The difference in total interest paid by a low-risk borrower (score = 760+) compared to a high risk borrower (score=600 or lower) is significant. In the below examples, the high risk borrower would pay an extra:
  - $2,100 in interest on $10,000 - 48 month Personal Loan (7% vs 16%)
  - $5,700 in interest on a $20,000 - 60 month Auto Loan: (5.85% and 15.5%)
  - $61,000 in interest on $100,000 - 30 year fixed rate Mortgage: (5.4% and 7.97%)

3. What makes up my "FICO" score and what is considered "average"?

If you're below average in one area, you will need to compensate with above average strengths in other areas.

- **Payment History (35%)**
  - 50% of consumers have never had more than a 30 day delinquency.
- **Amount Owed (30%)**
  - Roughly 50% of consumers: owe less than $1000 on each credit card; use less than 30% of their total credit card limit; and carry less than $5000 total non-secured debt.
- **Length of Credit History (15%)**
  - Average credit history is 14 years old.
  - Only 5% of credit histories are under 2 years old.



- **New Credit & Inquires (10%)**
  - Average Inquiries/New Credit: 1 per year.
    94% of consumers have less than 4 inquiries per year.
  - Statistically, people with 6 or more inquiries on their credit report are 8 times more likely to declare bankruptcy.
- **Type of Credit Used (10%)**
  - Average Consumer: 9 credit cards and 4 installment loans.

*Note: FICO is a trademark of the Fair, Isaac Corporation and the above statistical information is from their consumer website, located at www.myfico.com

4. How do I improve my Credit Score?

- **Pay your bills on time:**
  - A single 30 day delinquency can drop your score 50 – 100 points.
  - Multiple recent delinquencies can drop your score 100-200 points.
  - Remember – closing a previous delinquent or bad account does not make it go away – but its negative impact on your credit score will decrease over time.

- **Keep Credit Card Balances Low (below 50% of the credit limit)**
  - The closer you get to your credit card limit – the more points you lose from your credit score.
  - Payoff your debt – don't shuffle balances from one credit card to another.
  - Don't obtain additional credit cards to increase your total credit limit – it usually backfires.

- **If your credit file is limited, try to build the "average account age" or length of credit history:**
  - Don't close unused "older" credit cards. Pay them off and then cut the card up – but don't close the account until you have built up a larger credit history file.
  - Don't open several new credit cards at one time – it will lower your average account age.
  - Get a "Share-Secured" loan from the credit union. The loan is automatically approved, payments are through payroll deduction, and it will help build your credit history.

- **Build your credit slowly and wisely**
  - Only apply for credit when you need it. Excessive credit card accounts will lower your score.
  - Do **not** obtain a consolidation loan unless you cut-up the credit cards that created the debt. Statistically, most people who keep the cards end up twice as deep in debt within 2 years.
  - Do your comparison shopping for auto loans and mortgages within a **14 day period** as those credit inquiries only count as 1 inquiry and will not reduce your credit score.

5. How are credit scores used at the credit union?

- We use 2 national credit bureau credit scores as part of our 4 step evaluation process (see below).
  - One credit score measures the likelihood of serious delinquency;
  - The other credit score calculates the likelihood of future bankruptcy.

- You should be able to determine whether your application will be approved – and for how much – by reviewing the following 4 step process that we use on all loan applications:

  - **Step 1: If your debt ratio is 55% or below – move to step 2:**
    - Debt ratio = monthly expenses divided by gross monthly income
    - Most financial institutions use 40%. We use 55% to qualify more members.

  - **Step 2: If your credit history contains less than 2 current collection accounts – move to step 3:**
    - Bankruptcy: All included accounts are combined and count as 1 bad account
    - Note: You loan application may be disapproved if your credit history contains an excessive number of past collection accounts and/or charge-offs.

  - **Step 3: If your FICO credit score is 550 points or higher – move to step 4.**
    - Most financial institutions use a cut-off point around 620, many have increase it to 720, we dropped our cut-off to 550 to qualify more of our members.
    - A valid credit score must contain 4 or more credit accounts - with at least 1 year of credit activity.
    - Scores containing less than 4 accounts are scored at the "high risk" level.

- **Step 4**: **Once approved, the amount of financing depends on your actual credit score:** *(Note: if you don't know your actual FICO score, you can make an educated guess by reflecting on your past credit experiences and reviewing the "average" score criteria as shown on page 1)*
  - Score ranges:
    - Low Risk: FICO score of 750+
    - Medium Risk: FICO score between 621 – 749
    - Medium-High Risk: FICO score in Medium range – bankruptcy score in high
    - High Risk: FICO score between 550 - 620
  - Unsecured Personal loans: (repayment terms up to 60 months)
    - Low Risk: up to $20,000
    - Medium Risk: up to $7,500 to $15,000
    - Medium-High Risk : up to $5000 - $7500
    - High Risk: up to 100% of the applicant's gross monthly income.
  - Auto Loans: (includes motorcycles, boats, and RV's)
    - Low Risk: 108% financing
    - Medium Risk: 80% - 108% financing (depends on risk scores)
    - Medium-High Risk: 65% - 80% (depends on risk scores)
    - High Risk: 65% financing

6. How can I get more "Financially Fit" so that my credit scores will improve?

- **The Simple answer is: Build up your savings and Pay down your debt**
  - Building a savings account will reduce your dependency on loans (lower your debt level), plus help break the credit card "habit".
  - Paying down debt (especially credit card) will raise your credit score.
- **Savings Tips:**
  - Develop a realistic budget and then stick to it.
  - Pay yourself first – each payday –using Payroll Deduction. Start small and routinely increase the deductions amount – set a goal for to save 10% of each paycheck.
  - Build a savings account equal to 3 months (minimum) of your total monthly expenses.
  - Reduce "out-of-pocket" impulse buying as it is a frequent budget-buster. To get an idea as to how much you are spending, carry a small notepad and record all out-of-pockets expenses for a month or so. Then, include an out-of-pocket "allowance" in your budget and live within it.
  - Add pay raises/extra income to savings – not as a justification for new debt.
- **The "Stacking Method" for eliminating credit card debt:**
  - Cut-up as many of your credit cards as possible (only keep 1 or 2 major credit cards).
  - Start with the card that has the highest interest cost (card #1). Pay extra on that card each month (within your budget) until that card is paid in full.
  - Next, add the payments you were sending to Card #1 to your current card #2 payment. Continue sending in the combined payments until Card#2 is also paid in full.
  - Now, add the old Card #1 & #2 payments to the current card #3's payment.
  - Continue "stacking" payments until all cards are paid off.
  - Develop the habit (now) of paying off all new credit card charges when the bill arrives (Otherwise you will just be exchanging old debt for new debt).