

# Credit score: Why does it matter?



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Many people don't realize the importance of building and maintaining a good credit score to their overall financial well-being. Before you make any buying decisions involving credit, think about your overall financial situation and the long term impact of living "outside your means". The cost of bad credit may be more than you realize.

**What is a credit score? It is a number that signifies how likely you are to pay your bills or "honor your debt" or the "promise to pay" you gave when you took out credit.** There are different methods

of calculation used by the various credit reporting companies. Although the credit reporting companies use the same information, certain factors in an individual's credit report are weighted differently, giving you a range of scores across the different credit reporting entities.

Why should you care what your credit score is? Credit scores show how likely you are to honor your debts. **Credit scores are a key factor in determining both your eligibility for credit and the interest rates you will pay in relation to mortgages, car loans, and credit cards, as well as your car insurance rates, etc. Credit scores may affect your job opportunities as well because some companies look at a potential employee's credit score as an indicator of how responsible you are.** According to the Privacy Rights Clearinghouse, prospective employers may use credit reports to judge a person's responsibility level (eHow/creditscores-2013).

Credit scores range from 300 to 850. The higher credit score is the best. It can lead to easier access to credit when you need it, as well as the lowest interest rates. **This is because the higher credit scores lead the creditors to believe you are more likely to pay them back. If you are deemed more likely to pay them back, then you are considered less risky. As a less risky borrower, you are entitled to a lower rate.**

Thinking about buying a home? This is where you may feel the biggest impact from your credit score. **The difference in the interest rates offered to a person in Georgia with a score of 620 (5.551% APR-annual percentage rate) and a person with a 760 score (3.979% APR) is 1.572 percentage points, according to Fair Isaac's Web site (myFICO.com).** For example, on a \$250,000, 30-year mortgage, that difference would cost more than \$85,309 extra in interest charges over 30 years (according to Informa Research Services mortgage calculator)!! The difference in the monthly payment alone would be about \$236. When you move up to a \$500,000.00, 30-year fixed mortgage, the difference would cost \$170,617 and the monthly payment alone would be about \$474.00 more (myfico.com Loan Savings Calculator 2015). And at certain credit levels, you may not even qualify for a home loan at all, blocking yourself from even having that option.

As you can see, not maintaining a strong credit score may cost you plenty in the long-run. From a financial planning and investment perspective, the less money you are paying on your mortgage, your car payment and insurance, and your credit cards – the

more money you should have left to save and to invest for your future. This puts those with good credit scores ahead in both the short-term and in the long-run.

**You may not be able to control how your credit score is calculated, but you can control many factors that affect your credit score.**

There are a number of things that you can do that positively impact your credit score such as, always making loan, credit card, medical, and mortgage payments on time; managing the amount of overall credit you take out; paying all of your bills in a timely manner; minimizing the overall number of credit applications; minimizing overall debt levels; and by avoiding bankruptcy, foreclosure, and any repossession of property.

**One easy way to help ensure payments are made on time is to set up automatic debits to pay routine bills such as your mortgage, and to make at least the minimum payments on your credit card by the monthly due dates.** Also, if you cannot pay off your credit card balances in full monthly to avoid those interest charges, at least always make more than the minimum monthly payments.

It is important to be aware of your credit score, but even more important to know what information is showing up on your credit report where the information from which your credit score is calculated is listed. Checking your credit report at least once a year (I recommend at least three times) can help prevent identity fraud by allowing you to see if someone has opened credit in your name without your permission. It also provides you with an opportunity to identify and correct errors and problems with your credit report.

If you share a name with another family member, such as a son sharing a name with your father, you may be surprised to see errors in reporting your father's credit information on your record. You may also see credit that you paid off or closed still showing as active on your credit report. Unpaid medical bills seem to be a common factor affecting negative credit scores. **Any collections item, medical or not, can lower a person's credit score by as much as 100 points,** says a spokesman for myFICO.com. Typically, if you have a higher credit score, a negative item will hurt more than if you had a lower credit score. These are just examples of things you may need to challenge in writing to clear from your credit report to ensure your credit score is accurate.

The injury to your credit score will lessen over time, but collection items will stay on your credit report for seven years. Federal law requires negative items to drop off credit reports within that time. The only exception to that seven year time frame is bankruptcy, which can stay on a report for 10 years.

There are three major credit bureaus which you can check your credit score: Equifax, Experian, and TransUnion. However, **the website I recommend most is also recommended by consumer advocate Clark Howard at annualcreditreport.com. This site allows you to request a free credit report once every 12 months from each of the three major nationwide consumer credit reporting companies listed above, giving you three free reports annually.**

The decisions you make in every financial situation may result in either a better or worse credit score. The important message to remember is **you do have control over your this very important score through your financial decisions and how you honor your own debt. Your credit score may impact your financial health, your ability to get a job, and your ability to get the things you want in life.**