CREDIT AWARENESS:
The 5 Factors that Contribute to Your Score

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Introduction: The Purpose of Credit: How It Works and Why It Matters

Even though credit is one of the most important elements of life in the modern world, most people know far too little about how it actually works and why it is so important. It's not something that is taught in school, and this can lead many people to have a misunderstanding of how credit works. Eventually, this can lead to credit problems, and it can be very difficult to dig yourself out of this issue.

The goal of this book is to provide you with need-to-know information regarding your credit, and dispel some of the pervasive myths that surround it. Let's get started, so you can learn all of the basics that you need to know.

What Are the Three Credit Bureaus?

Who is it that keeps track of the credit? Who knows what problems you've had with your credit and comes up with your credit score. This is accomplished through the three main credit bureaus – **Experian**, **Equifax**, and **Transunion**.

The credit bureaus are responsible for collecting and maintaining information about an individual's credit. The information that they gather is then sold to lenders and creditors, as well as consumers. While there are many different credit bureaus, the three mentioned above are considered to be the main bureaus – the ones that most people utilize.

The bureaus have a large job. They will collect and maintain different types of information and details about individuals and their credit histories. This starts from the very first credit account opened.

Some of the information that the bureaus collect includes your repayment history, whether you miss or default on any payments, the amount of credit you have available to you and the amount that you are using, whether you have outstanding debts that are in collection, as well as various public records, including:

- Repossession
- Tax liens
- Foreclosure
- Bankruptcy

Additionally, the credit bureaus keep information about you that is not related to your credit. This includes your address, employers you have had and your current employer, and information about your salary. This is considered to be noncredit information, but it can still be important when businesses decide whether they want to work with you and provide you with credit.

For example, they might want to know how long you have been employed by your current employer before they are willing to extend any credit.

How Do the Credit Bureaus Get This Information?

Naturally, one of the next questions that you are likely to have is just how these bureaus obtain this type of information in the first place. It will typically come from locations where you have started to establish credit. If you have a credit card through a bank, for example, then it would be the bank that is funneling the information to the credit bureau. If you have a department store card, then it would be the department store, or their lending institution, that reports the information to the credit bureaus.

These companies will send regular updates on the accounts that you have open. The bureaus are also able to get information on you from public court records.

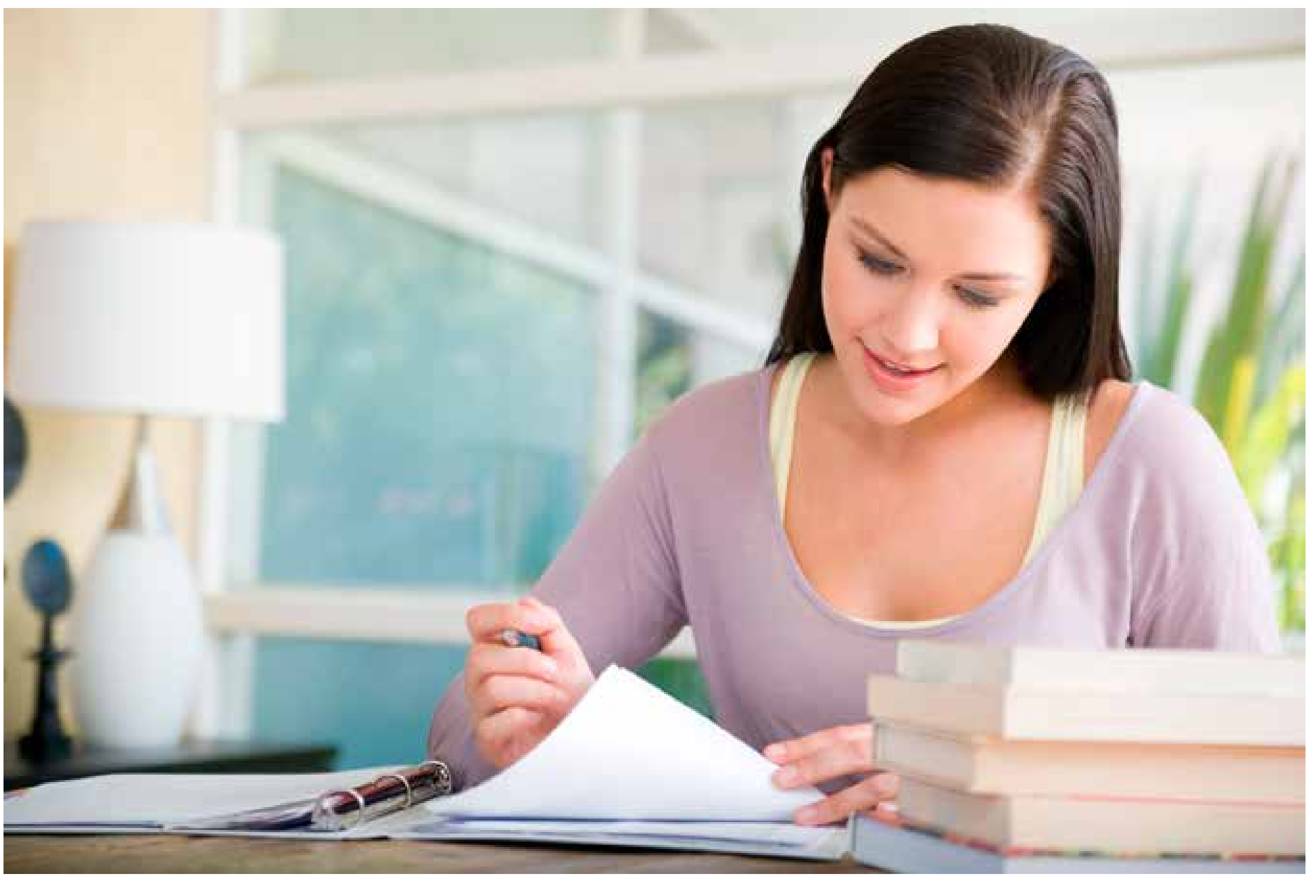
Who Uses Information from the Credit Bureaus?

There are many different companies that make use of the information gathered through the credit bureaus. The types of companies that most often come to mind include banks and other lenders, such as companies that issue credit cards. After all, they have a vested interest in making sure that you are going to be worthy of the credit they are offering.

However, these are certainly not the only types of companies that are going to be making use of this information. You will also find that insurance companies, landlords, debt collection agencies, and even employers will look to the credit bureaus to obtain information about you.

The bureaus will provide prescreening lists, which will then give the lenders a better idea of whether you will qualify for their offers. A credit card company might want to find only those customers who already have high credit scores. They might also want to find those who have a high credit card balance, and who might benefit from balance transfer cards.

If you have ever had prescreened offers coming into your mailbox and wondered how those companies decided to send you offers, it is quite likely that they received information from one of the credit bureaus. In many instances, the companies could be looking at the aggregate scores from across the three bureaus when they are making their decision. They feel that this may give them a better understanding of your creditworthiness and they can then determine whether they want to extend credit to you, and how much credit.



The Fair Credit Reporting Act

The Fair Credit Reporting Act was created as a means to provide fairness, accuracy, and privacy when it comes to the files that are collected by consumer reporting agencies, such as the aforementioned credit bureaus. Individuals are guaranteed a number of rights under this act. There are many rights under the FCRA, and it is a good idea to understand at least the basics of those rights.

These rights include:

✔ *The right to be told what information has been used against you* – If anyone uses information that was found in a credit report and denies an application for credit, employment, or insurance, they are required to tell you and they must provide you with the name, address, and phone number of the agency that provided them with the information.

✔ *The right to know what is in your file* – You have the right to request information that has been gathered about you and kept in files at the bureaus. You can get a free credit report once per year from each of the credit bureaus. If you need to check your report more than once per year, you will often need to pay for the file disclosure. However, there are certain cases where you will still be entitled to another free disclosure. They include:

- A fraud alert has been added to your file because of identity theft
- The file has inaccurate information due to fraud
- Someone took an action against you because of information in the credit report
- You are unemployed and will be applying for employment within 60 days
- You are on public assistance

- *You have the right to ask for your credit score* – You can request your credit score, but you will have to pay for it. However, if you are buying a home, the credit score information will typically be free through the mortgage lender.

- *You can dispute incorrect information* – If there is information in your file that is inaccurate or that is not complete or verifiable, you should report it to the agency, so they can investigate.

- *Inaccurate information must be corrected or deleted by the consumer reporting agency* – In instances when you show the bureau that there was incorrect or unverifiable information in the file, they are required to have it fixed or removed within 30 days. If they investigate and find that it is accurate, though, they are going to continue to report that information.

Outdated negative information – Most of the time, a consumer reporting agency is not going to report outdated negative information. If the information is more than seven years old, or if you have a bankruptcy that is more than 10 years old, you will find that most of the time, the credit bureaus are not going to report it.

Only those with a valid need can access your file – The FCRA states that only those who have a valid need for your information are going to be able to have access to it. This is limited to those such as employers, insurance companies, landlords, and credit companies.

Employers need to have consent – The only way that an employer is going to be able to access your file, whether you are already working for them or they are a potential employer, is if you provide them with written consent. One of the areas where written consent is not typically required is in the trucking industry.

These are some of the most important rights that are contained in the act. Having an understanding of how they work can help you to understand how and why certain companies, such as credit card companies, have denied or approved your application for credit.

When Are the Credit Scores Updated?

When you are looking at your credit score, one of the things to keep in mind is that increases and decreases to the credit score are not made instantly to these bureaus. Instead, the reporting of these scores will typically happen according to billing cycles. This means that the changes are not going to be recognized right away.

Generally, a creditor will report information, such as payment activity, balances, missed payments, and the like every 30 days. However, this can and does vary from one creditor to the next. Therefore, it is going to take some time to see those changes reflected, whether they are positive or negative.

You can rest assured that the creditor is going to make those reports though. So, if you make late payment, it is going to be reported as a late payment. Just because you don't see a hit to your credit score right away does not mean that it is not coming during the next update cycle.

Understanding Hard and Soft Inquiries

As you start to learn more about factors that go into your credit score, you are going to start hearing the term "hard inquiry" and "soft inquiry". Let's get a better understanding them, and how they can affect your score.

Hard Inquiries

A hard inquiry, sometimes called a hard pull, will happen when some type of financial institution checks your credit when they are making a decision on whether to provide you with a loan or credit. It could be a bank or a credit card issuer that requests the hard inquiry. They are very common if you are applying for a loan, a credit card, and for a mortgage. If you need to authorize the access to your credit score, you can generally assume that it is going to be a hard inquiry.

With these types of inquiries, there is a chance that it could lower your credit score by several points. However, it may not have any effect on your score. These types of drops to the credit score tend not to last for very long though, and it you are only going to be applying for a single card or loan, then you should not worry about it.

However, you should not attempt to apply for several cards or loans at the same time, or even within a few months of one another. If you do this, it is going to be seen by lenders and creditors, and they are more likely to view you as a credit risk. They might see this as an act of someone who is looking to expend a lot of credit in a short period, and they are not likely to want to risk working with you.

Instead, you should wait several months between loan applications and credit card applications. In addition, think about whether you truly need to have another card before you try to open up an account. Having a wallet filled with cards can be more of a hassle than it is worth, and there is the potential for more financial trouble.

Soft Inquiries

Soft inquiries, often called soft pulls, are the types of inquiries that occur when someone does a background check and checks into your credit as a part of that. This could occur when an employer runs a background check before they decide to hire you, or when a credit card company wants to check your credit without notifying you as a means to then let you know about offers that you might like.

However, these types of inquiries do not have any affect on your credit score. In some instances, they might be reported on your credit report, but they are not going to have a negative effect on your score. When you check your own credit score, it is considered to be a soft inquiry, so you will not have to worry that it is going to cause any issues with your score.

Why Being Aware of Credit Factors Is So Important

Far too many people are entirely unaware of what makes up their credit score and how much emphasis is placed on the different credit factors. This lack of knowledge is often what causes so many people to have issues with their credit. Even not understanding the detriment that too many hard inquiries can have could damage your ability to get credit, but many people simply do not realize it. Taking the time to go through this book and to understand the different factors, and how to improve those factors in your everyday life, can give you an advantage in our modern world that revolves around credit.

Having a good credit score is essential for a host of reasons. The following are some of the biggest reasons that having good credit, and learning how to maintain it, is so essential today.

Credit score affects where you live – Whether you are looking for an apartment to rent or a house to buy, credit is going to play a factor. Landlords are going to check up on your credit, and so will mortgage lenders. Without good credit, you might not get a loan, and you might not be able to find an apartment. The credit score is also going to determine your mortgage interest rate. If you are lucky enough to get approved and have a bad score, it means that you could end up having a higher mortgage rate.

Credit score affects what you pay – If you have problematic credit, but you are still able to get a loan or credit card, it means that you have higher interest rates in most cases. This means you are going to be spending more on your purchases than someone who has a better score.

Credit score affects what you drive – If you are buying a new vehicle, or even a used vehicle where you need to take out a loan, you can be sure that your credit score is going to play a role. It can be more difficult to get a loan, and again, your rates are going to be higher with a poor score.

Credit score affects your search for a job – As mentioned, employers are often going to check a person's credit score when they do their background check. There are certain types of jobs where having a bad score may preclude you from becoming an employee.

Credit score can affect your ability to start a business – Starting a business tends to take quite a bit of money. You need capital to get the business off the ground, and if you have bad credit, you are going to have trouble getting a small business loan.

Credit score affects your monthly bills and your daily life – Because you may have to pay higher interest rates on the loans or cards that you have, it means that you are going to have less overall spending power. You are spending too much on the high interest rates! Improving your score and learning to live without spending too much on credit is going to be the key to helping keep your monthly bills under control.

As you can see, your credit score is going to affect just about every aspect of your life. It makes sense to do as much as you can to protect it, or to repair it if it is already in trouble.

Gain the Knowledge You Need

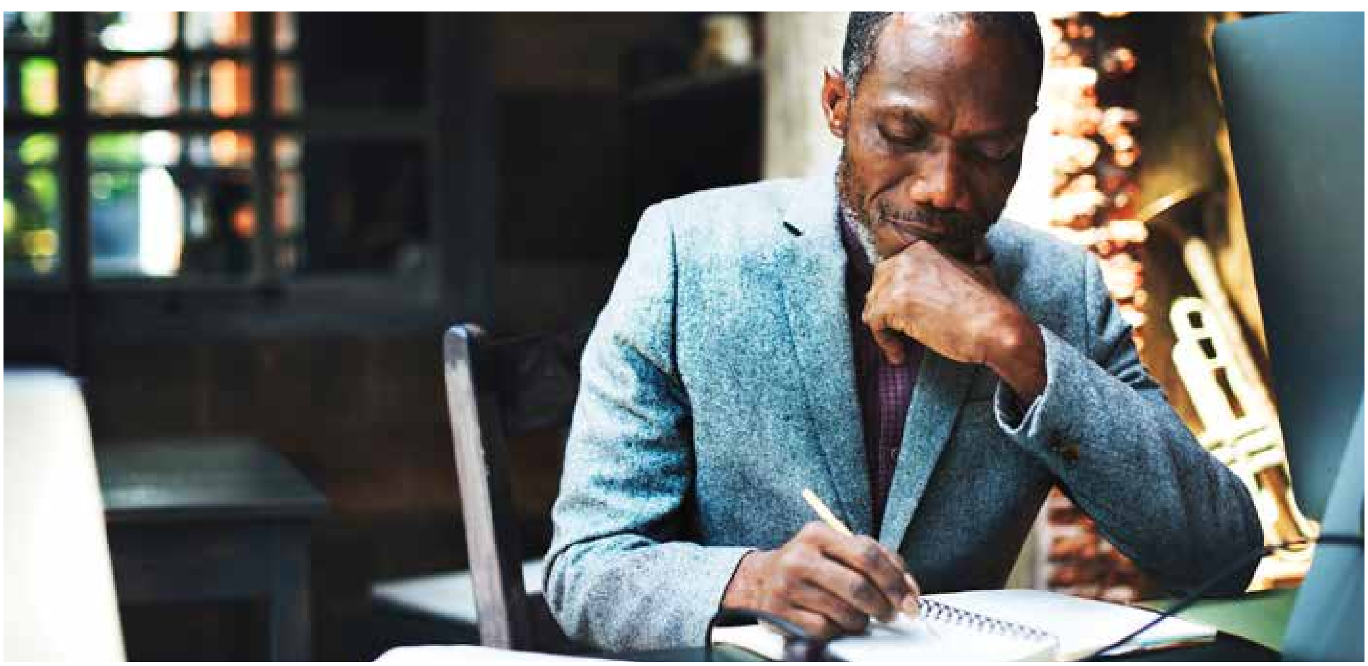
In the following chapters, we are going to be delving into the **five credit factors** that are going to contribute to your score, as well as just how much each of these factors contributes. Once you understand them, it truly does start to become easier to get your credit under control.

Chapter 1:
Utilization: Understanding Credit Use (30%)

You will notice the 30% in the parenthesis right after the chapter title. This lets you know how much the utilization of your credit is going to affect your credit score. You need to understand how to use your credit wisely if you are going to make the best use of it and have full control over your credit score.

Your credit utilization is the percentage of the available credit that has been borrowed. For example, let's say that you have $10,000 in available credit. 30% of that would be $3,000. If you had only $1,000 in credit, 30% of that max would be $300. The goal is to always make sure that you have never borrowed more than 30% of your available credit across all of your cards.

Lenders may measure individually by card, or across all cards, when they are making a decision on whether to provide you with credit or a loan.



The Myth

However, there is a pervasive myth that too many people unfortunately believe. The myth says that "if there is credit available, I can and should use all of it." This is certainly not true.

There are a few reasons why a person might believe this myth. Some people want to believe this, especially those who have trouble controlling their spending. They see the money as theirs. They have a compulsion to spend that money on things that they could not afford otherwise, and this ends up getting them into trouble. The only thing they have to show for it is more debt and items that they probably do not even need. While this often affects younger people, it can be a problem for people at any age.

It can be hard for those people who spend compulsively to see the error of their ways, even after they have been through the cycle of borrowing too much and getting into trouble in the past. Once they start to take care of their credit issues and get another card, they are right back to maxing them out. It's a terrible cycle.

In other cases, people might mistakenly believe that if they borrow and use a lot, and then pay it back, it will appear that they are a good credit risk and could get a higher limit. They believe that it shows they will pay back their debt. FICO does not see things that way at all.

They see someone who maxes out credit cards, or who gets close to maxing out their cards, as being a risk. They believe that those people are not handling their debt responsibly. If you have done this in the past, it can often be more difficult to get credit from other companies, even when you have paid off your other debt. The lenders just don't like to take on too much risk.

The reality of this myth is that when you are utilizing more than 30% of your available credit, you can end up doing harm to your credit score.

Think about it for a moment.

When you are using this much credit, you are going to have large credit card bills that you have to pay each month, and missing a payment is going to cause some serious harm to your score, as you will see later in the book.

Having high balances will also make it appear that you are overextended, even if you might not feel you are. This is going to lower your score and just having such high credit utilization makes most lenders and creditors think twice about lending to you. They do not want you falling behind on your payments.

Calculating Your Credit Utilization

Calculating your credit utilization is simple. You will divide your credit card balance by the credit limit and then multiply it by 100. Make sure that you are using your account statement for this rather than a credit report. The account statement will give you an accurate and real time information, whereas the credit report is based on billing cycles and might not have the most recent information.

When you do the calculation, it will let you know what percentage of your credit you are utilizing. Remember the 30% rule – you want to use less than 30% of your available credit.

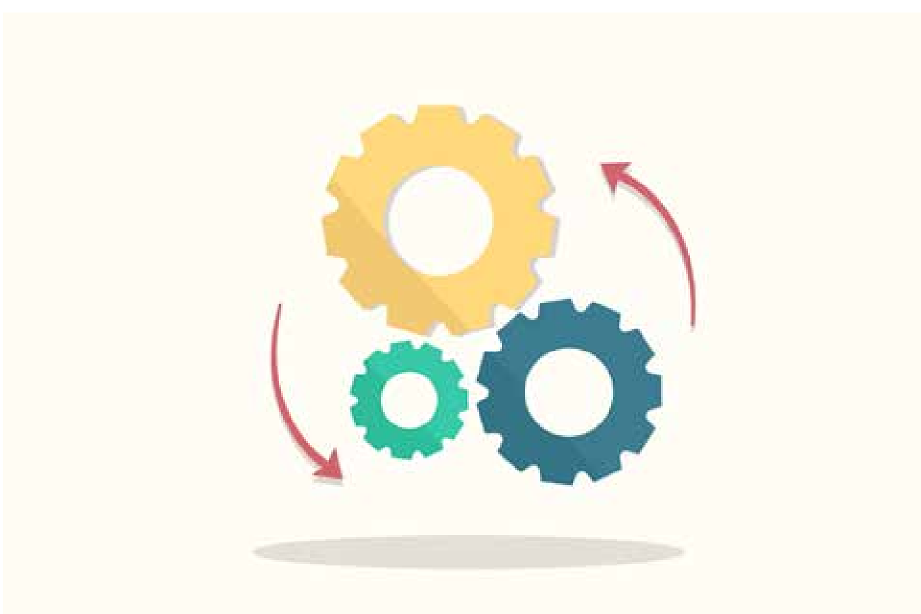
However, don't let that rule make you feel as if you need to keep it at 30%, as you will find that lower is going to be better.

What's the Solution?

Because this accounts for a whopping 30% of your credit score, you need to take it seriously. However, this does not mean that you can borrow and use more than 30% and just pay it all off at the end of the month. If the balance is high when the creditors report your utilization – no matter what you do at the end of the month – it is going to show your utilization as being high.

You need to work to make sure that your balance is always 30% of your credit limit or less. This way, your report will show that you have a low balance.

Below, you will find some real and workable solutions that can help you to ensure you are keeping track of your credit utilization, and ways that you can make sure it is as low as possible.



Track the Expenditures

This could help some people who may have issues keeping under the 30% limit, but it should not be used by anyone who has trouble with their spending habits. If you are responsible with your credit, but you find that you are getting close to the 30% mark each month, you could talk with the credit card company about getting an increase to the card's limit. This way, you will have more of a cushion, and you will stay well under the 30% mark.

Ultimately, this could help to improve your credit score. Just keep in mind that if the credit card company does a hard inquiry, it is going to cause the score to dip by a few points for a little while. As long as you are making your payments on time, it should not have any trouble bouncing right back.

Mid-Cycle Payments

One of the other tips that you might want to start using is to pay your credit card bill twice per month. If you pay half your bill now and half when it is actually due, you will find that it becomes easier to ensure that you are staying below 30% of your overall credit. However, this means that you still need to be aware of how much you are spending, and that you don't start spending more just because you see that you are under 30% of your limit!

Use Your Credit Cards Less

Not only will you want to keep track of your expenditures on the credit cards, which we mentioned earlier, you will want to rethink how you are spending when you use credit. Many people today use their credit cards for just about every purchase that they make, not realizing how much more they end up spending on those purchases because of the interest.

Instead, you want to go through your monthly expenditures and make sure that you are using the cash in the bank to pay for the majority of them. Ideally, you are only going to be using credit for emergencies and for the rare expenditure that you don't have cash for right now – but that you will be able to pay off quickly.

That's not to say that you can't buy things that you want on credit – you can. However, you have to be smart about it. Let's say that there is a television that you want for the living room, and it is currently on sale for $1,000. You only have $500 in extra cash that you can spend on it, but you don't want to miss the sale. You could put it on credit with your credit card, and then immediately pay the $500 to your credit card company (as with the mid-cycle payment mentioned above). As long as you get the money to them before they report to the credit bureau, it would only show $500 used in credit on your updated balance, since the other was already paid.

Do not use the credit card for all of the payments that you would typically have used cash for. Continue to use cash, and if you do not have the cash, then you might want to rethink those expenditures.

It Takes Some Effort and Discipline, but You Can Do It

If you want to keep your credit utilization low, it is not always going to be easy. It is going to take work and discipline on your part to keep track of everything that you need to know about your balance and your accounts. You need to be willing to keep up with tracking the expenses until it becomes second nature to you. Keep your receipts and spend five minutes a day logging them. Once you get into the habit, it won't take too long, and you will be happy that you have the information.

You also need to make sure that your discipline extends to how much you are spending. So many people today want the instant fix. They see something, they want it, and they whip out the credit card. Before they know it, they are deep in debt and well beyond 30% of their credit limit.

It can be difficult to dig yourself out of that type of hole, so don't put yourself in the situation in the first place.

The moral of this story is simple – never spend more than you can repay.

This is the **number one rule** to keep in mind if you want to keep a good credit score, yet it is something that many people willingly ignore. Of course, your credit utilization is not the only factor that makes up your credit score, and the next item in our list ties in with utilization very closely.

Chapter 2:
Payment History and On-Time Payments (35%)

Your credit utilization accounts for 30% of your credit score, but your payment history and on-time payments account for even more. They are 35% of your overall credit score! This is **the most important factor** when it comes to determining your score. FICO claims that it is important to look at a person's long-term behavior in the past as a means to predict their potential behavior in the long-term future. If someone has had problems paying their credit card debt and loans on time in the past, then the lenders believe that they are going to continue down this path.

While it might not initially seem fair, and you might argue that you can change for the better when it comes to making on-time payments, they have data that shows this is not always the case. Those who rack up debt and don't pay tend to keep doing the same thing time and again. This means it can be difficult for those who are actually trying to change to make improvements to their score and show themselves as being worth of credit.

Someone who has been a late payer or a nonpayer in the past is likely to fall into those same habits in the future, and they need to prove themselves. In terms of the credit score, FICO is going to be looking at different types of revolving loans, including credit cards, as well as installment loans. A mortgage would be an example of an installment loan.

The Myth

There is a myth that many people mistakenly believe when it comes to paying off their debt. They believe that "if I eventually pay back the creditors, my credit score will be ok."
That's not the way it works.

When you have late payments, they are going to quickly tarnish and tear apart your credit score. Even if you eventually pay that lender back everything they are owed, the damage is done. You are going to need to take steps to improve your credit, which can take a long time. We will be covering improving your credit at the end of the book. It's possible, but it can take longer than many people realize.

Your scores are going to consider different factors, including the frequency of your payments, the recency of the payments, and the missed payments and their severity. When you miss payments and when you make late payments, whether it is a loan payment or a credit card payment (they are weighed equally), it will hurt your credit immensely.

Because this is 35% of your credit score, you cannot take your payments lightly. Even if you have just a few missed payments, and you eventually paid them back, what type of message do you think this is going to send to other lenders? Even if your report shows that you paid the other lender back, why would another company want to do business with you? Why would they risk their own money to give you credit?

If they do decide to supply you with a loan or a credit card, it is often going to have a higher interest rate attached to it, and that means that your payments are going to be more.

Fortunately, there is a simple solution for you to make sure that this is never a problem. Make sure that you pay your creditors on time each and every month. This way, you never have to worry. When you combine this with keeping your credit usage low, you account for 65% of the factors in your credit score. It can be the "easy" way to keeping a good credit score.

Of course, we all live in the real world, and we know that sometimes, it can be difficult to make those payments on time. However, there are some tips that you can use that may help to make things somewhat easier on you.

Tips for Paying the Creditors

First, and most importantly, you need to make this a priority in your life. There are many people who wait until the last minute to make their credit card payments, or they skip a month if they feel that they want to have a little extra money in their pocket. As you have seen, this is going to be 35% of your credit score. Missing a month or two because you want to have some money to go out to dinner with friends is an irresponsible thing to do – there's no way around it. You have to focus on making payments to your creditors.

Let's look at five practical tips that can help.

Develop and Know Your Budget

How much money are you bringing in each month? How much money do you need to spend each month? At the end of the last chapter, we mentioned that you should never spend more money than you can repay. In some cases, this might mean that you need to rearrange your current budget for a few months so you can start paying down your debt and making payments on time.

Set up a budget that automatically sets aside the money that you need for your payment each month. Consider the credit card or loan payment money as if you didn't have it in the first place, and then balance the rest of your budget around the money that you have left. After making sure that you have a roof over your head, and food in your stomach, you need to make sure that you are paying the creditors on time. There are no excuses not to do this.

Find ways that you can reduce your other expenditures. For example, stop getting coffee at Starbucks and stop going to the movies each week. Later in the book, we will be discussing other ways that you can improve your credit and other ways that you can reduce expenditures and spend more on your credit card payments. It might mean going without some of the things that you want for a while, but if you can keep your credit score in check it is worth it.

Track Spending

In the first chapter, we mentioned that you should track your spending, so you can keep your credit balance below 30% of your overall limit. If you are already in this habit, then you are in luck. If not, it's time to start tracking now. You might be spending more than you think on items that you don't really need, and that money could be better spent ensuring that you always have your payment for creditors and that it is always on time, as well.

You could use your receipts, you can check your accounts, and you can use an app on your phone or computer to help you track your expenses, and to help you come up with your budget.

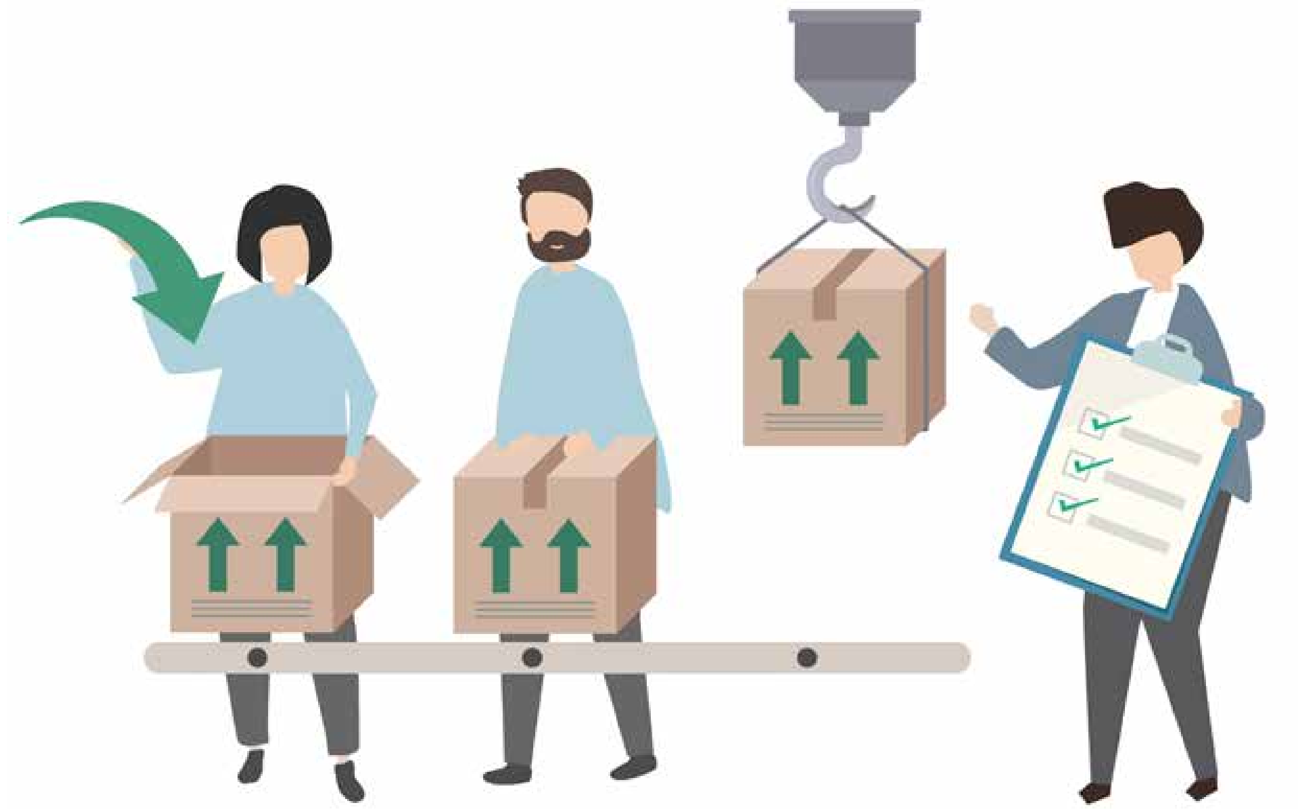
Keep Track of Deadlines and Pay Online When Possible

One of the reasons that some people don't pay their bills on time isn't because they don't have the money or because they don't want to make the payments. It's simply because time tends to get away from them, and they might not realize that the payment due date is coming up. Therefore, you will want to make sure that you are marking your calendar to ensure that you always know when the payments are going to come due.

While you can use a paper calendar on your wall to help with this, you might also want to consider using an online calendar, and a calendar on your phone, which can provide you with alerts. Be sure that you set the alerts so you know when you should send the payment, not when it's due. This will ensure that you get the payment into the mail on time.

You might also want to consider paying your bills online if you haven't already switched over to that method. This tends to be easier, and you can make payments that are on the day that it is due in the even that you are waiting for some money to come into your account.

It is also a good idea to have a checklist that you go through with all of your bills on it, along with their due dates. Get into the habit of checking this list regularly and marking off when you have made your payments. Once it has become a habit, you will find that it is far less likely that you are going to mistakenly miss a payment in the future.



Consider Automatic Payments

If you have a high amount of debt that you are trying to pay off, you might want to consider making larger payments, at least for a while. This can help to reduce the amount that you owe on the credit card faster, which can help with the interest. This is something that you should always attempt to do if possible. If you come into a large sum of money, you might want to put a large chunk of it toward the payment if you have a high balance. Paying down the debt could help to reduce the amount of your payments later, and it can make it easier to ensure that you have the money to pay them.

Change the Due Date

One of the other tips that you might want to use is requesting a change of due date for your payment. In some cases, you might have a credit card payment date that coincides with your mortgage, a car payment, or other payments. Instead, you might want to move it to another time of the month that is going to be more convenient for you. You will find that many lenders are going to be willing to do this, simply because they want to make sure they are getting the money they are owed.

Chapter 3:
Your Credit History (15%)

There are some that mistakenly think that their credit history is the same as their on-time payments, and that is not truly the case. The credit history refers to a number of things that make up your overall history. It includes the number of credit cards that you have, the number of loans that you have, and whether you pay your bills on time. It will show how long each of your accounts has been open, the amounts that you owe, your credit usage, and the number of recent credit inquiries.

As the name suggests, it is the entire history of your credit, and yes, it does include elements of the other factors that are used to determine your credit score. Because we are discussing your on-time payments and your usage in other chapters, we will focus on elements such as existing lines of credit and the length of your credit history – and why it matters.

The Myth

Again, there are some myths that tend to surround credit history, just as with other elements of credit. One of the myths that is often repeated is, “if I close an active credit account, it will help me to increase my score.”

That’s not the case because your score is going to be based in part – 15% of it – on how long you have had established lines of credit. If you were to open up two new accounts this year, they would not show much in the realm of an established credit history. They are too new. Established lines of credit are those that are in good standing and have been around for four or more years.

So, closing an account that you have had for four or five years is not going to do anything to raise your credit score. Even if you have had issues with payments with that lender, it is not going to help to close the account. Instead, you want to work hard to make sure that you are paying that creditor on time to improve your standing with them.

Having older lines of credit that are in good standing are what will help to improve your score.

What Constitutes Good Established Credit Lines?

Because when your credit score is calculated, the length of your credit history plays an important part, it means that even someone who has just started up their first credit card account is not going to have perfect credit. This is because the history and length of your accounts being open is a factor. Having a longer credit history is going to provide more information, which can give creditors a much better indication of your behavior with credit in the long-term.

Remember, creditors want to know what it is going to be like working with you over the long haul, and your credit history is what gives them an indication of that.

A good credit line is one that has been established and kept open and in good standing for several years. Accounts that are over four or five years old are going to fall into this category. FICO is going to look at the age of your oldest account, as well as the age of your newest account, and take an average age of all of your accounts. The credit history is also going to include how long it has been since you have used certain accounts.

According to FICO, even after you have closed an account, it is still going to keep aging on your credit report until it finally comes off. They can stay on your account for up to 10 years. One of the most important elements when you do close an account is going to be the revolving debt to credit limit ratio.

Keep in mind that if you have older accounts that you have closed, when they drop off the credit report, it has the potential to change the length of your credit history. This is because when the old one vanishes, it is essentially nonexistent.

To help develop a strong credit history, you will want to keep in mind the following basic tips.

Keep Existing Lines of Credit Open

Instead of closing off old accounts, it tends to be a much better idea to keep them open. Having those older accounts on your credit report really will be a benefit to your overall score, and it is one of the easiest things that you can do to help improve your score. All you need to do is keep those old accounts open and keep them in good standing – which we will talk about on in the next section. If you want to have the best credit score possible, keep those older accounts open.

If you choose to close an account, there is a chance that it could have a detrimental effect on your credit score. If the card has a high credit limit, and you have high balances on other cards or loans, closing the card with the high limit could actually hurt your credit score. This is because it will appear as though you are utilizing a higher percentage of the credit that you have available.

Old credit tends to be better credit, at least in the eyes of FICO. It shows that you have been able to keep an account for longer. The baseline for an established account would be four or more years.
Of course, you do need to make sure that you are maintaining those accounts properly and paying your bills on time.

Keep the Accounts in Good Standing

However, you not only want to keep the credit lines open, you also have to make sure that you are keeping those accounts paid on time as discussed in the last chapter. If your accounts are not in good standing, meaning that you have late payments or that you have defaulted on your accounts, then your credit is going to suffer.

Take the advice about paying your credit card bills on time to keep your account in good standing from the previous chapter and make sure that you apply them.

In addition to making sure that you are taking care of your credit card and loan payments on time each month, FICO also considers other types of accounts in their traditional scoring model. This includes rent and utility bill payments, which they use as alternative data and can help to score customers who have a shorter or thin credit history. It is important to pay all of your bills on time.

Is There Ever a Good Time to Close a Credit Card?

You might be wondering if you should always keep your old credit card accounts open, or if there is ever a time when you should close them. While the rule of thumb is that you should keep your old accounts open because they can have a positive impact on your credit score – and closing them could drop your score – that's not to say that you never will want to close out an old account.

There could be several reasons that you might want to do this, which are valid. However, you should always look at the pros and cons of canceling a card. Below are some of the reasons that you might want to cancel a card.

The Card Company Changes Terms and Won't Negotiate

If you have had a card for a number of years, there may come times when the credit card company changes their terms. Most of the time, any changes to the original terms are going to be minor, and they are not going to cause any issues for you.

However, that's not always the case. Therefore, it is always important to read over those terms to understand what they are going to mean for you the consumer.

If you find the terms are unagreeable to you, and the company is not willing to negotiate, then you might want to consider cancelling the card. Some examples of terms that could change include the company lowering your credit limit or increasing your interest rates. Neither of these are good news for you! You never want to keep a card if it has the potential to cause you more financial harm than good.

When You Have a Spending Problem

Taking care of your finances is about more than just having a good credit score. It should be about overall financial health. If you have a credit card – even an older account – that you keep maxing out and having trouble paying off, it might be time to close the account and get your spending under control.

When you are charging a lot on your cards, it doesn't matter how many cards you have. It is going to become a problem. Good credit is still going to cause problems when you keep overspending. You need to be able to take full control of your finances, even if it might mean a hit on your credit report right now.

Once you have a better handle on your spending, you can then open a new account and rebuild your credit. It truly is better to do this than to keep spinning around in the cycle of spending too much on credit and then scrambling to get the bills paid on time each month.

When You Are Paying an Annual Fee for a Card You Never Use

If you have had a card for many years, but you never actually use it, and you are paying an annual fee for the card, you are likely wasting money. You should make it a point to consider the age of the account, the credit limit that you have, and whether it makes sense to keep the account open.

It will typically depend on the amount of the annual fee and what other benefits you might have from the card. If it is an account with a high credit limit, then you might simply want to keep it open and use it occasionally if the fees and interest rates aren't too high. Ideally, you will be able to have credit cards that do not have any annual fees associated with them.

Chapter 4:
Credit Mix: Diversity Is Key (10%)

How many lines of credit should you have open at a time? Having a good credit mix is actually going to account for 10% of your overall credit score. Therefore, even though you might have heard others tell you that you should only have one line of credit, this advice is simply not correct.

The Myth

Many people, particularly those who have had trouble with credit in the past, believe fervently that "responsible credit use means having only one line of credit and paying it on time." At first blush, this myth sounds rather convincing. After all, if you only have a single line of credit, it tends to mean that you will have less than you need to pay off each month. However, the reality of the matter is something different entirely. Ideally, you are going to want to have more than one credit line, and you will want them to be as varied as possible. We will discuss this more later in the chapter.

One of the reasons this myth tends to be believed is because of the last part of the sentence. You do need to make sure that you are paying off your debt on time each month. It is the most important part of being responsible with your credit.

However, that doesn't mean you should just have one line of credit open.

Types of Credit You Might Want to Pursue

Because credit diversity is going to account for 10% of your credit score, you want to make sure that you have varied lines of credit. While having a couple of credit cards might be how most people start, it is important to remember that diversity in the types of credit matters. Some of the other types that you are going to want to consider include:

- Auto loans
- Student loans
- Home loans
- Retail credit cards

Having these other types of credit active can be quite helpful when it comes to showing diversity of credit. Even though it might only account for 10% of your overall credit score, if you want to have the best score possible, it is a good idea to take advantage of every option that you can find to do so. This tends to be a relatively easy way to do it, as long as you are paying off all of your bills on time.

Are Installment Loans Truly Beneficial?

Installment loans tend to be a great choice for those who want to diversify their credit, but you shouldn't get a loan solely to help boost your credit score. Use them when you need them, and they will help. Through their nature, they are going to help to build up your credit history and payment history. They will help to build your credit score, but they are just one of many factors. You also need to incorporate all of the other elements discussed in the book.

Don't Rush and Overextend Yourself

Knowing that a diverse mix of credit is great, but that does not mean that you should run out and open up as many credit cards as you can and apply for as many loans as possible. That would be irresponsible. Instead, you want to start out slowly when you are adding to your credit.

If you have one or two credit cards open right now, that is going to be a very good start. As long as you are sure that you have the financial capacity to handle more credit, and you are able to use it wisely, you can open up another credit line. Instead of getting another credit card right now, though, you might want to consider getting a small loan as a way to mix up the type of credit you have.

An installment loan, such as an auto loan, could be a great option if you are looking to get a new car anyway. If you need a personal loan, or you want to go back to school and need school loans, you could add those to your list of credit lines. As long as you are paying the loans back on time, and you are keeping up with the credit card payments, it can provide you with the added diversity that you need.

Don't Make the Mistake of Doing Too Much Too Quickly

Now, there are probably some out there that believe this could be a fast way to improving their credit score. They may think that opening up three more cards, getting a home loan, and trying for an auto loan all within the same year are going to help them out.

That is certainly not going to be the case.
Remember, when you have hard pulls on your credit report, which would be used for these types of credit, they are going to knock a couple of points off your credit score each time. While they are going to bounce back, it does take some time. When other lenders see that you have had multiple hard pulls and are trying to take out more loans or get more credit cards, it can make them wary, as well. They worry that you are trying to get a lot of credit in a short period, and they don't always trust that.

Instead of trying to do everything at once, take out only the cards or loans that you feel are truly necessary, and make sure that you are always paying them on time. This has been said a number of times already in the book, and it will be said again because it bears repeating. It has a massive effect on your score, and it tends to be where most people are going to fall short.

What you want to do is go slow. If you have a credit card or two, take out a small loan that you could use for something that you need or want. Even for a vacation. Then, make sure that you pay that loan back on time. In fact, it might be a good idea to have some money saved up and set aside that you can use to ensure that you have the money to pay back the loan each month.

This might seem counterintuitive, but if you are trying to build your credit score, it makes sense, as it can provide you with that added safety net.

Opening up new credit lines, which is discussed further in the following chapter is going to have that immediate negative impact, but it could improve your credit in the long run when you are using it properly. Just make sure that you don't open too many at once – that's where the trouble starts.

Are You Currently Overextended?

Before you start to open up more accounts and lines of credit, you need to make sure that you are not going to be financially overextended. You need to make sure that you are managing your debt properly, and part of that means knowing when you are overextended or in danger of getting into a financial problem because of your credit.

The following are some of the indicators that you could be on the way to being overextended – or that you are already there. In those cases, you would not want to open up any new lines of credit until you take care of your current financial predicament. After all, responsibility is essential if you want to have and keep a good credit score.

Spending More on Credit Than You Are Paying Off

Many people carry their credit card debt from one month to another without really reducing the amount that they owe. They might pay the minimum amount, or even a little more than the minimum, but they keep spending on credit each month. They end up spending more on credit each month than they are paying back, which means that they are slowly digging themselves deeper into debt.

For example, if you have $1,500 in credit card debt on one card that has a $5,000 limit, and you are continuing to spend $200 a month on the card, while only paying $150 on your bill each month, it is going to catch up to you eventually. You will get to a point where you don't have any credit left.

Not Saving for Retirement

Let's say that you are able to pay your credit card bills and your other bills each month, but you don't have much money left over. Even though you might have a job that pays into Social Security and perhaps a 401k, you need to make sure that you have plenty of money that you can put into your retirement plan. This will ensure that you have a safety net once you get older, and that is just as important – perhaps even more important – than getting more credit cards right now.

If you are able to contribute to your retirement fund, and you are able to pay all of your bills on time, then you are probably not overextended, and you can think about opening up new lines of credit. If any of the above experiences sound familiar though, then it might be time to rethink opening up a new line of credit until you have things under control with your finances.

Finding the Right Lines of Credit

As long as you are careful, and as long as it is not going to put you into a financial hole, you can open up new lines of credit. In the following chapter, you will learn how to do this properly, so that it can have the best impact on your credit score.

Chapter 5:
New Lines of Credit (10%)

So, should you open up new lines of credit? Given the fact that the last chapter talked about not overextending yourself, and some of the dangers that could occur when you try to add new lines of credit as a means to diversify your credit, you might be wary. That's actually a good thing. You shouldn't just open up as many lines of credit as you can. You need to do it wisely, and it can be done. Do not let the myths dissuade you. After all, having additional lines of credit added to your credit report will account for 10% of your score.

The Myth

The common myth says, "opening a new line of credit will hurt my score." Why is this myth so prevalent? If you have been paying attention to other parts of the book, you know it is because this myth has elements of truth to it. When you open up a credit line and have a hard inquiry on your account, it is going to ding your credit score and knock it down by a few points.

However, this should not be something that keeps you from trying to open up new lines of credit when you need them or when you are trying to get a little boost to your credit. The long-term benefits of having a new line of credit, which is nurtured and used properly, is likely to outweigh the initial drop in score.

The reality is that even though they might have a short-term negative effect on your score, it tends to be well worth it in the long run.
So, how should you go about opening up new lines of credit? The following tips will help to ensure that you are finding the best options for credit, whether you are looking for another credit card or an installment loan.

Get Only What You Need

As we mentioned earlier in the book, you don't want to get lines of credit that are going to end up causing you more trouble than good. Only choose lines of credit that you are going to be able to use responsibly and that you feel are necessary at the time. This could include a loan for a car, for example. It's a great example of an additional line of credit that can help to nurture your credit score when you pay it properly, and it provides you with something that you actually need – a vehicle.

One at a Time

Because when you have a hard inquiry on your credit report, it will cause a drop in the score by several points, you don't want to attempt to apply for more than one loan or credit card at a time. In fact, you should probably only have hard inquiries on your account a couple times of year at most. Any more than this and it is going to cause too much damage to your score in too short of a time. It is going to make some who might have been willing to lend to you warier to do so.

Look for Smart Options When Opening New Lines of Credit

One of the mistakes that many people make when they start to diversify their credit is not being choosy about the credit that they are getting. They are willing to take just about any new credit card and they will agree to nearly any loan thinking that it is going to help them.

You need to be very careful when you are choosing your lines of credit. Not all credit cards are made equal, and the same is true of loans.

The interest rates are going to vary from one to the other. Some cards might have annual fees, which you will want to avoid whenever you can.

Always take the time to read through all of the terms of the loan or the credit card agreement. Understand what it is that you are signing up for and ask questions if you have them. Make sure that you check the fine print to make sure that you are getting credit that is actually going to help you rather than put you further into debt. Always understand anything that you sign.

Look at the Reputation of the Lender

Just as you would look up reviews of a restaurant before you went to dinner, or a vehicle before you bought it, you need to learn more about what you are getting. Take the time to learn more about the lender or creditor that you are considering. See what others who have had credit cards or loans from them have to say. Have they had a lot of problems with them? Did the experience go well? Having a little bit of insight into the lender can be helpful in determining whether you want to do business with them.

Understand the Difference Between Revolving and Nonrevolving Lines of Credit

As you start to explore the different options with opening lines of credit, two of the terms that you are going to hear are revolving and nonrevolving credit lines. You will want to have an understanding of what these mean and what type of credit would fall into each category.

A **revolving credit** line would be like a credit card. It is a type of credit that you use to pay for goods and services up to the maximum amount for which you have been approved. When you pay your bills on time, it will improve your credit score, and the creditor may increase your spending limit. They are considered to be revolving because you can continue to use them indefinitely, as long as you are making your payments to the creditor on time each month.

A **nonrevolving credit** line would be a loan, such as an auto loan or a personal loan. With these types of loans, you will have access to a certain amount of funds that you borrow all at once. They are not going to reset after each billing period. It is a loan that you have to pay off a bit at a time until you have paid it back in full. At that time, you could apply for another line of credit from the same lender. You use the loan once, and if you get another loan, it would be considered a new one, which is why it is said to be nonrevolving.

Secured vs. Unsecured Lines of Credit

Other terms that you are going to hear when you look into lines of credit are secured and unsecured. These terms, when they refer to credit, are very different from one another. Let’s look at what each of these means.

The **secured lines** of credit tend to be safer for lenders, and they are not quite as convenient for those who are borrowing. An example of this type of loan would be a Home Equity Line of Credit. As with other loans, you would borrow the money and then pay it back over time. The reason these types of loans are considered to be secured is because there is some type of collateral on the line. For example, with a HELOC, the collateral would be your home. If you do not pay the loan, you would have to forfeit your home.

The **unsecured lines** of credit tend to be a better option for consumers who want to borrow money. With these, there is no collateral. There is only the promise that you are going to pay back the loan. Auto loans and personal loans, along with credit cards, tend to be considered unsecured. It is these types of credit and loans that are typically going to be helping you to improve your credit score, and that you are going to want to use to help you improve your credit score.

Open New Lines of Credit and Be Smart About It

There is nothing wrong with opening up new lines of credit, as long as you are smart about how you do it. Take the advice from this chapter and from throughout the rest of the book to make sure that you are getting the right credit for your needs, and that you are responsible with that credit.

In the conclusion of the book that follows this chapter, we will start to look at how you can increase your credit score through a variety of practical steps.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Conclusion:
Practical Steps to Start Increasing Your Score

You now know what factors are going to contribute to your credit score, and how much of a percentage each of those factors figures into the number. However, we've only touched on things that you can do to improve your credit score. In this last section of the book, we are going to dive deep into some of the practical things that you can start doing to help boost your credit score.

It's Not an Overnight Solution

While the tips in this book are practical and they will really work to help you to improve your credit score, you will find that they take time. There are no magical solutions that will fix your credit instantly. It took time for the score to fall, and it is going to take even more time for you to fix it. However, if you are diligent, you will be able to make improvements. The tips below, some of which have been mentioned earlier in the book, are the perfect way to do it.

Keep Track of Your Credit Score With Soft Pull Tools

If you want to improve your credit score, the first thing that you need to do is be aware of what your credit score is right now. However, you don't want to request a hard pull just to see your credit score. Instead, you want to start using some of the online soft pull tools that can allow you access to your credit score whenever you need it.

There are some affordable options out there that could work quite well for this including Credit Karma.

Keep in mind that you can also get your credit score from the major credit reporting bureaus for free once per year. When you have an idea of what your credit score is currently, it can give you an idea of just how much work you have to do in order to get it back into shape. Below, you will see what is going to constitute a good score and a bad score.

- Excellent Credit – 781 to 850
- Good Credit – 661 – 780
- Fair Credit – 601 – 660
- Poor Credit – 501 – 600
- Bad Credit – below 500

No matter where your credit score might be right now, you will be able to make positive changes to it and start climbing the ladder back toward excellent credit. Knowing your credit score, no matter how bad or embarrassing it might be, is going to give you the fire that you need to start making improvements.

Check Your Credit Report and Dispute Any Errors You Find

Under the Fair Credit Reporting Act, the correction of any mistakes on your credit report are the responsibility of the credit reporting company and the information provider. Because they don't know about the errors on the report, it is up to you to check your credit report at least once per year – or whenever there seems to be something aberrant happening with your credit – and look for problems.

You will want to look over the credit report to make sure that everything is entirely accurate. If you find any information that is incorrect, such as credit cards or loans that are not yours, or incorrect amounts of debt displayed, you will want to tell the credit reporting company. Let them know in writing what information you believe is inaccurate.

You will then mail the letter to the agency (one of the main credit reporting companies), providing them with copies of any documentation that will support your position. In the letter, you will want to identify everything that you are disputing, let them know why you are disputing it, and request that it is fixed or removed from your report. It is important that you remain calm in your letter and that it states only facts, not emotion. You will want to send the same letter and copies of documentation to the information provider.

The claims will then be investigated. It is required that they do this within 30 days, and they can then notify all of the major credit bureaus so the information is fixed across the board. If the investigation does not solve your problem, you can request that they include a statement of dispute in your file and in future reports.

Never Assume

It can be easy to get complacent and just to assume that everything is accurate in your credit report, especially if you haven't noticed any major changes. However, there is always the chance that an error could have slipped through. Instead of simply believing that your credit report is fine and accurate, it really is in your best interest to check it out at least once a year with your free credit report.

If there are errors, dispute them as soon as you find them. Getting incorrect material off of your credit report is a good way for you to improve your credit score. Letting it sit on your report is only going to let it keep hurting you.

Start With a Secured Credit Card

Another good tip that you might want to use if you have truly bad credit right now, and you can't get a regular credit card, is to choose a secured credit card. You put money onto the card, such as $500, and you then use the card like you would a regular credit card, buying and then paying what you owe each month. Other than the fact that you are supplying the initial funding, it works like a regular credit card.

The credit card company will report your payments to the credit reporting agencies, and your credit score is going to start to rise. This can be a great option for those who have rotten credit and who are looking to make a change.

Pay Down Your High Balances as a Priority

If you have high balances, or maxed out balances, you need to make them a priority. It is important that you put in the effort to pay them down as soon as possible. Not only does having a high balance look problematic on your credit report, it could also be costing you more money than you know. Think about the amount of interest that you are continuing to pay each month – even if you have relatively low interest. Over the years, this is really going to add up, and your credit score is not going to improve.

Instead, you need to make sure that you are putting in some real effort into making changes in your life that will allow you to pay down your balances. There are a number of different ways that you can accomplish this. You probably won't like the way they sound, but they are very effective.

Sell Items for Money

If you have a high credit card balance, it might be time that you started to think about some of the items you have around the house that you could sell for some fast cash. Maybe you have an extra vehicle, such as a motorcycle that you don't ride, or you have some power tools that are just gathering dust. Regardless of what they are, they could probably do you more good if you were to sell them and use the money to help pay down your balance.

Change Your Lifestyle

Rethink the way you are spending your money. There are probably plenty of little things that you can do and change about your lifestyle right now that could provide you with additional money that you can use for your credit card debt.

For example, you might want to stop going out for coffee a couple of times a week, and you might want to pack your lunch instead of buying it. This could help many people save well over a hundred dollars a month. Imagine how much faster you would be able to pay down your debit if you did this.

Get a Second Job

In some cases, you might find that the best option is going to be to look for a part time job that can bring in some extra cash for you. It might be driving and delivering food through an online service, or it might be working at a local retail store. Put as much of the extra income as possible into paying down your balance. You will not have to keep your second job forever – only for as long as it takes to pay down your debt.

When you use these tips to get extra money, it can also help to teach you a lesson about credit. You are going to be less likely to allow yourself to wind up in the same situation again.

Don’t Miss Payments

You probably already knew that this tip was going to be on the list. After all, it really is the most important and best way to make sure that you are improving your credit score. When you make your payments, the creditors are going to report those payments to the reporting agencies. Paying your bills on time is a slow and sure way to improving your credit score from what it is right now.

Even if you have to change the way you are living right now so you can have some extra money each month to pay down your debt, it is going to be well worth it. Use some of the tips from directly above to ensure that you do not miss any payments.

See If You Can Raise Your Credit Limit

You can consider getting in touch with the credit card companies about increasing your credit limit. This is going to give you more purchasing power, but that’s not why you want to request one of these raises. Instead, you are looking for an increased limit so you can change your utilization. If you have a greater credit limit, it will appear as though you have a lower percentage of money that you owe on your balance. This essentially lowers your utilization without you needing to pay the debt down immediately.

Open a New Account

As mentioned in the last chapter, one of the ways that you can help to improve your credit score is going to be to open up new accounts, such as a new credit card or a loan. Remember that diversity of credit is important, and you only want to open one at a time, so it doesn't hit your credit score too hard. With this type of tip for improving your credit score, you are looking at the long game. It will cause a dip immediately but could be worth it for improving your score over the long haul.

Benefits of Having a Good Credit Score

Now that we have started to look at some of the best ways that you can start to make real improvements to your credit with some practical tips, it is time to get a closer look at just why you want to have a good credit score. Going through life with bad credit is a problem, and it is going to cause you more problems than you might know. However, when you take the steps to improve your score, you will start to notice a number of benefits.

- **Easier Time Getting Approved for Credit Cards:** When you have a higher credit score, it will be easier for you to get approved for credit cards and personal loans when you need them. If you have been turned down in the past, it can be a welcome feeling to be approved. Of course, having a great credit score is not a guarantee that you are going to get approved, but it is much easier.

- **Get Lower Interest Rates:** One of the biggest benefits, and one that can save you quite a bit of money over the years, is being able to get lower interest rates. When someone has bad credit, the interest is raised as a means of protection for the lenders. With lower interest, you could save tens of thousands of dollars or more over the course of a lifetime.

- **Higher Limits:** You will also find that you can often get your credit limits raised quite a bit when you have better credit. It tends to mean that you can be approved for larger loans, as well.

- **Easier to Get Approved for Home Loans and Apartments:** When you are renting an apartment or looking for a mortgage, your credit score is going to play a major factor. Having good credit means you are going to have to worry a lot less about having a place to live since it will be easier to find approval for rentals and loans.

- **Better Car Insurance Rates:** Even auto insurance companies can hold your bad credit against you and charge you more for your insurance. They claim that those who have bed credit tend to file more claims, so they saddle them with a higher insurance rate. Being able to cut the cost of insurance by a bit could save you a lot over the course of a lifetime.

- **Avoid Security Deposits on Utilities and Cell Phone Contracts:** Were you aware that many cell phone companies and utility companies will check your credit before working with you? If you have bad credit, they are often going to require a security deposit in order to work with you. When you have good credit, you are not going to have to worry about this.

You Can Improve Your Score – Make It a Priority

If you really want to make improvements to your credit score, you need to make it a priority in your life. You have to take the advice and information from this book and start applying it. As we said, improving your credit score and getting to the point where you can get the loans and credit cards that you need takes time. It can take a lot of time and effort. However, it is entirely worth it.

Your journey to a better credit score starts right here and now. Get started and make those changes sooner rather than later.

Resources:

https://www.thebalance.com/understanding-credit-utilization-960451

https://www.creditcards.com/credit-card-news/help/5-parts components-fico-credit-score-6000.php

https://www.myfico.com/credit-education/credit-scores/

https://www.experian.com/blogs/ask-experian/credit-education/report-basics/fair-credit-reporting-act-fcra/

https://www.experian.com/consumer-products/experian-equifax-transunion-credit-report-and-score.html

https://www.creditkarma.com/advice/i/hard-credit-inquiries-and-soft-credit-inquiries?pg=2

https://www.consumer.gov/articles/1009-your-credit-history

https://money.usnews.com/money/personal-finance articles/2015/03/12/5-signs-youre-financially-overextended

https://www.bankrate.com/finance/debt/7-simple-ways-improve-credit-score-1.aspx

https://www.consumer.ftc.gov/articles/0151-disputing-errors-credit-reports