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Credit Suicide

By: Chris Brown

Few things influence the home buying process more than your credit. I like how Clark Howard refers to the three credit repositories as, “the three screw-ups”. There is some validity to that, and hopefully recent legislation will help clean up many of the inaccuracies. Regardless, lenders need a source to determine levels of risk for lending money… and the Fair Isaac Company is where it lies. (Note: Fair was one of their last names… doesn’t necessarily denote fairness.) There are close to 50 different things that influence your credit; some good, some bad. Within those 50, there is some 14,000 variations…talk about a fragile balance! For example, did you know that if you pay off a collection it might actually lower your score! Don’t worry most lenders don’t know it either. Also, beware of credit counseling services that promise all kinds of miracles. The only things that can be legitimately removed from your credit are things that are invalid, erroneous, or outdated. Aside from that, if it is yours… it’s yours. There may be ways to “flower it up” but it isn’t coming off. (Being intellectually honest, you know it shouldn’t either.)

If you are going to be hunting for a home, be sure to curtail the temptation to go out make purchases that may affect you credit. Obviously you wouldn’t want to go buy a car, but other things that may not be quite as obvious may be the purchase of furniture or home improvement items that would need financing. Chances are you may need these things, but wait till after closing.

What is the biggest credit mistake?

You wouldn’t believe how common it is! The biggest credit mistake that most of us make is closing our old paid off credit cards. I know that is seems like the right thing to do when you pay off the balance but 15% of your FICO score is made up of your credit history. If you close a credit card with no current balance that you’ve had for years, you are getting rid of a lot of your credit history.

Another 30% of your FICO score is made up by your Debt to Credit Limit ratio. With this component, you show how well you manage the credit extended to you by using it wisely and judiciously. Let’s say that you had two cards with $2,000 limits and one was maxed out and the other one was just paid off. Well you have $4,000 of credit extended to you and you’re using almost $2,000 of that credit (you don’t want to go over 50%). Now you cancel the paid off card and your new debt to credit limit ratio is 100% ($2.000 out of $2000). Ouch, that hurt your credit score.