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Understanding and Enhancing Your Credit Score

Lending to small businesses is quite different than lending to large ones. Many bankers view large businesses as separate, autonomous entities from their owners, the shareholders. Bankers usually work with the executive management in large businesses such as CEO, COO, CFO, and Controller. These managers usually are not majority shareholders in the large business. Conversely, in small business lending situations, the shareholders and the managers are usually the same people. There is a fine line between the finances of the business and those of the owners. The financial health of the small business often mirrors the spendthrift nature of its owners. As a result, a lending decision for a small business often depends on the creditworthiness of its owners.

Lending institutions use many tools to determine whether or not to lend money to small business owners. One tool used is the personal credit scores of the owners. A credit score is a calculated number that summarizes your ability to manage your credit. The number gets updated as your credit circumstances change. Later in this article, we will examine how you can affect this number as you handle your financial affairs. Every time you request credit or someone makes an inquiry of your credit, this score is recalculated. The three national credit bureaus use their own scoring systems. Experian uses the Experian / Fair Isaac system. TransUnion uses the Empirica system. And Equifax has the Beacon system. However, the most commonly used credit scoring method is the FICO scoring method, founded by Fair Isaac and Company in the 1980s.

What's in a Number?

The FICO credit score can range from 300 to 850. The higher the number, the more attractive the borrower. The FICO scoring method uses information from five areas to determine a score: payment history, amounts owed, length of credit history, number of inquiries, and types of credit used. Payment history accounts for about one-third of the score. This makes sense since borrowers who have paid their bills on time are usually good credit risks (and vice versa). Another one-third of the score is based on the amount of outstanding debt you have. The final one-third of the score is based on information about (i) how long have you established your credit, (ii) the number of inquiries on your credit report, and (iii) the types of credit you currently use.

Damaging your Score

Here are some things that might damage your credit score:

- How many bills have been paid late?
- How many accounts have been sent out for collection?
- Bankruptcy, judgment, and liens
- The more recent the damaging information, the worse your score
- Credit cards at or near their credit limits
- Numerous requests for credit regardless of whether the request gets approved or not

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Accelerate your Number!

Here are some tips on improving your FICO number, increasing your chances of getting that loan you need, and lowering your interest rate and/or points:

- If you've missed payments in the past, get current and stay current
- Pay well in advance of the payment due date
- Limit the number of credit cards you use
- Keep credit card balances at 25% or less of their limits
- Pay off debt rather than moving it to other accounts
- If you're new to managing credit, open only a few accounts

What's a Good Number?

There's much debate on what a good number is. However, most would agree that a score of 700 and above is "low risk," while a score of 600 or less is considered "high risk."

For more information on credit scores, visit:

http://www.myfico.com/CreditEducation

http://money.howstuffworks.com/personal-finance/debt-management/credit-report.htm

www.Equifax.com

www.TransUnion.com

www.Experian.com