FDIC

August 13, 2021

FEDERAL DEPOSIT INSURANCE CORPORATION
consumer **news**

Credit Reports and Credit Scores

What they are and how to positively influence them

A credit report is a record of your current and past debts, including your payment history. It is used by banks, other financial institutions, and businesses to make decisions about your loan, rent, and even employment applications. Understanding the information in your credit report can help you achieve and maintain a good credit history; good credit opens the door to opportunities.

What is in your credit report?

Your credit report states what loans you have, how long you have had them, and the balances. It includes information on what you owe on credit cards and how well you are repaying those debts. The report also contains information about loans you may have defaulted on and any debt collections and judgment activities (a judgment is a court ordered decision on a debt payment). Banks, courts, and other businesses report information to credit reporting agencies. Credit reporting agencies compile the information from these different sources to create your credit report. A good website to order your credit report for free is AnnualCreditReport.com.

What is a credit score?

A credit score is a number based on information available in your credit report. You actually have more than one credit score, because different credit reporting agencies calculate your score differently. Generally, your scores are similar, but typically not identical. Credit scores also change over time as information is reported. For example, when you pay off a loan or get a new loan, that information is reported to credit reporting agencies and your credit score is recalculated. The good news is that you can improve your credit score.

For more on credit scores, visit FDIC Explains Credit Scores.

What factors go into a credit score?

Many criteria go into a credit score including:

- Your bill-paying history, current unpaid debt, and the number and type of loans and accounts you have.
- How long you have had your loan accounts open and how much of your available credit you are using.
- If you have had a debt sent to collection, a foreclosure, or a bankruptcy, and how long ago.
- Whether you recently applied for new or more credit.

Why is a good credit score important?

Good credit scores suggest to banks and other financial institutions that you have handled your finances well. A credit score predicts how likely you are to pay back a loan on time. A scoring model uses information from your credit report to create a credit score. With a good credit score you could be offered better loan terms than someone with a poor credit score, such as a lower interest rate or more time to pay back your loan. A low credit score indicates that there is a higher risk that a person will not repay a loan. Landlords may look at your credit scores for the same reason. They want to know if you are likely to pay your rent on time. Some prospective employers also consider credit scores when hiring. Credit reporting agencies provide guidance on what a good score is. You can check with your lender on their credit score requirements.

Can I influence my credit score and my credit report?

How you manage your loans significantly influences your credit score. To achieve and maintain good credit scores, keep in mind the following:

- Make sure you pay your bills and debts on time. You may want to consider automatic payments for your loans and credit cards using your bank's bill pay service. This will help you pay on time, and on-time payments reflect well on your credit report.
- Create a budget. Track when your payments are due, how much is due, and how much money is coming in each month to help you stay on track. For suggestions on how to create a budget, see the sample available in the FDIC Consumer News February 2019 issue.
- Pay down your debt. Having loan and credit card balances at their limits are expensive and can have a negative impact on your credit score. Use a strategy like paying the lowest balance debt off first, then pay the next lowest debt you owe so you can pay it off faster, and so on. Another common strategy is to pay off the debt with the highest interest rate first so all of your hard earned money is paying down your debt, not just paying interest.
- When you pay off your credit card or loan, you might think you should close them, which is fine if you have a lot of them. On the other hand, keeping a credit card that you have had for a long time will probably help your credit score.
- If you cannot make your loan or credit card payments, call your banker or creditor right away. They may be able to help you with a solution before it becomes a problem that affects your credit score. Everyone has a financial hiccup once in a while. Don't be afraid to reach out when it happens to you. For information on working through financial difficulties, visit FDIC Consumer News July 2020.
- Only borrow money for things you need. Make paying down or paying off your loans and credit cards a priority, before adding new debt, whenever possible.
- Shop for credit only when you need it. Making numerous applications for loans is also reported to credit reporting agencies, and may lower your credit score.
- Monitor your credit report. You can receive a free credit report annually from all three of the major credit reporting agencies: Equifax, TransUnion, and Experian. Learn how to order your free credit report by visiting the Consumer Financial Protection Bureau (CFPB).
- Fix any errors you find on your credit report. To find out how to fix credit card errors, visit FDIC's Consumer News October 2018.

How do I get credit if I don't have a credit history?

You start small and build a credit history by doing one of the following:

- Get a secured credit card. A secured credit card works like a credit card, but usually starts with a low limit, like $400. You deposit money with the bank, typically the same amount as your credit limit. You must pay the minimum payment, and if you fail to do so, the bank will use part of your deposit to make your payment. Be sure to get the card from a bank who will report it to the credit reporting agencies, so you begin to build your credit history.
- You can also start by getting a traditional credit card with a low credit limit and a co-signer. The co-signer will be required to make the payments if you don't, so it is important that you make your payments on time. Also, late payments will result in a low credit score. If you have paid on time for an extended period, not only will your score improve, but your bank may consider increasing your credit limit.
- Whether you get a secured credit card or a traditional credit card, always find out all the terms, including any fees and penalties you could incur. This will help ensure that the credit card you select, and the way you use it, enhances your credit history.

Be sure to ask your bank about credit building tools to successfully build a good credit history and get good credit scores.

Additional Resources

FDIC February 2021 Consumer News: Getting Beyond the Tough Times, https://www.fdic.gov/resources/consumers/consumer-news/2021-02.html

Consumer Financial Protection Bureau (CFPB): What is a credit score? https://www.consumerfinance.gov/ask-cfpb/what-is-a-credit-score-en-315/

CFPB: Where Can I Get My Credit Score? https://www.consumerfinance.gov/ask-cfpb/where-can-i-get-my-credit-score-en-316/

Federal Reserve: Credit Reports and Credit Scores https://www.federalreserve.gov/creditreports/pdf/credit_reports_scores_2.pdf

Federal Trade Commission (FTC): Credit Scores https://www.consumer.ftc.gov/articles/0152-credit-scores

FTC: Understanding Your Credit https://www.consumer.ftc.gov/articles/understanding-your-credit

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