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Credit Score Basics

By Michael Kalscheur, CFP®
Senior Financial Consultant, Castle Wealth Advisors, LLC

Your credit score is one of the most valuable assets that you have for your financial well-being. This may be a surprising statement, but consider the following ways a good credit score can help you and a bad credit score can hurt you:

- **Loans** – It is fairly well known that your credit score determines whether a lender will give you a loan (mortgage, car, credit cards, etc.) and what interest rate they will charge if they do give you the loan. A bad credit score can cost you thousands of dollars in higher interest costs, and can even prevent you from getting a loan at all.

- **Auto Insurance** – Did you know that your insurance company can pull your credit score and use it when determining your premiums? A recent survey showed over 90% of auto insurance companies are already doing this, meaning a low score could be costing you even if you don't have a loan.

- **Employment** – As part of their application process, many employers are now asking permission to access your credit report. Multiple late payments or a previous bankruptcy may make you look undependable, and may reduce your chances of getting that job offer.

- **Landlords** – Much like employers, potential landlords look at your credit score to see if you can be trusted to make your rent payments on time. If you have a poor history with your other bills, a landlord may deny your application.

Knowing how your credit score is calculated is the first step in increasing your credit score (and saving you money). Here is a breakdown of what goes into your credit score and how you can improve it:

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1. **Payment History** – 35%
   This is the largest of the factors in your credit score and reflects how many and what bills you have paid on time, or not. Late and/or missed payments are the most detrimental strike to your credit score.

   Tip: Always make your credit payments on time, even if it is just the minimum amount due. Consider paying electronically or over the phone to ensure that payments are not “lost in the mail,” and be sure to make payments well enough ahead of time to avoid a delinquent report on your credit score.

2. **Amount of Debt** – 30%
   The second major factor is the overall amount of debt you have. However, it is not the absolute amount owed, but the ratio of debt to available credit that is key. If you have $10,000 in debt, but $100,000 in available credit, you will look better than someone who has $5,000 in debt but only $10,000 in available credit.

   Tip: Cut up the credit card if you are not using it, but don’t close the account. The available credit helps your ratio. A ratio above 50% will hurt your score.

3. **Length of Credit History** – 15%
   Simply having a longer track record of paying bills helps your score. Scoring is based on your oldest account as well as the average of all your accounts.

   Tip: Here again, don’t close that credit card account that you have had since college; the history helps. Parents can help their children start building their credit score by getting them their own credit cards early on and teaching them to pay the balances on time and in full.

4. **New Credit/Credit Inquiries** – 10%
   If you have several new credit accounts, or multiple inquiries in a short period of time, it may

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Credit Score Basics *(continued)*

look like you are in trouble and need credit quickly. The good news is that multiple inquiries for a single purchase (i.e. a home) are treated as a single item.

Tip: Don't apply for new credit right before a big purchase, such as a car or a house. Do shop around for the best (lowest) interest rates on loans, as the inquiries will not hurt your credit score, and a lower interest rate means money savings.

5. **Kind of Debt** – 10%
   If you have multiple kinds of debt, such as a mortgage, auto loan, student loans and credit cards, your score will be higher than having just one type of loan.

   Tip: Look for ways to diversify your credit at no cost to you. For example, instead of buying the new washer & dryer with cash, put it on the 6 month same-as-cash store credit card (just be sure to pay it off before the end of the term).

A good credit score is not only important to have in order to finance items such as a home or automobile, but it can also help or hurt in other ways. If you start early, plan well, and use credit wisely and pay amounts due on time, you will be successful in establishing good credit.

Michael Kalscheur, CFP®, is a Senior Financial Consultant at Castle Wealth Advisors, LLC. Castle specializes in helping wealthy families and closely-held business owners with strategies to protect and transition family assets from one generation to the next. Castle's senior partners also work with clients throughout the country in making logical decisions to help them fulfill their personal and business financial goals. For more information visit www.Castle3.com, call 1-888-849-9559, or e-mail Michael directly at Michael@Castle3.com.