Your Credit Score

An insider's guide to credit scoring and home financing

Paragon BANK

Table of Contents

Introduction

Your credit rating and credit score affect your ability to qualify for the best rates on services, insurance and especially home loans. Personal credit ratings and scores have also become a qualifying gauge for employers, particularly those who seek to place employees in a position of management or financial responsibility.

The History of Credit Scoring

The credit scoring system used today was originally designed in the 1950's to help lenders determine how well consumers could pay back borrowed money. The lender's biggest concern was whether or not an individual had the ability to repay a loan in a timely manner.

Congress passed the Fair Credit Reporting Act in 1971 to establish guidelines for fair practices regarding the use of credit scoring. This law was designed to promote accuracy in reporting and protect the privacy of consumers. In light of the increased use of credit scoring and a growing fear of identity theft, recent legislation has been passed to further protect Americans and improve consumer awareness.

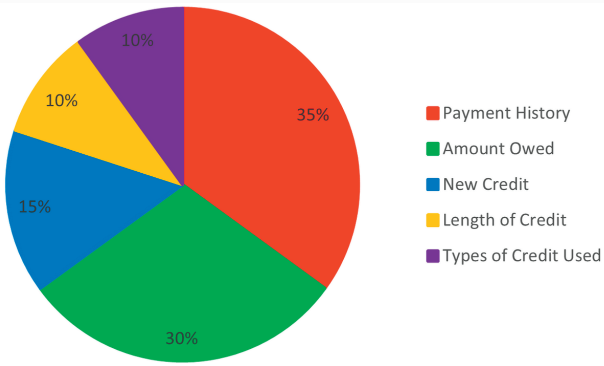
The Fair and Accurate Credit Transactions Act of 2003 (sometimes referred to as The FACT ACT or FACTA was signed by President George W. Bush on December 4, 2003. This amended the Fair Credit Reporting Act, enabling each American to obtain one free credit report every 12 months from each of the three main credit reporting agencies (CRAs): Equifax (R), Experian (R), and TransUnion (R). These bureaus have created a central website, www.AnnualCreditReport.com, to accommodate Americans who wish to obtain free copies of their credit report on an annual basis.

Why Your Credit Score is So Important

The credit scoring model seeks to quantify a consumer's ability to pay off debt on time. Credit scores have may different ranges, however, the score that is used by 90 percent of lenders and creditors in this country is the FICO(R) score, which ranges between 300 to 850. The higher the score, the better for the consumer. A high credit score translates into a lower interest rate, which can save a consumer thousands of dollars in financing fees over the life of the loan.

The Five Factors of Credit Scoring

1	**Payment History** (35% impact)	Paying off debts on time has the greatest positive impact on your credit score. Paying off balances each month rather than only making minimum payments also has a positive impact. Late payments, judgments and charge-offs all have a negative impact. delinquencies that occurred in the last two years carry more weight than older items.
2	**Outstanding Credit Card Balances** (30% impact)	This factor marks the ratio between the amount owed and the remaining available credit. Ideally, the consumer should make an effort to keep balances as close to zero as possible, and definitely below 30% of the available credit limit.
3	**Credit History** (15% impact)	This portion of the credit score indicates the length of time since a particular credit line was established. A seasoned borrower will always be stronger in this area.
4	**Type of Credit** (10% impact)	A mix of credit, such as an auto loan and a credit card, is more positive than a concentration of debt from only credit cards.
5	**Inquiries** (10% impact)	This percentage of the credit score quantifies the number of inquiries made on a consumer's credit within a 12 month period. Each new credit inquiry can deduct points from a credit score. Note that personal credit inquiries do not impact credit scores.



Remember that the credit score is a computerized calculation. Personal factors are not taken into consideration when a credit report is generated. It is merely a snapshot of a credit profile and can fluctuate with time.

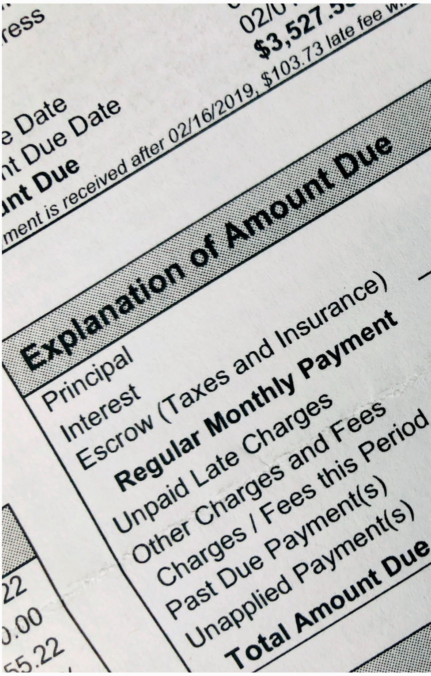
Unfortunately, bad credit scores are mostly a result of late or unpaid and outstanding bill payments. Of course, there are exceptions when unforeseen circumstances come into play, such as health complications or loss of employment. Keeping the five factors in mind will help you manage your credit activities for higher credit scores.

The Impact of a Low Credit Score

1 **Your Interest Rate My Be Higher**
Lower credit scores may be subject to higher interest rates and finance charges over the course of any loan. The website myFICO.com offers a mortgage payment calculator that is updated regularly to show consumers how their FICO(R) score can affect their interest rate.

2 **Your Closing Costs May Be Higher**
Consumers with lower credit scores may be subject to higher closing costs. Known as loan pricing adjustments, these are fees based on your loan amount, implemented by Fannie Mae and Freddie Mac in 2020 to accommodate for the risk associated with lower credit borrowers.

3 **You May Pay More for Private Mortgage Insurance (PMI)**
PMI is insurance that mortgage lenders require from most homebuyers who have less than a 20% down payment when purchasing property. Lower credit scores may be subject to higher private mortgage insurance rates.



Obtaining a Credit Report

If you are considering a home purchase, it is in your best interest to make every effort to increase your credit scores early on. Oftentimes many people are surprised when they find inaccuracies, errors or delinquencies in their credit history as they apply for loan financing.

Today, there are many resources from which to obtain credit information. Consumers also now have the opportunity to correct and maintain credit reports.

Reports from the credit bureaus. You can get started by acquiring a copy of your credit reports from each of the three major CRAs. It's important to get reports from each of the three - not just one - since the CRAs do not share data. The reports provide an idea of what information lenders and service providers see when it comes to your debys and your credit history.

You can order your credit report and score directly from each credit bureau online, through the mail or via telephone for approximately $10 to $20:

- **Equifax: 800.685.1111 www.equifax.com**
- **Experian: 888.397.3742 www.experian.com**
- **TransUnion: 800.888.4213 www.transunion.com**

Free credit reports. By law, each of the CRAs must provide a free copy of your credit report, at your request, once every 12 months. Go to www.AnnualCreditReport.com or call 1.877.322.8228. Note that these free annual reports do not disclose credit scores.

Disputing Errors on the Credit Report

When reviewing your credit reports, make sure that the information contained within the reports is correct. If you find that you have errors on your credit report, you can follow this procedure to correct those errors.

1. Make a copy of the report and circle the item(s) you are questioning. Keep your original copy for your own records.

2. Prepare a letter to the CRA that provided you with the report in question, and request to have the erroneous item(s) removed or corrected. if you have documented proof iin support of your claim (e.g., proof of payment) be sure to include a copy of that documentation with your dispute letter. If you've ordered your report directly from the CRA, fill out the included dispute forms when disputing errors.

3 In addition, prepare a letter to the creditor reporting the item on your credit reports, especially if you feel you are a victim of fraud or identity theft. Inform the creditor that you are disputing an error reported to the CRA, state why the claim is inaccurate, and include any relevant documentation to prove your point,

4 Send your correspondence via certified mail.

You should receive a response from the CRA within 30 to 45 days. if the error has been corrected, they will send you a fresh copy of your credit report at no charge to show you that the item has been removed or corrected.

if the bureaus do not respond within 30 to 45 days, send a follow-up letter reminding them that per the Fair Credit Reporting Act they were required to respond within 30 days from the date they received your initial dispute. Also remind them that they are liable for damages, including punitive, for non-response, and that if necessary you will seek legal representation. Attach your original dispute letter and proof of delivery to the complaint.

Just because the credit bureau has determined an item "investigated" does not mean the results are accurate. If you are 100 percent sure that your claim is true and accurate, and the bureau responds stating that the creditor has verified the information and the item will not removed or updated, you must request a reinvestigation under Section 611 of the Fair Credit Reporting Act. It's best to do so within five days of receiving the results of their investigation.

You can repeat this process as many times as you want; however, after three to four attempts, you may consider filing a complaint with the Federal Trade Commission Consumer Response Center. You may be able to have y our case added to a class action lawsuit against the bureau that is reporting the inaccurate information. You can access the FTC Complaint Assistant at www.ftccomplaintassistant.gov.

What If I Have No Credit?

On occasion, those seeking financing will not have enough credit history to obtain the loan they wish to secure. In this case, they can start establishing history by opening small lines of credit that report to all three major CRAs, and make purchases that can be paid off easily. Your bank or credit union may be a good place to start to request a credit line.

if you have not yet established credit, you are completely out of luck. An alternate option would be to obtain a secured credit card. A secured card may be an excellent way for a person with no credit to establish credit. This type of card works like a debit card and will require deposited funds for purchases - the main difference being that your credit history will be reported to the three credit bureaus. Do your research up front to ensure that they do so. Also be advised that not all banks or credit unions offer secured credit cards, and some cards may even charge application and other fees.

It is also wise to start saving money for the down payment on your home. The lender will look at your application more favorably when you are able to provide a down payment percentage. Bear in mind, there are certain loan programs available that permit a percentage of gift money (for example, from relatives) for down payment.

Do's and Don'ts During the Loan Process

Each lender has different credit guidelines to follow. Some lenders are required to order a credit report a second time prior to loan closing, which is why it is crucial to avoid certain credit behaviors during a loan process. The following tips are examples of some key credit behaviors during a loan process:

DO SIGN UP FOR CREDIT MONITORING so that you can watch your credit from shopping to closing. For a small fee, usually less than $15 per month, many companies and even CRAs themselves offer monthly credit monitoring services to inform you of any new credit activity that may impact your scores. Credit monitoring is especially helpful to detect the first signs of identity theft.

DO PAY BILLS ON TIME. Stay current on existing account and avoid any late bill payments. Paying more than your minimum balance due will help keep debt in check and could also improve your credit worthiness.

DON'T APPLY FOR NEW CREDIT. New credit inquiries can negatively impact scores. Depending on elements in your current credit report, a score can drop as much as 15 point for a single credit inquiry.

DON'T MAX OUT YOUR CREDIT CARDS. Use credit modestly during the loan process, and avoid major credit card purchases. Balances exceeding 30 percent of the total available credit line can bring credit scores down. This includes transferring debt from one card to another, which will impact the total available credit per card.

DON'T CLOSE CREDIT ACCOUNTS. Closing a credit card will adjust the total amount of available credit, which will impact credit scores. Also, closing a card may impact other factors to your score such as the length of your credit history.

FINALLY, DO STAY IN TOUCH WITH YOUR LOAN AND REAL ESTATE PROFESSIONALS. Consult your mortgage or real estate professional with questions about whether a specific action can affect your credit reports or scores during the loan process.

Credit Education

The Federal Trade Commission (FTC) regulates credit repair services and provides free resources to help consumers better understand credit. Visit www.ftc.gov for publications and online information.

Paragon BANK

Nancy Walls
Community Development Officer
NMLS #1564258
901.626.5201
nancy.walls@bankparagon.com
bankparagon.com