

FICO 08 – The Good, The Bad and The Ugly

It appears Fair Isaac's new version of the FICO scoring model is about to become a reality. The release of FICO 08 has been delayed for over a year due to public outcry and lawsuits over some of the changes surrounding the new model. All appears to be settled now and its release by all three bureaus will be soon coming.

TransUnion has implemented the new model and it is expected that Equifax and Experian will release the model before the end of the year.

Many financial institutions have already adopted FICO 08, but for mortgages, lenders doing traditional conforming loans backed by Fannie Mae and Freddie Mac are still waiting for Fannie and Freddie to approve the new model. Freddie Mac has started testing and they hope to begin using the new model as soon as October. We expect Fannie and Freddie to adopt the new FICO scoring model by the end of the year 2009.

What does this mean to you? Let's start with **the Good**.

The new formula will include some authorized user accounts. According to Fair Isaac they have figured out a way for the new model to recognize legitimate Authorized User accounts as opposed to Authorized Users who have "rented" trade-lines to piggyback on someone else's credit. So adding a spouse or child to a credit card will still benefit them.

The new model will also be a bit more forgiving of a consumer who has had a charge off or a repossession as long as the rest of their credit is good and as long as they haven't had any issues after the negative account.

Perhaps the best aspect of the new model is that the formula will ignore small collections under \$100. In the past few years, things such as library fines, parking tickets and those extremely frustrating small medical bills have started to appear on credit reports causing incredible damage to scores. With the new model any of these under \$100 will still show up on the report but they will no longer be factored into the scores.

Now for **the Bad**.

It's always been known that closing accounts won't help your scores and could possibly hurt them. Now it will absolutely hurt them and could hurt a lot. The more open accounts you have the better. And if you have more closed accounts than open accounts you could see a significant decline in your credit score.



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To avoid having creditors close your accounts due to inactivity you're going to need to use them. The new scoring model does not like a lot of unused cards. And a lot of creditors anymore will automatically close your cards if they have not been used for a while. Charge a tank of gas or buy a new pair of socks and pay the card off when the bill comes, but use it.

FICO 08 also puts more emphasis on a mix of credit – revolving and installment loans. If you have only credit cards your score will be lower than someone who also has some sort of installment loan, like a mortgage or auto loan.

And **the Ugly**.

High balances on credit cards have always been an issue and now they will carry even more weight. It used to be that keeping a balance below 50% of the high credit was good and below 30% was great. With the new model, below 30% is good and below 10% is great. With so many credit card companies feeling the credit crunch, some of them are slashing credit limits – sometimes as much as by 50%, which could be detrimental to a consumer's credit scores.

If you get a letter from one of your creditors saying they are decreasing your credit limit (they have to notify you by mail), see if they will reverse the decision. They may or may not agree to do this but your chances may be pretty good if you have a good payment history with them. If that doesn't work try moving some balances around. This may mean you end up with 4 or 5 cards with balances as opposed to 1 or 2 but it's better to have 5 cards with low balances when one card with a high balance. And remember, the scoring models do not take it into consideration that you may pay the bill off every month. The creditors may report to the bureaus a week or two before you pay the card off, so that is the balance that will end up on your credit report.

So there it is – not all bad but not all good. Pay attention to your balances, try to have a good mix of credit and keep those older accounts open and the affect of these changes to your credit scores will probably be minimal.



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