

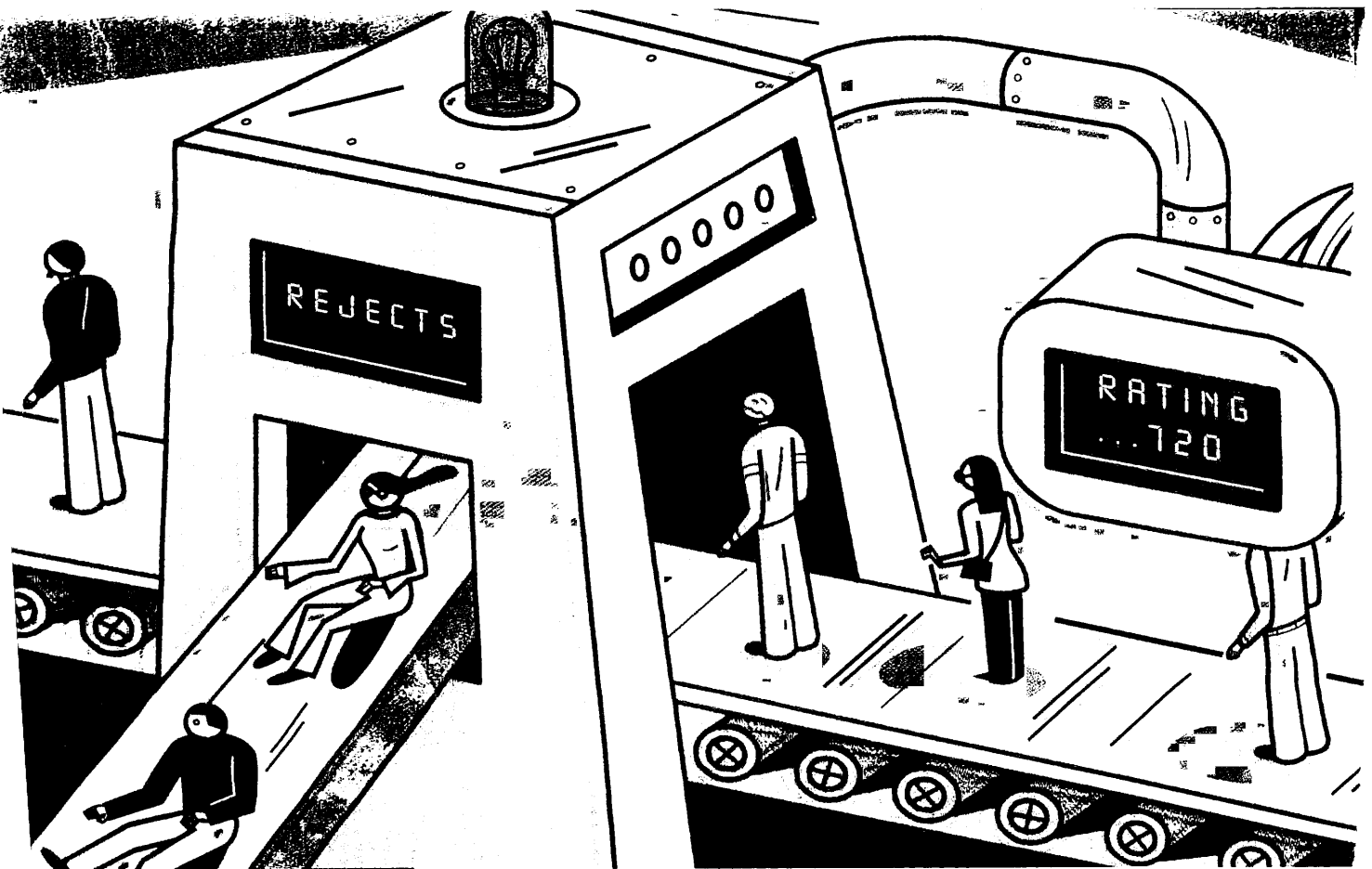
Anatomy Of a Credit Score

More companies are looking at ratings—so managing them is crucial. **BY TODDI GUTNER**

DURING A SHOPPING spree a few months ago, I opened several retail credit-card accounts to take advantage of an immediate 10% discount on that day's purchases. Surely this familiar offer was risk-free as long as I paid my bills on time, right? It wasn't until I reported this story that I found out my credit score could have been negatively affected by the spate of new accounts I opened in such a short time. I had no idea.

Many people are ignorant of what their credit score is, how they can hurt or help that score, and how it can be used against them. Some 49% of 1,013 consumers polled do not understand that credit scores measure credit risk, according to a 2005 survey by the Consumer Federation of America and Fair Isaac Corp., the company that created the most widely used credit score formula called FICO.

Lenders have used these scores for years to determine whether to grant you a





SimplyAccountable. Up to 30% Savings...Guaranteed.

Companies need more accountability when it comes to health care costs. Which is why UnitedHealthcare created SimplyAccountableSM, our new product that provides guaranteed savings on health care costs for new self-funded customers with a minimum of 300 employees. Here's how it works – We'll perform a benefit plan assessment and recommend the optimal mix of UnitedHealthcare's network, clinical and consumer solutions. And then we'll put a substantial percentage of our fees at risk as our guarantee of annual savings for you.

To learn more, talk to your broker or consultant, or visit uhc-cfo.com/BWM



Value 2

Some restrictions may apply based on group size. Administrative services to self-funded plans provided by United HealthCare Services, Inc., United HealthCare Insurance Company or United HealthCare Service LLC. Insurance coverage provided by or through United HealthCare Insurance Company, United HealthCare Insurance Company of New York, or their affiliates. ©2005 United HealthCare Services, Inc.

loan and what interest rate you'll pay. "Credit scores are very powerful predictors of consumers' future [bill-paying] performance," says Mike Fratantoni, a senior research director at the Mortgage Bankers Assn. But with the rise of technology that can automatically assess consumer creditworthiness while you wait, FICO scores are now requested by insurance companies, cell-phone providers, utilities, landlords, and even prospective employers. That's a reason to make managing your FICO score a priority.

But first, just what is a credit score? To come up with one, Fair Isaac uses 22 pieces of data collected from the three major credit bureaus (Equifax, Experian, and TransUnion) to calculate a credit score—300 is the lowest, 850 the highest. The final number is a composite that comes from individual ratings in five categories: payment history (35% of the rating); length of credit history (15%); new credit (10%); types of credit used (10%); and debt (30%). Income is not a factor. "A person can have a very high income and nev-

er pay their bills," said Craig Watts, public affairs manager for Fair Isaac.

Fair Isaac calculates a FICO score based on the data provided by each credit bureau. It's not uncommon to see up to a 50-point differential between ratings. The reason: Bureaus collect data at different times of the month, or one bureau may have inaccurate information.

The higher the score, the lower the risk you are to a creditor—and the less interest you'll pay. Only 13% of the population has FICO scores of 800 or above; the median is 723. There is no single cut-off for loans, and it varies from industry to industry. But generally borrowers with scores above 740 receive the best rates.

To see how a change in your FICO score affects how much you'll pay, consider this example (table). On a \$350,000, 30-year fixed mortgage, you'll pay 6.24% in interest, or \$2,153 a month if you score between 720 and 850. If your score drops to between 620 and 674, your interest rate jumps to 8.05%, and your monthly cost rises to \$2,581. You will pay an additional

\$154,131 over the life of the loan, according to a calculator on myfico.com.

WATCH YOUR WORTHINESS

WANT A PEEK at your FICO scores? Many people think they can get their FICO scores from their credit reports. They can't—but it's still a good place to start. The Fair & Accurate Credit Transactions Act of 2003 entitles you to a free credit report from each major credit bureau once a year. I ordered my reports by telephone from annualcreditreport.com and received them all within 10 days. It's smart to request a report from a different agency every four months so you stagger the reports over a year. That way, if there's bad information in one, you'll spot it sooner.

When you request a free credit report, each bureau will offer to calculate a credit score for \$6.95. Experian and TransUnion use proprietary formulas; Equifax uses FICO scores. Pass up these offers because the information is not as comprehensive as you'll get elsewhere, and lenders are less likely to look at these scores.

For the most detailed explanations on

Higher Scores, Lower Rates

Lenders use FICO scores, three-digit numbers ranging from 300 to 850, to determine your creditworthiness. You have three FICO scores, one from each major credit bureau. Generally, the higher your FICO scores, the lower your interest rate. See how different FICO score ranges affect interest rates and monthly payments on a \$350,000 30-year, fixed-rate mortgage:

FICO SCORE	ANNUAL PERCENTAGE RATE*	MONTHLY PAYMENT	TOTAL INTEREST
720-850	6.24%	\$2,153	\$424,984
700-719	6.37	2,181	435,252
675-699	6.90	2,306	480,005
620-674	8.05	2,581	579,115
560-619	8.53	2,699	621,601
500-559	9.29	2,889	690,134

*Rates as of Nov. 11

Data: Informa Research Services, Inc., myfico.com

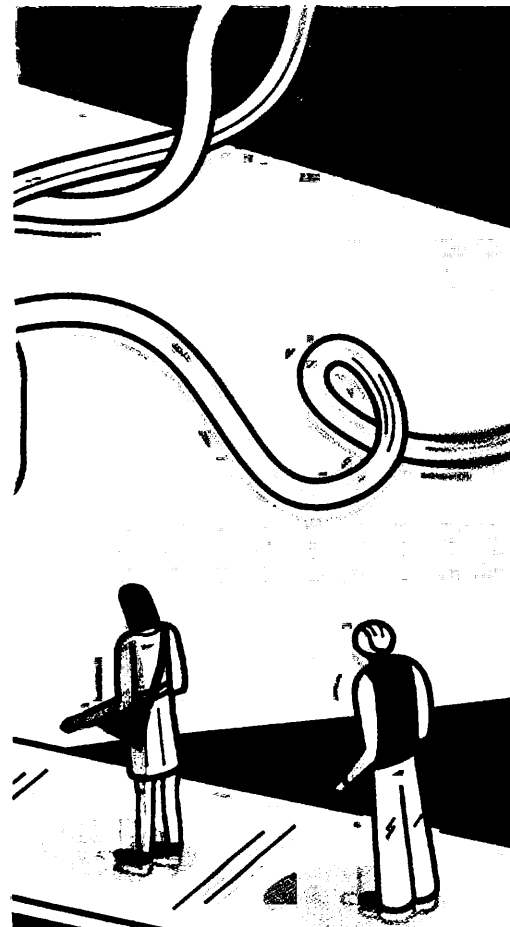
your FICO scores, go to myfico.com. A score from one credit bureau costs \$14.95, all three are \$44.85. It's useful to buy all three because large lenders either average the scores or take the middle one. You'll want to check your FICO scores once a year or several months before you apply for a loan.

The negative factors that bring your score down remain on your credit report for seven years and can adversely affect your FICO score. But lenders typically look back only in the past two years when they make credit decisions. One 30-day late payment shouldn't make a difference. Lenders look for trends.

I paid for three scores and anxiously waited while the computer calculated them on the spot. Within seconds, I was relieved (not to mention a bit proud) when 771, 751, and 738 popped up on my screen. Still, I wondered why I wasn't in the 800-plus range. To find out, I reviewed the various strategies credit experts recommend to raise FICO scores.

» Pay all bills on time. This is probably the most important factor in the FICO calculation. If you're consistently 30 days

HARRY CAMPBELL



overdue, your score can drop by as much as 100 points, depending on how long the account has been open and how long ago the late payment took place. To avoid late payments, consider automating your bill-paying process. I got high marks in this arena.

»Think twice before closing accounts. Lenders are looking for consumers with long credit histories that have been managed well. But because of the increase in identity theft, you don't want too many open accounts that you don't use. "Be judicious about the accounts you have," says Norm Magnuson, public affairs officer for the Consumer Data Industry Assn. In an effort to consolidate our finances, I canceled an American Express account I had for 20 years to become an authorized user on my husband's account. While I benefit from his 20-year credit history on that account, it was still a mistake to eliminate my own. I have a few cards in my name only, but the history isn't as long.

»Minimize credit-card applications. Bingo. That was cited as a problem on all three of my FICO scores. On average, a consumer has a total of 11 credit obligations, of which seven are credit cards and four are loans. I had 21, of which six had balances. Each time you apply for credit, a lender requests to view your report. This inquiry is noted and can reduce your overall score. Don't apply for unnecessary credit, and if you're in the market for a big-ticket item that requires a loan, avoid credit applications for 18 months prior to your purchase.

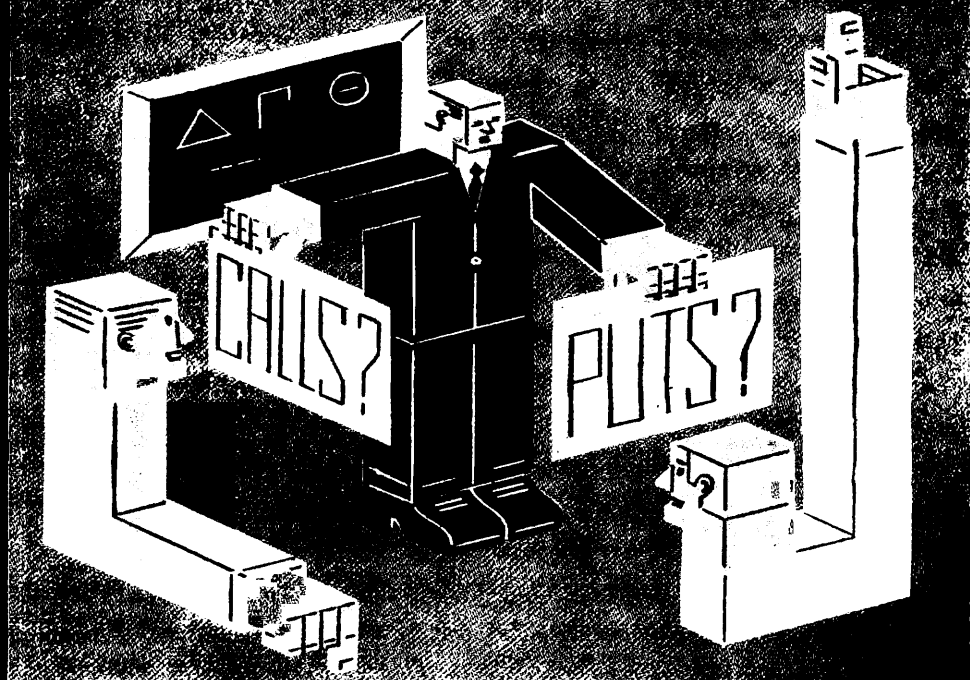
»Keep balances low. The FICO score evaluates your total balances in relation to your available credit. This is known as credit utilization. Credit cards that are "maxed out" can lower your score. Try to spend only 30% of your credit limit. If you have a \$10,000 limit on one card, keep the balance near \$3,000. My credit utilization was too high. It helps that I pay off my balances every month, but it is better to spread the spending.

While my FICO reports said that "most lenders would consider consumers in this score range as extremely low risk," the competitive spirit in me wants to get over the 800 mark. To that end, I recently refrained from signing up for a Target Stores credit card to get \$10 off on a \$100 purchase. ■

BusinessWeek **weekend**



For more on this story watch BusinessWeek Weekend. Check your local listings or go to businessweekweekend.com to view this and other stories from our weekly TV program.



The Agony Of the Options

Or how a crash course on "bear put spreads" and "collars" left me humbled. **BY ADRIENNE CARTER**

IHAVE ALWAYS CONSIDERED myself a savvy investor. My father taught me about mutual funds at the age of 12, and I opened my first brokerage account when I was 20. But after spending two days learning to trade options, I was humbled.

As an investor, I understand the appeal of options. Options contracts, which give the right but not the obligation to buy or sell stocks, indexes, or other financial instruments at a specific price in return for paying a premium, can help hedge a portfolio or generate income in a market that's moving sideways. That, plus cheaper online commissions and improved trading technology, helps explain why the options market is booming. In October monthly options trading volume hit an all-time high of 155 million contracts, up nearly 44% from the previous year, according to the Options

Industry Council, a trade organization.

Using options can be hazardous to your portfolio's health if you don't know what you're doing. These days, you can get educated dozens of ways, from books and Web sites to classes and personal tutoring (table, page 120).

Upon the recommendation of an industry insider, I signed up for the two-day introductory course at Optionetics, designed to teach individuals how to trade options on their PC or via a broker. The Redwood City, Calif., financial education firm has been giving such seminars for over a decade. Since 1993, more than 50,000 people have attended its courses in major U.S. cities and abroad. Because I was reporting a story, I didn't pay the tuition, which typically runs around \$4,000.

My 120 or so classmates at the Brooklyn (N.Y.) site in early November were a diverse group. I'd expected mainly re-