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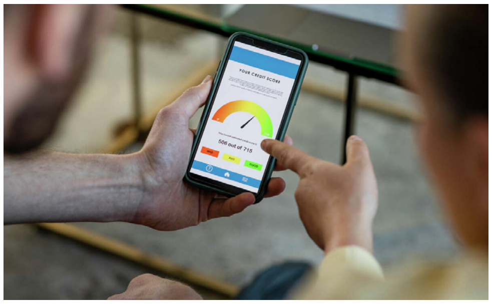
FICO SCORE VS. CREDIT SCORE: WHAT'S THE DIFFERENCE?



By: Aly J. Yale - May 11, 2023

Your credit score plays a big role in your financial life.

It can determine what loans you're eligible for, what rental properties you can secure, and even what interest rate you'll pay on your mortgage.

But what exactly are credit scores? And how are they different from FICO scores? The short answer is that FICO scores are one type of credit score. Here's what you need to know — and the credit scores you should be shooting for.

FICO scores vs. credit scores

A credit score is a numerical representation of your risk as a borrower. Scores range from 300 to 850. Lower scores are riskier (meaning you're less likely to repay a loan) and higher scores indicate less risk.

There are several types of credit scores. FICO scores — or those issued by the Fair Isaac Corporation (FICO) — are the most common. There are also VantageScores, which are issued by the three main credit reporting bureaus: TransUnion, Experian, and Equifax.

"The FICO credit rating is the widest-used system for assessing your credit — or another way to determine how well you are managing and being responsible with your credit and debt," says Kristopher Whipple, founder and partner at Kristopher Curtis Financial in Nashville, Tennessee. "Generally speaking, a higher FICO score suggests you borrow and pay back what you owe on time."

Keep in mind that your score can vary depending on what type of score it is. For example, your FICO score may be higher or lower than your VantageScore, as each score weighs a variety of factors differently. There are also multiple models of each score — like the FICO 2, FICO 3, and FICO 8, for instance.

"Some of these models are targeted at specific industries and applications like mortgages, auto loans, and bank cards," says Rob Burnette, an investment advisor at Outlook Financial Center in Troy, Ohio.

If you don't yet know your score, check with your bank or credit card issuer. Often, these companies offer free credit score monitoring. If yours don't, you can purchase your credit score from one of the three credit bureaus. (The bureaus will also typically provide you with one free credit report a year.)

What are credit scores used for?

Credit scores serve many purposes, not always related to actual credit. "FICO scores and credit scores are used by lenders, credit card issuers, landlords, and sometimes employers to assess your creditworthiness and financial responsibility," says Markia Brown, a certified financial education instructor at Money Plug. "These scores help them determine your eligibility for loans, credit cards, rental agreements, employment, and more."

Lenders use them to assess risk when considering a new borrower. "Based on your score and the evaluation of risk by the lender, [the lender computes] the amount of credit offered, the interest rate, and payment terms," Burnette says.

The better your credit score, the more likely you'll get approved for a loan — as well as get approved for the amount you want with an affordable interest rate. (Lower scores mean the opposite).

Employers sometimes use credit scores to evaluate how financially responsible a job candidate is, while landlords use them to determine if a possible tenant is likely to pay their rent. Finally, credit scores also factor into insurers' risk assessments. Car and homeowners insurance companies may give lower premiums to policyholders with high credit scores and pricier ones to those with low credit scores, as they have a higher likelihood of making claims.

Good vs. bad credit scores

Having a good credit score can make a big difference in what loans and financial products you're eligible for, as well as what interest you're charged. Good credit can also help you secure housing or even land a job.

But what's a "good" and "bad" score depends on the model. See below for a breakdown of credit score categories for both FICO and VantageScores.

You'll need to meet a minimum score to qualify for most loans and financial products, but the exact score varies widely. With mortgages, for example, you usually need at least a 620 score to get a conventional loan. An FHA mortgage, which is backed by the government, requires just a 500.

"Above 700 gives you a lot better loan option rates," Whipple says. "And higher than 750 gives you the best potential of low rates on your loans."

How to improve your credit scores

If your score isn't in the "good" range or better and you plan to apply for a loan, new employment, or rental housing, you may want to work on improving it before you do.

There are many ways to do this, but "First and foremost, pay your bills on time," Whipple says.

He's right: With FICO scores, payment history makes up 35% of your score — the biggest chunk out of all five influencing factors.The other factors include credit utilization (how much of your available credit you use), length of credit history, mix of credit accounts (such as a credit card, car loan, mortgage, and more), and the number of new credit accounts you've opened recently (fewer is generally better).

You can also ask to increase your credit limit on your credit cards or, if you have high balances, work on reducing those. Ideally, you want to keep your credit utilization — or how much of your total credit line your balance accounts for — to 30% or less.

"Keeping your credit utilization to less than 30% is another way to improve your credit score," Burnette says. "Utilization above 50% will have a negative impact."

Finally, if you don't have much experience with credit, think about getting a credit card, using it for day-to-day expenses, and paying it off each month.

"Start using credit cards sparingly and pay them off immediately," Whipple says. "One idea is to only use a credit card at the gas station — something you already have to purchase monthly and is typically not a huge expense. Using the gas station technique or even your monthly utilities and paying them off quickly can be a great way to build credit."

Kristopher and his partner, Curtis, have just opened their new office in Nashville, Tennessee. They bring over 30 years of experience and relationship to the financial industry with a focus on tax and retirement strategies. They pride themselves on making the complex simple. Kris, his wife Liz, and their 4 kids have lived in Nashville for 14 years.

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