Keeping credit scores clean before you close on a home

Don't go overboard on credit cards or you may lose the loan

Print Email

By Lisa Holton

You've done everything right. You started your home search with a personal credit score of around 700. You took your time finding the right lender, the best interest rate, and made sure you prequalified for a loan before you started hitting open houses. You found the perfect place at the right price.

Now you're at closing ready to sign -- but something's amiss. You check your loan papers against your earlier documents and find that the rate you thought you had is significantly higher. Or even worse, the closing officer walks in with a pale expression and a cell phone and says it's your lender calling.

You don't have the loan after all.

It happens. Unwitting prospective homebuyers who go on credit card binges -- be it for appliances, furniture, paint or decor items -- for their new homes the minute their loans are approved could face the same situation.

While it doesn't happen all the time, some lenders' underwriting departments take one last-minute look at your score to make sure you're not overextended by the time the first payment rolls around. It's one more sign that credit scoring is a 24/7 process in a world stung by economic hardship.

Says one Chicago-area lending expert, "It's not something loan officers would do because they want to close loans. But in this economy, there are nervous underwriting departments behind them that do double-check scores before closing just to make sure that people can actually pay that mortgage on time."

Lenders policies vary

Such credit roadblocks are a frustration for potential buyers facing the most affordable U.S. home market in recent years. IHS Global Insight, a forecasting agency, released figures early in December 2008 showing that by the end of the third quarter, home prices across the United States were 6.5 percent below their 2007 peak.

According to Tom Kelly, a Chicago-based

spokesman for Chase, double-checking credit scores after a loan approval is given is not their policy. "Once a mortgage application is approved and the rate is locked, we do not make additional credit inquiries. Regarding credit advice, we always ask potential buyers to review their credit file in advance, clear up any errors and get pre-qualified."

However, Barry Paperno, consumer operations manager for Fair Isaac Corp., the company that created the FICO credit score, says that based on what his company sees, lenders of all sizes sometimes do re-check credit scores during the loan process. "Lenders have always had the right to do that."

Homebuyers face stricter lending requirements
Yet Paperno notes that lender caution has set the bar significantly higher in the past year alone for borrowers hoping to score a lender's best rate. "Right now, 760 is the minimum requirement for the best rates on a 30-year fixed mortgage -- that's about 20 points higher than it was at the same point a year ago."

Henry Apfelbach, assistant vice president and home loan manager for Countrywide Home Loans in Chicago, says credit scoring is important, but only one major part of the picture when it comes to approving borrowers for favorable rates. "Loan-to-value matters too. I just priced out a mortgage loan at a 666 (FICO score), but it had an LTV of 31 percent, not 80 percent, and it got a very good rate. Maybe not the best, but these people had the right compensating factors to keep them in the game."

As for the scenario of borrowers being approved for loans only to see changes or cancellations later once they've gone overboard with spending, Apfelbach won't confirm or deny such scenarios, but will add this. "Any professional in this business knows the No. 1 thing and that's to set a borrower's expectations properly. I have to represent my company in the proper way, and that means coaching your client properly to manage that credit," says Apfelbach. "If someone is buying a home for the first time, and they're tight on things, I always tell them not to go wild on things. It's not only about a closing scenario, it's about how they're going to afford everything in their lives once they get into that

Hoping to buy a home?
Do a 1-year credit makeover

If you fear your credit score -- or any other aspect of your credit history -- may keep you from your dream of homeownership, now is good time to clean up your act. Here are some suggestions:

Get those balances down: An upcoming change in Fair Isaac's FICO scores will reward lower debt utilization. Make a plan to get debt levels in each account under 50 percent or less. And be smart -- pay off your highest-rate balances first.

Get some advice: You might be focused on pulling together a down payment, but it might not be a bad time to sit down with a tax professional or a financial adviser to talk about the way you're going to manage your debt going forward.

Set a credit report review schedule: You have the right to get all three of your credit reports -- from Experian, TransUnion and Equifax -- once a year for free. You can do so by ordering them at annualcreditreport.com. Don't order all three of them at the same time, though. By staggering receipt of each of your credit reports, you'll get a continuous picture of how your credit picture looks because the three bureaus feed each other the latest information. It's a good way to clean up errors and keep a steady watch for identity theft.

Give up the late or minimum payment habit. If you've failed to make on-time payments of credit card bills, car loans or utilities, it's time to turn a new leaf. Likewise, adjust your overall spending -- give up a latte or six -- so you can pay more than your minimum balances. One trick for paying on time: get a calendar and when bills come in, mark the due date and then mark a mailing date five to seven days before that on the calendar. The other alternative? Go electronic. If you have electronic bill payment, you designate when the bill is due and pay the bill with a push of a button the day before. It'll keep you in good stead with your lenders while home."

In any event, Apfelbach maintains that "anybody who qualifies in the normal tradition of a loan is not seeing any more difficulty than they did in the past. The only customers I see surprised in my business are those looking for no-doc or low-doc loans (loans based on limited income verification). These were really meant for people who didn't want to disclose income, so they were willing to pay a higher rate. They weren't meant for everybody as they came to be during the past couple of years."

improving your cash flow.

Lay off the cards (mostly), but don't close the account: Closing accounts -- even those that have had $0 balances for years -- is a bad idea. Lenders want to see a long record of credit management, and longtime accounts that you haven't touched in years may actually help your score because it shows you have some restraint. Card issuers have become quick to close dormant accounts, so break out the card and use it occasionally.

One real estate agent says she feels a responsibility to keep her clients informed about maintaining their credit. Judy Demetriou, a partner with Village Green Realty in Winnetka, Ill., says, "I generally go over the whole issue of keeping good credit data when we first talk ... usually, buyers here don't go crazy buying things before the closing, but I do tell them to wait until they are in the house or condo a while to see how they use their space." Yet she adds that "today's young people, first-time buyers, have lived with using credit so easily that they don't understand the importance of good credit and how much debt they should have, though there's the beginning of awareness about this. It's starting to change."

How a new credit score will affect borrowers

Paperno says that Fair Isaac next year will launch an update of its FICO score and the more important issue may be how vigilant consumers are not only about their on-time payment behavior, but how well they monitor their balances going forward. On the good side, there will be a certain increased leniency toward one-time late payments on bills. "Let's say you're late once, but your history has been very clean over the last couple of years. With the new version, being late on one account will not have as much of an effect as it does right now," Paperno says.

Borrowers will take a heavier hit on balance levels in the future, he says. "Folks with higher credit utilization, the score will be more sensitive. So get those balances down." Paperno suggests that the best idea is to bring balances on all lines of credit -- and particularly credit cards -- to 50 percent of their limit and keep cutting from there. "The lower your utilization, the better your score."

See related: Use it or lose it: Issuers quick to close dormant accounts, Learn the ABCs of credit scores, credit scoring

Published: December 10, 2008

Comments or questions, Story archive

Three most recent Credit scores, credit reports stories:

- Experian FICO score may soon be off-limits to consumers – Come Valentine's Day, you will likely lose access to your FICO score from credit bureau Experian, even though lenders will continue to use that score to make decisions about your credit. ...
- Long-awaited credit scoring revisions unveiled – The rollout of the long-awaited update to Fair Isaac's popular FICO credit scoring model was finally announced today, but it will likely take some before the changes have a real impact. ...
- Are you a bankruptcy risk? Enigmatic score may tell lenders – It's a number that lenders may consider when deciding whether or not to lend you money, but it isn't the well-known credit score. Meet the bankruptcy score, the credit score's more mysterious cousin. ...