Why Maintaining Your Credit Score Becomes Even More Important During the Continuing Credit Crunch

It's always a good idea to be vigilant about your credit score, but even if borrowing loosens up a bit in 2009, you still need to do everything necessary to keep your credit score high.

Fair Isaac, the company that created the FICO score, has been working on a new version of its landmark credit scoring method that might have serious consequences for you if you're planning on borrowing for a home or establishing any other new credit in 2009.

The new version of FICO is going to be particularly focused on your balances, not only on your on-time payment records.

Your top priority under this new system: Get balances down.

Reports say that the new FICO revision will actually allow a bit of lenience on late payment – something that might affect more than a few consumers with the downturn in the economy. Obviously, this won't mean that someone can chronically pay late, but once or twice won't make the same impact as in earlier FICO versions.

Yet credit utilization – essentially the amount of credit you're actually using relative to your credit limit – is a much bigger deal simply because high balances are so prevalent right now. From the lender's perspective, high balances mixed with a tough economy means a higher risk of default among customers.

So what's a good target utilization rate for all your revolving credit accounts? No more than 50 percent of your credit limit, and if you can get it significantly lower than that over time, that's a good plan. So, the lower your credit utilization, the better your score.

What does that mean for ordinary Americans who don't meet that under-50 percent goal? It means you shouldn't be applying for new credit or refinancing for awhile. But because most lending institutions may continue their strict lending requirements, you might as well defer borrowing goals in favor of reforming your credit behavior.

So instead of bemoaning your tougher chances of getting a loan for a home or a car, why not use the current environment to launch a credit makeover that will position you for a better shot six months to a year from now? Some ideas:

You'll need at least a 740 score for the best rates: You'll often hear that credit scores of 700 and up will get you best customer status with lenders. You should aim higher. For the lowest rates and best terms, you need to get your credit score above 740 (the top credit score, by the way, is 850), so keep that target in mind.

Budget: If you've never reviewed your spending and picked out areas where you can cut, you've never done a budget. Start tracking your spending either on paper or with financial planning software and start pinpointing what spending you can shift over to paying off debt.

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One more time -- get those balances down: Get all your non-deductible debt under 50 percent of your credit line in each account. Go after your balances with the highest interest rates first, and once you hit 50 percent...keep trying and get those balances down further.

Get some advice: It might not be a bad time to sit down with a tax professional or a financial adviser – such as a CERTIFIED FINANCIAL PLANNER™ professional -- to talk about the way you're going to manage your debt going forward.

Keep an eye on your credit reports: Remember that 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 www.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. You'll also be able to clean up errors as you find them -- errors can drag down a credit score – and you'll also keep an eye out for identity theft. Oh, and by the way, keep in mind that all "free" credit report sites are not free – if they ask you for a credit card number, remember they're doing that because they want to *charge you.* Just go to the site above and you'll be fine.

Get on time and pay more than the minimum: Yes, we indicated above that you might get a bit of a break on late payments with the new FICO system, but that's a break you should consider only in a dire emergency. Electronic bill payment will allow you to save on postage while guaranteeing on-time postage, and the budgeting advice mentioned above will allow you to put a few more bucks toward getting that loan or credit card bill paid off.

Once you're paid off, don't close the account: In the world of credit scoring, closing accounts (even those that have not had balances for years) is a lousy 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.

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