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# Preparing Credit For Loan Approval After Damage Due To The Economic Downturn

by [Advisor Voices](#) on February 13, 2014 | posted in [Advisor Voices](#)By [Tracy Becker](#)Learn more about Tracy on [NerdWallet's Ask an Advisor](#)

Most consumers do not understand how credit scores work. Even if a person has experienced a bankruptcy, foreclosure, short sale or loan modification — or has fallen way behind on mortgage payments— they can still participate in the home ownership/loan approval process again.

There are new kinds of loans and assistance for those who have experienced major, credit-damaging events.

To understand the total picture of improving one's credit, we must look at the rest of a consumer's credit portfolio, not just his or her delinquent accounts.

Yesterday I reviewed a credit report with a FICO score of 724. This report included a short sale from August 2013. FICO has published information about how short sales affect credit scores. If you started with a 780 and had a short sale with no deficiency balance your score could drop as low as a 655-675. Obviously, the individual with the 724 FICO score after the short sale must have had an 840 FICO prior to the damage. Although it is very unusual to see such a high credit score, it speaks to how important building the best credit scores can be — even when you face a catastrophic credit problem.

This woman had many active credit accounts, old average age of credit, low balances on her credit cards, and a nice variety of installment, revolving and mortgage accounts. The only delinquency was the short sale. With a 724 score she might qualify for loan approval within 12 months depending on why the property went to short sale. If it was due to the economic downturn — and if proof of this could be documented — she could qualify with a lender who's participating in the FHA's new "Back to Work" program. With her very good credit score she would probably get the best pricing as well.

On the other hand, if a consumer had the same short sale with many other delinquent accounts and unpaid bad debts over varied time periods, the score would be much lower, probably in the low 500s. This type of credit would not win loan approval under the FHA program, since one of the rules is the credit must reflect all delinquencies occurred from the same economic hardship. Therefore late payments from varied timeframes would knock a person out of qualifying. Besides losing out on participating in the "Back to Work" program, this individual's credit score is so low that he may have to wait many more years to get approved at affordable prices. Working on improving his credit as quickly as possible could save some of those years where he would be waiting for the score to inch back up naturally.

For someone who has had bad debt that was settled and paid with limited or no open credit, it is essential to open and nurture the right new credit accounts. With only closed negative credit, a consumer may not even have a credit score. To open new credit they must shop for only those cards that would be approved for someone with such poor credit. Seeking out the right credit repair specialist who could improve some of the delinquencies while providing credit management skills and education, could change this person's quality of life for years to come.

For example, John has a 501 FICO score. He is in his early thirties and is beginning to make a nice income. He wants to purchase a property for himself. He did not understand how credit worked in the past, therefore he had late payments on an overdraft account as well as a medical collection and a delinquency on a store card. He also co-signed for a mortgage to help his mother, but unfortunately she lost her job and the home went to short sale four months before we met him.

After reviewing his credit we found there were some accounts that could be improved to current. John began the credit repair process and used our client educational credit website to develop his credit management skills and learn how to build good credit. After a few months we had changed three of his delinquent accounts. He began applying for better credit cards and started using them correctly. He also followed steps we offered on being added to an old credit card of a trusted friend. This was a year ago and now his scores are a 680. He may also qualify for the "Back to Work" loan.

When John began his credit repair process he had no idea he would have the opportunity to get loan approval within this short period of time. Because he worked on improving his credit through our repair process, his 680 FICO credit score will afford him very reasonable rates if he is approved for a home loan.

Most negative information remains on a person's credit report for at least seven years from the date of the delinquency. A bankruptcy could remain as long as 10 years. There are many laws that apply to credit, creditors, the credit bureaus and consumers.

Since there are so many reasons why credit becomes damaged, including divorce, illness, injury, loss of income, or just plain lack of understanding of the credit system, there are also ways in which skilled professionals might be able to remove or change information depending on why, when and what happened with each account.



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