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Whether a bank will approve a mortgage for you hinges on your past dealings with debt

Presented by

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New Year's parties and the resolutions you made may already feel like a distant memory, but if you plan on buying a home later this year, one resolution you will want to keep is to organize your finances.

Any mortgage lender you go to will want to know how much of a risk you would be as a borrower. To determine where you stand in terms of creditworthiness, you can apply to see your credit score and report through equifax.ca or transunion.ca.

The three-digit score represents your likely risk to lenders. The higher the score the lower the risk.

"The risk ... is the likelihood that you're going to go 90 days, or worse, delinquent [on your loan] generally within a 12- to 24-month time frame," says Tom Reid, director of consumer solutions for TransUnion.ca.

The score is derived from your payment behaviour, debt levels and credit history.

"The two worst things you can do on your credit score are be at a high utilization on all your accounts and start missing payments," says Rob Regan-Pollock, senior consultant at Invis mortgage brokerage. "The system is viewing the risk that you're starting to crack and are no longer able to meet your obligations ... you're maxed and you're not making payments ... that's the beginning of the end."

It may not seem terribly important when you're spending your paycheque at restaurants and retailers, but it's when you want to buy a house that that all-important credit score is key to whether or not you will qualify for a mortgage.

"A lot of lenders are credit-score driven. They'll look at the credit score as a snapshot of somebody's credit. It's not always accurate but it's very important to keep your credit good," says Paula Roberts, a mortgage broker for Mortgage Intelligence in Unionville. "Typically [a score of] around 620 to 650 is acceptable, anything over 700 is very good, anything over 800 is excellent."

To achieve and maintain a good score, Ms. Roberts says it is crucial not to miss any payments; even if your minimum payment is only \$10 a month, make it.

Not all credit is created equal. Mr. Regan-Pollock says good use of cards from reputable banks will get you a higher score than a high-interest loan that has consolidated your debts.

So why all the hard work? A good credit score can help earn lower rates when you do borrow for a house.

"Lenders are relying heavily ... on credit scoring as a method of determining which borrowers are entitled to which programs," says Mr. Regan-Pollock. "It also has an impact on interest rates in certain cases, where lenders can ... offer a slightly better rate on preferential terms" for those with very good scores.

As a broker, Ms. Roberts says she can always get the best rates for clients who have a score of between 680 and 820 as they are considered to be good credit risks.

"But if someone is under 600, it's very difficult to give them credit and that's when the rates will start going up. Some lenders won't even consider an application [with a score] under 620," says Ms. Roberts.

At one time, applying to see your own credit rating would negatively affect your score, but this is no longer the case.

If you apply for a number of credit products at one time, and each business inquires after your score, that can negatively impact it, as it may seem your expenditures could get out of control. "You want to apply for credit in moderation," says Mr. Reid, while noting that "not all enquiries are indicative of somebody that may be a distressed borrower.

"[For] a mortgage ... [we recognize] it makes smart sense to shop for the best rate ... we take mortgage enquiries generally within a two-week time frame, and if there are multiple enquiries we consider that as a single enquiry."

Building up a decent credit score can take time.

"If [consumers] want to use their credit score to apply for a mortgage they need to [begin establishing a good rating] sooner than they think; it does sometimes take up to a year to optimize credit scores," says Mr. Reid.

During that year, advisors say, the best strategy is to not miss a payment, not to apply for new credit and to stay within 50% or less of your credit limit.