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## Cloud of secrecy surrounds new credit scores

Lenders look at a wider range of data (such as how often you switch jobs, phone lines) in determining risk.

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Banks and credit card issuers are digging deeper into people's lives, using powerful new tools.

Beyond the credit score, they are looking at where you live, how often you switch jobs or telephone lines, whether you get paid with direct deposit and other factors to decide whether you deserve a loan.

And unlike the well-known FICO score, which can be easily monitored online, most of the new scoring models have been developed solely for the use of lenders. As a result, would-be borrowers may be denied credit based on factors they never knew were relevant.

Federal regulations that go into effect in July will shine new light on these scores, by requiring lenders to disclose which ones they

used in denying someone a loan. But the underlying data and formulas used will remain a mystery.

"These scores are like black boxes," said Chi Chi Wu, a staff attorney with the National Consumer Law Center in Boston. "No one knows what the models are and exactly how they're being used, but the information can have a tremendous impact on people's lives."

Minneapolis-based Fair Isaac Corp., the creator of the FICO credit score, recently started marketing the "Deposit Behavior Score," which tracks how people manage their checking and savings accounts. Little is known about the score -- Fair Isaac declined to discuss it -- except that frequent overdrafts can drag it down.

Other new scoring metrics measure everything from property values to employment history, even the income levels and unemployment rate in particular ZIP codes, to determine a person's creditworthiness.

By some estimates, more than 100 credit scores -- most with obscure names and secret algorithms -- are in circulation. The traditional FICO score still matters, but lenders will often combine multiple scores.

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## Secret formulas

The scores are designed to help lenders do a better job of predicting borrower defaults, and possibly avoid a repeat of the subprime mortgage meltdown. However, consumer advocates say the secrecy of the new scores makes it difficult for borrowers to know why they have been denied credit. Mistakes often go undetected.

"How can you correct the accuracy of something when you don't even know what it is you need to correct?" asked Evan Hendricks, editor and publisher of the Privacy Times newsletter.

The new federal requirements that go into effect this summer will give people a clearer idea of what information was used in deciding their credit requests, but not the underlying data.

"That would be like getting Coca-Cola to disclose their secret formula," said John Ulzheimer, president of consumer education at [Smartcredit.com](http://Smartcredit.com)<sup>2</sup>, a credit information website. "It's not going to happen."

FICO remains the preeminent credit score. Its use skyrocketed during the credit boom because the score was easy to obtain -- all

the major credit bureaus provide FICO scores -- and relatively simple to understand. The three-digit score is largely based on payment history and the size of a person's debts.

About 25 percent of U.S. consumers -- 43.4 million Americans -- now have a FICO score of 599 or less, which categorizes them as risky borrowers, according to a recent estimate by Fair Isaac. That's an increase of 2.3 million Americans since 2008. The FICO score ranges from 300 to 850.

Lenders were caught by surprise during the credit meltdown in 2008, when even some customers with high FICO scores had trouble repaying their loans. That sent businesses scurrying for new ways to measure risk.

"No one just relies just on FICO anymore," said Ken Lin, chief executive officer of Credit Karma, which tracks credit score information.

## Deposit behavior scores

Fair Isaac was quick out of the gate with its Deposit Behavior Score. The firm declined to discuss the score and how it is used.

However, credit experts say such scoring usually measures a person's risk based on

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how they manage a checking account. People who overdraw their accounts frequently, or do not have their payroll checks deposited once or twice a month, may get lower deposit behavior scores.

For now, deposit behavior scoring is used primarily by banks to measure their own customers; the information is generally not shared among institutions. However, with bank profits squeezed by strict new regulatory limits on overdraft and debt-card fees, credit experts say the concept is likely to take hold and a generic "deposit behavior score" might someday be as ubiquitous as the FICO score.

"If you know that someone's bank account once a month goes from \$3,000 to \$100, you know that person may be skating on thin ice," said Carter Malloy, a credit analyst with Stephens Inc., an investment bank in Little Rock, Ark. "A traditional credit score may not capture that."

## Digging deeper

Many of the new scores analyze far more than a person's financial habits.

In 2008, ScoreLogix, a Delaware-based data analytics firm, began marketing a "Job

Security Score" to lenders. The score attempts to gauge a person's creditworthiness based on income stability. To do this, the firm measures individual borrowers based on hundreds of economic variables, down to employment and income levels in specific ZIP codes.

David Watral, director of business development at ScoreLogix, said the firm has generated millions of Job Security scores over the past few years, though he declined to reveal the data that go into them. "If I get too specific, then I put myself in a position of revealing trade secrets," he said.

Meanwhile, the major credit bureaus have been rolling out proprietary scores of their own. The three major bureaus, TransUnion, Experian and Equifax, have access to vast amounts of personal information from credit reports, including past and current addresses, employers and lines of credit.

Last summer, TransUnion unveiled a new score called "Credit Optics Plus." The score attempts to predict risk by tracking "stability" factors such as changes of address, telephone lines and other personal data. The score may benefit young people or recent immigrants who may have stable incomes and employment but thin credit histories,

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while possibly penalizing people who move a lot because of their jobs. Lenders are still testing the score.

Other firms create scores from information culled from public sources and the Internet. LexisNexis, a large data warehousing firm, uses homeownership, rent data, criminal convictions and property ownership data, among other factors, in creating its own credit risk score, known as Riskview Total Solutions.

"Consumers really have no clue how many times they're being scored," Ulzheimer said.

Terry Clemans, executive director of the National Credit Reporting Association, said consumers' best strategy is to pay their bills on time and monitor information in their credit reports. Despite the explosion of new formulas for calculating risk, he said, most lenders still use information from credit reports as the basis of their scoring models.

"People can't control the scoring metrics," Clemans said. "What they can control is making sure they the information that's being used is as complete and accurate as possible."

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