Top six credit rating myths

Modern life depends on our ability to borrow – but what we think contributes to that crucial credit rating and what actually matters are two very different things, as new research from CreditExpert, the credit monitoring and identity fraud protection service from Experian, shows.

With personal debt in the UK hitting an all-time high of £1.3 trillion, it's more important than ever to understand the factors that affect our ability to borrow – and how to manage credit sensibly.

Unfortunately, half of us don't fully understand what a credit rating is and how it affects our ability to borrow. A third of us have been refused a loan at some point and 40 per cent of this group don't know why.

This simple guide separates credit fact from fiction, so you know what really matters to lenders – and what you don't need to worry about.

Myth 1: Previous occupants at my home affect my credit rating

Pub bores often put this nonsense about and 71 per cent of you believe it – but it's completely untrue. The previous occupant of your house or flat could have been a millionaire or a bankrupt but that makes no difference to lenders at all.

What they are interested in is your ability to cope with a loan, so they will look at your individual circumstances. If you've recently moved, they will want to know your previous addresses, generally for the last three years, so that they can check that you really were living where you said you were. Again, if a hugely wealthy person or a pauper is now living where you used to, it won't affect your credit rating.

It is a good idea to register to vote, wherever you live. That's one of the factors lenders take into account.

Myth 2: Family and friends living at my address could harm your credit rating

Until a few years ago, lenders checked the credit reports of others living at your address. They could then take their position into account when deciding whether to offer you credit – and 63 per cent of people in the CreditExpert survey think that's still the case.

That no longer happens. Instead, you credit report contains a section listing your financial associates – people with whom you share a joint account, such as a joint mortgage.

Lenders will look at the credit reports of these people when they assess your creditworthiness. If your associate has a poor credit report, it could affect your chances of getting the deal you want – even if your own record is spotless.

To make sure that you don't get penalised, it's important to check that the list in your credit report is correct. It's also a good idea to get any financial associates to check their own report before you make a new application.

Myth 3: Credit reference agencies decide your credit rating

No, they don't – but 53 per cent of people think they do and also make the decision whether or not to lend to you.

In fact, credit reference agencies collate the information held in credit reports and hold it securely. This information includes the credit agreements you have, such as credit cards, loans and mortgages, your repayment history and whether you have any court judgements against you or have been made bankrupt.

Lenders use this information, along with your application form, to calculate a credit score – a number that represents the risk that you will not repay what you owe. Generally, the higher your score, the lower the risk you represent and the easier you'll find it to get a good deal.

It's important that your credit report is up to date and accurately reflects your circumstances, or your credit rating could be affected.

Myth 4: Your credit rating is poor because you're on a blacklist

There's no such thing as a credit blacklist, even though 41 per cent of you blame this if they're refused credit.

Red-lining – ruling out whole streets or estates – simply doesn't take place and your credit score does not take account of factors such as gender, religion, race or ethnic origin.

What does count to lenders is continuity, which is why your credit report shows years of your credit history and application forms often ask for your previous address. Lenders want to know how well you have managed your affairs over time, because that helps them to predict how you may behave in the future.

One interesting factor that they do note, however, is whether you’re on the electoral register. They use this public record of whether you have signed up to vote to check that you are who you say you are and live where you say you live, as a precaution against fraud. That’s why this information is included in your credit report.

Myth 5: You have only one credit rating

You can have many different credit ratings, depending on who you apply to, what you apply for and your circumstances at the time you apply. Still, 29 per cent of you think that you have a single score that applies to every type of credit, from a store card to a mortgage.

Every lender uses a slightly different equation to calculate a credit score – some also use different versions for different products. Your credit rating also changes when your circumstances change. For example, paying off a debt could improve your score, while missing a series of repayments could damage it.

Myth 6: Past debts don’t count

Unfortunately, they do, even if you’re financially fit today. In this area, you’re pretty realistic – just 12 per cent of us believe that an old debt doesn’t matter.

If you have missed repayments in the past, it stays on your credit report for 36 months. With a court judgement, the evidence is there for six years. A discharged bankruptcy stays on record for at least six years but a bankruptcy restrictions order is there for as long as 15 years. Lenders see these and mark you down, because they fear you may not honour your obligations.

Don't panic – you may be able to take remedial action by adding an explanation of the circumstances surrounding any problems to your credit report. For example, you might have missed a few repayments because of illness or an accident. Lenders will see this note and can take it into account.

• Check your Experian credit report for free, click here.