



Asset Funders Network



THE POWER OF CREDIT BUILDING

CREDIT BUILDING STRATEGIES FOR FUNDERS



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CREDIT BUILDERS ALLIANCE (CBA)

CBA is a nonprofit organization creating innovative solutions to help non-traditional financial and asset building institutions, serving low and moderate-income individuals, build client credit and financial access in order to grow their businesses and/or personal assets.

CREDITBUILDERSALLIANCE.ORG

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CREDIT BUILDING IMPROVES the outcomes grantmakers seek.

A good credit history is crucial in today's economy. Far more than just a number, a good credit score is a prerequisite for every day financial services like a low-cost credit card, a bank account or car loan. A good credit history can make the difference in accessing the affordable lending products necessary to go to college, buy a home, or start and grow a small business. Renting an apartment, paying for car insurance, signing up for utilities and even landing a job can also be affected by a person's credit history – or the absence of one.

For many low-income individuals with no or "thin credit files"¹, the ability to establish a good credit history is hampered by lack of access to affordable mainstream credit building financial products. Individuals with poor or thin credit often rely on payday loans to meet their credit needs. The high-cost of these loans, combined with the fact that on-time payments are not reported to the credit bureaus, prevent people from building credit and other assets, often across generations.

Without a strong credit history it is difficult, if not impossible, for households to get and stay ahead.

Growing numbers of grantmakers recognize the importance of credit building and its ability to improve the outcomes they seek for individuals and families. Their support has been critical to the emergence of credit building as a distinct, yet essential, component of programs designed to achieve economic mobility and security. However the need far outpaces the current funding base. Recruiting additional funders committed to credit building as a stepping stone to financial health and wellbeing is imperative.

The Power of Credit Building: Strategies for Funders provides grantmakers with an understanding of how credit building works and why it is important. It offers evidence of how credit building integrated across sectors directly improves opportunities for individuals, families and small businesses struggling to thrive and provides recommendations for grantmakers interested in incorporating credit building into their funding strategies.

FACTS

- **64 MILLION U.S. CONSUMERS** have insufficient or no credit history.²
- **MORE THAN HALF (56%) OF U.S. CONSUMERS HAVE LOW CREDIT SCORES**, ranging from 500-649.³
- **PEOPLE WITH LOW OR NO CREDIT SCORES** may pay \$200,000 more over a lifetime for financial products and services than those with good scores.⁴
- **THE AVERAGE CREDIT SCORE** of a Millennial in 2013 was 628, positioning them at the tipping point between higher cost and more affordable credit products.⁵



CREDIT BUILDING IS A POWERFUL TOOL to help individuals and small businesses take control of their financial lives.

WHAT IS CREDIT BUILDING?

Credit building is a powerful tool that helps individuals and small businesses take control of their financial lives and leads to asset building. It is the act of making on-time monthly payments on a financial product such as an installment loan or a credit card that is reported by the creditor to the major credit bureaus. Responsible credit building pairs reporting payments to the credit bureaus with relevant and timely credit education; opening and successfully managing financial products is key to building and maintaining a good credit history.

The term “credit building” is often confused with “credit repair.” Credit building is the only way someone with no or a thin credit profile is able to establish or reestablish a credit score. It is often an effective and faster first step for those with poor credit profiles who wish to boost their credit scores. Typically credit repair focuses on reducing current debt loads and paying off historical accounts in collections. Comprehensive credit building programming

may encompass credit repair as a complimentary and essential component to resolve errors or deal with debt.

In just six months, on-time payments reported to the credit bureaus on an installment loan as small as \$100 can help an individual with a low credit score increase his or her score by an average of 35 points and move an individual with no credit score to a prime credit score.⁶

Building credit with a credit card may afford households with even greater benefits. If the balance can be paid off in full at the end of each month, savvy credit card users have access to an interest free loan for up to 30 days. And a revolving credit account in good standing stays on a credit report indefinitely. For low-income families, this can be a powerful tool not only for credit building, but for smoothing income fluctuations or weathering financial emergencies.

WHAT IS “GOOD”?*

| RANGE | FIGO SCORE ⁷ | CONSUMER IMPACT |
|----------------------------|-------------------------|--|
| SUB-PRIME (POOR/LOW) | UNDER 620 | NO ACCESS OR UNFAVORABLE RATES AND TERMS |
| PRIME (FAIR/GOOD) | 620 – 780 | REASONABLE OR GOOD RATES AND TERMS |
| SUPER PRIME (EXCELLENT) | 780+ | BETTER OR BEST RATES AND TERMS |

*LENDER THRESHOLDS VARY



CREDIT BUILDING REQUIRES the existence of at least one positive trade line — or credit account — on an individual’s credit report.

CREDIT BUILDING PROMOTES FINANCIAL CAPABILITY

A \$300 car repair may mean that a single mother cannot get her children to daycare or herself to work on time. This quickly results in lost wages and potential unemployment. When she takes out a payday loan to fix the car or pay late bills, she is pushed into an unsustainable cycle of debt, often paying two or three times the amount of the original loan in fees alone before it is fully repaid. This exacerbates her family’s financial instability and creates overwhelming psychological and physical stress. In contrast, the same single mother can weather this short-term financial setback to her long-term advantage with access to a credit card with a reasonable interest rate. She could repay that \$300 as her cash flow permits, paying the full balance or even the minimum monthly payment on time. If managed well, she will save hundreds of dollars in interest while also building her credit. Seeing the impact of her financial decisions reflected on her credit report and the corresponding increase to her credit score is empowering and reinforces her resolve to prioritize her positive payment behavior in pursuit of future goals.

CREDIT BUILDING PRODUCTS

Credit building requires the existence of at least one positive trade line — or credit account — on an individual’s credit report.⁸ To build credit, that credit account must be both *open* and *active*.

Lenders report both installment (e.g. car loans, student loans, mortgages, etc.) and revolving (e.g. credit cards or lines of credit) credit to the credit bureaus. In order to build credit, installment loans must carry a balance and require a monthly payment. While paying off debt is a good thing, once paid in full a loan is no longer active and will not continue to build credit. Revolving credit, on the other hand, offers an indefinite credit building solution as long as it is actively used; at least once every six months and ideally monthly. An outstanding balance on the credit card is not required to build credit.

“Credit Builder” loans and secured credit cards are valuable stepping stones to mainstream financial products for those seeking to establish or rehabilitate their credit histories and improve their scores – and are often considered less risky by lenders. More and more nonprofit lenders and credit unions offer small-dollar Credit Builder loans that are “secured” by the loan proceeds themselves and released to the borrower upon repayment. In the case of a secured credit card, which may also be offered by a credit union or a bank, individuals deposit funds in a bank account as collateral.

In addition to traditional financial products, alternative forms of positive “credit data”, such as utility and telecom payments, reported to the credit bureaus help individuals and entrepreneurs build credit. Research indicates that adding this data enables 74% of those with no or thin credit files to obtain credit scores, notably impacting Latinos, African Americans, youth between 18 and 25, and seniors.⁹ Furnished to the credit bureaus responsibly, alternative credit data reporting offers millions of Americans the chance to build credit without taking on additional debt or incurring the burden — and risk of not being able to pay — an additional monthly expense.¹⁰



CREDIT IS A MEASURE of one's financial health and increasingly influences lenders and others on who they decide to do business with and under what terms and conditions.

CREDIT REPORT AND SCORE: KEY TOOLS FOR MEASURING SUCCESS

While a newly established or improved credit score is the most simple metric by which to measure credit building success, a credit report is a more comprehensive tool that provides valuable insight into one's financial history, knowledge and behavior. It is a unique, longitudinal instrument for objectively measuring key financial indicators beyond just the credit score.

For those with credit histories, credit reports are excellent tools for understanding a person's historical credit payment patterns, including whether they have resulted in civil judgments or bankruptcy. They also reflect which financial institutions and financial products individuals currently rely on and why (e.g. a car loan offered by a local credit union), and help inform critical budget decisions based on existing debt obligations.

If a person has no credit history or a thin file with no active credit accounts in good standing, the lack of information

OVER 95% OF NONPROFITS SURVEYED AGREE THAT CREDIT REPORTS:

- Are a valuable tool for understanding and addressing a client's credit profile, challenges, and opportunities;
- Improve the ability to measure and track a client's credit and financial progress over time;
- Engage client participation in a tangible way that leads to improved credit and other financial assets.¹¹

on a credit report is an equally powerful cue. It provides practitioners with the perfect opportunity to introduce credit building and leverage ongoing credit building success to help clients track their progress along the path to greater financial stability and security in real-time. As individuals begin to build credit, credit reports reviewed at regular intervals offer a series of teachable moments that can motivate individuals to continue to improve financial behavior and achieve asset building goals.

THE POWER OF CREDIT: BENEFITS TO INDIVIDUALS AND FAMILIES

In today's economy, a good credit history is a financial asset. Distinct from debt – which is a liability defined by what we owe – credit is a measure of our financial health and increasingly influences lenders and others on who they decide to do business with and under what terms and conditions. Having good credit benefits individuals and their families in the following ways:

INCREASES CASH FLOW AND CREATES OPPORTUNITIES TO SAVE

A good credit score can save a person thousands of dollars over a lifetime. A good credit history offers individuals and families better loan terms and reduces or eliminates costly deposits for goods and services, resulting in a sustainable and systematic way to save money.¹² For example, an individual with a FICO score of:

- 720 will pay \$4,020 less for a \$10,000, 5-year auto loan – saving \$67 a month – compared to someone with a score of 500.
- 760 will pay \$69,280 less for a \$100,000, 30-year mortgage – saving \$192 a month – compared to someone with a score of 620.¹³



A GOOD CREDIT HISTORY
offers individuals and families
better loan terms and reduces
or eliminates costly deposits
for goods and services.

IMPROVES EMPLOYMENT AND HOUSING OPTIONS

Most people require some minimum level of stability – a place to live and an income – before they can begin to sustainably build assets. Credit building is critical in successfully laying that groundwork.

- An estimated 1 in 4 unemployed Americans are required to go through a credit check when applying for a job with 1 in 10 denied a job due to negative information on their credit report.¹⁴
- Many landlords check prospective tenants' credit report for previous housing collections items and other indicators of how responsible the applicant is at managing money. Those with good credit histories therefore have more – and often better – rental options.¹⁵

BUFFERS ECONOMIC SHOCKS AND SMOOTHS INCOME

Many American households, particularly those that are low-income, require credit to weather economic shocks such as unexpected expenses, a sudden job loss or to stretch and smooth income to meet their basic needs. Consumers without a good credit history may have to turn to high-cost payday lenders to obtain credit.

- 5.5% of adults nationwide have used payday loans in the past five years, spending approximately \$7.4 billion annually to meet their small dollar, short-term credit needs.²¹
- Many consumers rely on payday loans to cover ordinary living expenses – not just emergency situations — on a regular basis throughout the year.²²

IMPROVES ACCESS TO HIGH-QUALITY CREDIT PRODUCTS

While a good credit history and score can mean lower fees and interest, a thin credit history — or none at all — can make it difficult to qualify for high-quality, more affordable credit products from traditional lenders to meet short-term financial needs or take advantage of opportunities to build assets by purchasing a home, earning a college degree or starting a business.

- In 2009 Fannie Mae raised its minimum credit score for conventional loans from 580 to 620. Even with a 20% down payment, a mortgage applicant can be rejected with a score below 620.¹⁶
- Many students rely on private loans to support or supplement their education. It is difficult to obtain a private student loan with a FICO score below 650.¹⁷

EXPANDS OPPORTUNITIES FOR SMALL BUSINESS GROWTH

Small business ownership offers a vital pathway to asset building.¹⁸

- Lenders generally require a personal credit history, and sometimes a business credit history, before approving a small business loan.¹⁹
- The number of nonprofit microenterprise and small business lenders reporting their underserved borrowers' loans to the credit bureaus in order to help them build credit and access mainstream credit products almost doubled between 2008 and 2011.²⁰



INTEGRATING CREDIT BUILDING STRATEGIES into existing programs creates better outcomes for low-income consumers.

FUNDERS TURN TO CREDIT BUILDING TO GET RESULTS

Growing numbers of grantmakers and their nonprofit partners recognize that integrating credit building strategies into existing programs and services creates better outcomes – especially among low-income consumers. For example, a recent survey of nonprofit lenders revealed that over 95% agree that reporting their borrowers' loans to the credit bureaus improves their clients' credit scores and increases their access to safe and affordable mainstream credit products. Nonprofits also note that reporting strengthens the quality of their loan portfolios by providing clients with an additional positive incentive to make their payments on-time.²³

Grantmakers committed to credit building programs are demonstrating that access to responsible credit products, combined with financial education, helps level the playing field and makes long-term asset goals more attainable for all Americans. Some early investors in this work include the Citi Foundation, Annie E. Casey Foundation, Bank of America Foundation, CapitalOne Foundation, Charles Stewart Mott Foundation, Experian, Ford Foundation, JPMorgan Chase, Levi Strauss Foundation, The MacArthur Foundation, MetLife Foundation, and the W.K. Kellogg Foundation. However, more funding in this area is required. The following are examples of how foundations are investing in credit building across sectors to help strengthen outcomes for individuals and families.

JOBS ARE NOT ENOUGH

Getting a job is a major first step towards achieving financial stability. But for many low-income workers, wages alone do not cover basic living expenses such as rent, utilities, daycare and even food. Making the link between

financial stability and good credit, the Local Initiatives Support Corporation (LISC) in Chicago added a credit building product to their network of Financial Opportunity Centers (FOCs) in 2010 with funding from numerous national and local foundations. In addition to employment, financial and income support services, the FOCs now offer a credit building loan paired with a matched savings account, called Twin Accounts.

Participants in Twin Accounts are issued a 12-month, \$300 loan, the proceeds of which are immediately transferred into a "locked" savings account where they remain until the loan is paid off. To incentivize the most important element of credit building, LISC Chicago matches each loan payment – dollar for dollar – as long as the payment gets to the lender on time. Twin Accounts costs no more than an IDA program, with funding covering financial counselor salaries, counselor training on credit building, and match funds for Twin Accounts customers.

Successful participants end the 12-month program with \$300 in savings, and up to \$300 in match. Within six months participants who are "unscored" at program entry typically generate FICO scores in the high 600s. Those with low scores at program entry see an average increase of 30-60 points. To date, 63% of all Twin Accounts participants have made ALL of their payments on time, and 83% have successfully paid off the loan (and therefore saved \$300) in 12 months. More importantly, Twin Accounts participants are using improved credit scores to get better jobs, move to higher quality apartments, and decrease expenses through use of better-priced financial products and services.²⁴



GRANTMAKERS COMMITTED TO CREDIT BUILDING demonstrate that access to responsible credit products makes long-term asset goals more attainable for all Americans.

MICROENTERPRISE AND SMALL BUSINESS DEVELOPMENT

Self-employment or small business development is an important asset building option for many Americans, particularly as the availability of living-wage jobs have dwindled over the years.²⁵ Nonprofit microlenders increasingly see the negative effects of low or no credit scores on the entrepreneurs they serve as they struggle to obtain loans to start or grow their businesses.²⁶ These lenders act as a credit – and credit building – bridge between those entrepreneurs and traditional financial institutions.

Based in St. Louis, Missouri, Justine PETERSEN (JP) has been offering microenterprise development, home ownership services, and financial coaching to low- to moderate-income individuals since 1997. With support from Citi, Bank of America and others, JP is a credit building pioneer — simultaneously offering credit building as a standalone opportunity and integrating it strategically into its asset building efforts.

Success at JP is multifaceted. On average, clients with no credit score reach 680 and those with low scores see a 50 point increase in six months. Entrepreneurs in particular leverage improved credit to start and grow their businesses through better rates and terms with suppliers and landlords, and ultimately access to mainstream small business loans leading to increased income and net worth.

JP also uses its deep experience in the credit building field to support other nonprofits and practitioners working to help their clients build credit.²⁷

ECONOMIC JUSTICE FOR DOMESTIC VIOLENCE SURVIVORS

Women who experience domestic violence must often rebuild their financial lives. Establishing or rebuilding their credit is a critical milestone on that journey toward independence. To address the financial needs of survivors, the Allstate Foundation offers grants to state and local domestic violence coalitions to provide financial education, job readiness and training, individual development accounts (IDA) and microloans. A number of domestic violence groups have creatively leveraged these activities by incorporating credit building to improve outcomes.

Since 2009, the Kentucky Domestic Violence Association's (KDVA) Economic Justice Project provides services and programs that work with survivors to help them gain economic self-sufficiency. One way they do this is by offering no-interest microloans to their IDA participants. The loans, which are secured with the borrower's IDA savings, are designed to assist survivors in meeting immediate needs while building positive credit.

Survivors participating in the program leverage increased credit scores (many by 50 to 100 points) and IDA savings to obtain mainstream financial products such as affordable car loans, small business loans or home mortgages needed to reestablish their lives.

SETTING THE STAGE FOR YOUTH

Many young people transition to adulthood without having learned the importance of a good credit history or how to build one. They discover this when they apply for – and are denied – a job, apartment, cell phone service, bank account, car or student loan. For those who are able



EMBEDDING CREDIT BUILDING into social service, workforce development, health and education programs, helps effect positive behavior change.

to access financial products, many may not understand the consequences of late payments or overspending on their emerging credit reports and scores.

Mission SF Community Financial Center (Mission SF) — a San Francisco-based nonprofit — works to position youth and young adults to take control of their finances. Using their “Pathways” model, Mission SF financial counselors have engaged hundreds of young adults on community college campuses and in workforce settings — referring them to a local credit union partner to open bank accounts, access loans that help build credit, and take other steps towards financial security. Program participants not only establish scores in the high 600s or move from subprime to prime in just six months, they are able to save money, secure housing, access employment, and go to school.

Last fall, Mission SF was one of only three sites across the country awarded a grant through the Financial Capability Partnership Initiative funded by the Kresge Foundation through the National Federation of Community Development Credit Unions and the Center for Financial Services Innovation. With this funding Mission SF is piloting “MY Path to Credit,” a model that integrates a credit building loan product paired with one-on-one coaching into a workforce site for youth ages 18-24. With over 60% of participants lacking any credit history at all, MY Path to Credit will position them to move into their own apartments, get jobs, and further their educations.

FROM PAYDAY TO MAINSTREAM

Many low-income people with no, thin or poor credit histories lack the savings, a social safety net or other assets to weather financial shocks or smooth income without relying on predatory lenders. With grant funding to cover

startup costs and a Program Related Investment (PRI) of loan capital from the Meyer Memorial Trust, Innovative Changes (IC\$) opened its doors in 2010 to provide small-dollar, short-term consumer loans, financial education and credit building programs as a responsible alternative in Oregon.

IC\$’s loans are combined with financial education to help clients, 70% of whom are low-income women and mostly single heads of households, set the stage for financial stability. In addition to building credit, IC\$ loans help people better align income with expenses, catch up on past bills and taxes, cover housing and medical needs, pay off higher-cost debt and more.

Within six months borrowers on average, establish a prime score of 670 or increase an existing low score by 42 points, which can move them from subprime to prime. As a result, IC\$ has been able to help clients refinance car loan interest rates, qualify for affordable mortgages and graduate into low-interest credit cards and new bank accounts through partnerships with local financial institutions.

INNOVATIONS IN ALTERNATIVE CREDIT DATA REPORTING

Currently, many companies and landlords report poor payment history to the credit bureaus through the collection process. Far fewer, however, reward positive payment behavior by reporting on-time payments. This can lead to a negatively skewed assessment of the credit risk posed by many individuals and entrepreneurs, particularly those with low- and modest-incomes who lack other viable opportunities to build credit.



GOOD CREDIT MEANS
greater financial stability,
savings and asset building
opportunities.

As affordable housing providers (AHPs) across the country increasingly embrace asset building as a strategy to improve their residents' outcomes, several are exploring a new and innovative model of credit building by reporting rental payments. A 2013 survey of more than 300 affordable housing residents revealed that 96% understand the importance of good credit and 97% believe that having their rental payments reported is a good way to build their credit.

Over the last two years, the Citi Foundation and Credit Builders Alliance (CBA), a national nonprofit network of almost 400 community based organizations engaged in credit building, have catalyzed interest in and laid the foundation for rent reporting as a valuable and viable credit building opportunity for residents of nonprofit and public AHPs. In 2014 CBA is implementing its *Power of Rent Reporting Pilot* with eight AHPs. Each AHP is committed to leveraging the rent reporting opportunity as a financial capability tool for their tenants by pairing it with credit education then measuring and documenting the results.

INTEGRATING INTO THE FINANCIAL MAINSTREAM

Those excluded from America's economic system have limited prospects. Peer lending circles have long been an informal way for family, friends and neighbors – particularly in immigrant communities – to help each other gain access to capital they otherwise could not get from traditional financial sources. Through its social loan model, Mission Asset Fund (MAF) has formalized peer lending circles to help financially excluded communities meet short term credit needs and build credit while also becoming visible, active, and successful participants in the U.S. financial mainstream.

Based in San Francisco, MAF has received support from numerous grantmakers across the country. On average, lending circle participants leverage the funds and support they receive to increase their credit scores by 168 points²⁸ and to reduce their debt burdens by over \$1000. Many go on to start small businesses, purchase homes, open bank accounts and even become American citizens.

“**BEING POOR ISN'T THE ENTIRE PROBLEM. IT'S HAVING BAD - OR NO - CREDIT. MANY LOW-INCOME PEOPLE ARE GOOD MONEY MANAGERS - THEY JUST DON'T HAVE THE FINANCIAL PRODUCTS THAT REPORT TO CREDIT AGENCIES.”**

—RICKI LOWITZ, DIRECTOR,
ECONOMIC OPPORTUNITIES, LISC CHICAGO

CREDIT BUILDING RECOMMENDATIONS FOR FUNDERS

Successful credit building depends in large part on the support of grantmakers to invest in best practices, improved outcomes and innovative opportunities. The following strategies are recommended to grantmakers in advancing their funding goals through credit building:

- ◆ **BUILD ORGANIZATIONAL AND STAFF CAPACITY.**

Reporting loan repayment behavior to the credit bureaus and pulling credit reports as a financial coaching tool requires specific knowledge, skills, and technology. Investments in staff training, skills-building, and appropriate reporting technology as well as underwriting the costs associated with reporting loan data and pulling credit reports from the credit bureaus are all necessary elements in ensuring sustainable, compliant, and effective credit building efforts.

- ◆ **EXPAND CREDIT BUILDING ACROSS SECTORS.**

Embedding credit building beyond traditional asset building programming into social service, workforce development, health and education programs can help effect positive behavior change. Funders can encourage their grantees to incorporate credit building into their work and nurture its integration by including credit building as a fundable activity in their guidelines and embedding credit building metrics such as improved credit score, access to affordable mainstream financial products, savings, and decreased financial stress into grant outcomes.

- ◆ **PROMOTE COLLABORATION.** As credit building gains more and more traction, funders can play an important role in supporting and encouraging smart community-based collaboration by funding activities and seeking outcomes that involve: 1) Cross referrals for nonprofits to join forces to help clients by bringing together their respective areas of expertise and 2) Relationship building between nonprofits and mainstream financial institutions. While many practitioners in the growing and diverse credit building ranks are lenders who can leverage their own financial products by reporting directly to the credit bureaus, many more rely on outside partners to facilitate access to credit for their clients. In some cases, nonprofits do both to maximize impact and ensure sustainable credit building beyond the timeframe of a specific intervention.

- ◆ **NURTURE PEER LEARNING.** Professional peer learning is critical to the further development of the credit building field. By supporting practitioner Credit Building Learning Communities at the national or community level, grantmakers can help foster an environment of commitment to continual improvement of services and replication of best practices.

- ◆ **FOSTER KNOWLEDGE AND INNOVATION.**

The credit reporting industry has changed dramatically over the past 10 years, with more changes likely in the next decade. Investments in research and pilots of different credit reporting, education products and models is important to ensure those who need it most, benefit from these changes.

- ◆ **SUPPORT EVALUATION.** Many nonprofits struggle to develop objective, reliable measures and data on the outcomes associated with financial education and lending. Investing in the development of standardized credit building outcomes beyond credit scores and impact indicators will help ensure successful programs, both for clients and nonprofits²⁹. Funding for more rigorous evaluation is essential to fully understand the long-term implications and impact of credit building on people's financial health and upward mobility.

- ◆ **EXPLORE POLICY OPPORTUNITIES.** Funders' support of credit building policies and emerging innovations in the field, such as rental payment reporting, will better ensure that low- and moderate-income individuals and entrepreneurs are able to successfully participate in the modern credit system.

“CREDIT IS THE PASSPORT
TO THE NEW ECONOMY.”

—ANDREA LEVERE, PRESIDENT,
CFED, WASHINGTON, D.C.



GRANTMAKERS RECOGNIZE that credit building is integral to putting individuals on a path of economic mobility and security.

CONCLUSION

A good credit history is not only an asset, it is the means to greater and more sustainable financial stability, savings and asset building opportunities.

As credit reports and scores are used more widely by creditors, employers and other businesses, grantmakers are recognizing the connection between consumers' credit profiles and the opportunities available to them. Over the last five years the nonprofit community has begun to embrace *credit building* as integral to helping low- and moderate-income and other underserved constituents build and sustain financial assets.

Funders and practitioners must continue to leverage their resources to support responsible credit building programs and policies that combine access to safe, affordable financial products with skilled and relevant financial education. In this way, they create ideal conditions for individuals and families to build credit and assets.

KEY CREDIT BUILDING TERMS

CREDIT. The ability of a customer to obtain goods or services before payment, based on the trust that payment will be made in the future.

CREDIT BUILDER LOAN. A loan that helps build/establish a credit history; generally, these loans are small, help build credit relationships with community lenders, are reported to the credit bureaus, and replace asset-stripping/costly alternatives (i.e. payday loans).

CREDIT BUILDING. The act of making on-time monthly payments on a financial product such as an installment loan or a credit card that is reported by the creditor to the major credit bureaus.

CREDIT BUREAU. A credit-reporting agency that is a clearing-house for information on the credit rating of individuals or firms – often called a consumer reporting agency. The three largest credit bureaus in the U.S. are Equifax, Experian, and TransUnion.

CREDIT HISTORY. A record of transactions involving the use of credit. If you do not have a credit history you will not have a credit report

CREDIT REPAIR. Traditionally, counseling focused on developing debt management plans.

CREDIT REPORT. A record of a consumer's credit history.

CREDIT SCORE. A number that summarizes your credit risk. It generally is used by lenders to assess the odds that you will become delinquent in repaying your debt within the next two years, and is based on a snapshot of your credit report at a particular point in time.

CREDIT TYPE. Refers to the type of credit agreement made with a creditor; for example, a revolving account or installment loan.

FICO SCORE. FICO is an acronym for the Fair Isaac Corporation, the creators of the FICO score. The FICO score range is between 300 and 850. In general, a FICO score above 650 indicates that the individual has a very good credit history. Individuals with scores below 620 may find it more difficult to obtain financing at a favorable rate.

INDIVIDUAL DEVELOPMENT ACCOUNT (IDA). A savings account for lower income individuals where savings are matched by private or public funds; they are typically used for a specific purpose such as education, purchasing a first home, or starting a business.

INSTALLMENT CREDIT. A credit account in which the debt is divided into amounts to be paid successively at specified intervals.

LINE OF CREDIT. An arrangement between a financial institu-

tion, usually between a bank and a customer, that establishes a maximum loan balance that the bank will permit the borrower to maintain. The borrower can draw down on the line of credit at any time, as long as he or she does not exceed the maximum set in the agreement.

MICROENTERPRISE. A small business that employs a small number of employees. A microenterprise will usually operate with fewer than 5 people and is started with a small amount of capital. Most microenterprises specialize in providing goods or services for their local areas.

PAYDAY LOAN. A short-term loan borrowed at a very high rate of interest against the borrower's next paycheck. These loans are also called cash advance loans or check advance loans.

PREDATORY LENDING. Unscrupulous actions carried out by a lender to entice, induce and/or assist a borrower in taking a loan that carries high fees, a high interest rate, strips the borrower of equity, or places the borrower in a lower credit rated loan to the benefit of the lender.

REVOLVING ACCOUNT OR REVOLVING LINE OF CREDIT. Credit that is available up to a predetermined maximum limit so long as a customer makes regular payments.

SECURED CREDIT CARD. An alternative to a credit card, the secured card requires a cash deposit which becomes the unsecured credit line for that account. Funds are "secured" in a savings account to be used for payment in case you are unable to make your payment. Typically, the credit limit is generally the amount in the savings account and most range from \$300-\$1,000. For example, if you place \$500 in your account, you will have a \$500 credit limit.

SECURED CONSUMER LOAN. a loan in which the borrower pledges some asset (e.g. a car or property) as collateral for the loan.

SUBPRIME CREDIT. General term for borrowers of subprime debt, or loans made to people with less-than-perfect credit or short credit histories. Subprime credit includes the original borrowing itself, as well as any derivative products such as securitizations that are based on subprime loans and then sold to investors in the secondary markets.

TRADE LINE. An account listed on a credit report. Each separate account is a different trade line. A trade line describes the consumer's account status and activity. Trade line information includes names of companies where the applicant has accounts, dates accounts were opened, credit limits, types of accounts, balances owed and payment histories.

UNSECURED CREDIT. A loan that is issued and supported only by the borrower's creditworthiness, rather than by some sort of collateral; unsecured credit loans are sometimes called signature loans.

ENDNOTES

- 1** Individuals with no credit history will not be able to generate a credit report or a credit score. An individual with a “thin credit file” will have a credit report but may not be able to generate a credit score due to insufficient credit history or not enough credit accounts. In both cases individuals are seen as credit risky and inexperienced with managing credit because they have a limited credit history.
- 2** Experian Information Solutions.
- 3** Brooks, J., Wiedrich, K., Sims, Jr., L., & Medina, J. *Treading Water in the Deep End, Findings from the 2014 Assets and Opportunities Scorecard* (CFED, January 2014). Different credit reporting agencies use different credit scores, which may use slightly different credit score scales. In all cases the higher the score the better. The credit score source for this data point is TransUnion’s TransRisk score, which ranges from 300-850.
- 4** Liz Weston, “Lifetime Cost of Bad Credit: \$201,712.” *MSN Money*, October 13, 2011, <http://money.msn.com/credit-rating/lifetime-cost-of-bad-credit-201712-dollars-weston.aspx?page=0>.
- 5** Experian National Score Index, 2013 (<http://www.experian.com/live-credit-smart/state-of-credit-2013.html>). The credit score source for this data point is the VantageScore 3.0, which ranges from 300-850.
- 6** CBA Member Survey, July 2013.
- 7** FICO scores are the most widely known and used and range from 300-850. Different lenders and businesses assign different underwriting score floors to determine what is considered subprime, prime or super-prime.
- 8** The best practice in credit building is to maintain three active credit accounts (ideally a mix of installment and revolving credit), making on-time payments on those accounts every month for at least six months.
- 9** Policy and Economic Research Council and the Brookings Institution, *Give Credit Where Credit is Due: Increasing Access to Affordable Mainstream Credit* (2006).
- 10** In June 2013, Congressmen Mike Fitzpatrick and Keith Ellison introduced the bipartisan *Credit Access and Inclusion Act* [HR 2538], still pending in the House, that would allow landlords and utility and telecom companies to report all on-time payment data to credit reporting agencies.
- 11** CBA Member Survey, July 2013.
- 12** According to the Corporation for Enterprise Development’s (CFED) Household Financial Security Framework, in order to save, household income must exceed expenses necessary to meet basic needs and pay down debt. Like credit building, savings is a critical strategy for all Americans and an important step along the asset building continuum, particularly for those with low- and modest incomes (http://cfed.org/assets/pdfs/CFED_One_Pager.pdf).
- 13** Data derived from MyFICO.com.
- 14** Traub, Amy, *Discredited: How Employment Credit Checks Keep Qualified Workers out of a Job* (Demos. 2013). Many employers review credit reports as part of the job application process in an effort to assess a candidate’s stability and the likelihood that he or she may be dishonest or commit fraud. However there is little evidence that credit profiles are reliable indicators of a job applicant’s ability to perform a job, particularly for those whose credit histories suffered due to a medical situation or a period of prolonged unemployment.
- 15** <http://www.tenantsunion.org/en/rights/tenant-screening>.
- 16** <http://www.homebuyinginstitute.com/news/fha-credit-requirements-updated-506/>.
- 17** *Private Student Loans*, Report to the Senate Committee on Banking, Housing, and Urban Affairs, the Senate Committee on Health, Education, Labor, and Pensions, the House of Representatives Committee on Financial Services, and the House of Representatives Committee on Education and the Workforce (Consumer Financial Protection Bureau, August 2012). According to the CFPB, outstanding private student loan debt totals approximately \$150 billion.
- 18** Klein, J. and Fischer, L, *Building Assets Through Microbusiness* (FIELD, The Aspen Institute, 2014).
- 19** <http://www.sba.gov/community/blogs/6-step-guide-how-get-business-loan>.
- 20** Data from FY2008 and FY2011 U.S. Microenterprise Census, FIELD at the Aspen Institute. In FY 2011, 207 organizations completed the Census; 122 were direct lenders.
- 21** Urahn, S., Plunkett, T., Bourke, N., Horowitz, A., Lake, W. & Roche, T., *Payday Lending in America: Policy Solutions* (The PEW Charitable Trusts, October 2013).
- 22** Urahn, S., Plunkett, T., Bourke, N., Horowitz, A., Lake, W. & Roche, T, *Payday Lending in America: Who Borrows, Where They Borrow, and Why* (The PEW Charitable Trusts, July 2012).
- 23** CBA Member Survey, July 2013.
- 24** To make sure participants can continue building credit beyond the 12-month loan term, LISC limits the use of match funds to one option: the opening of a secured credit card. LISC will soon add a second year on to Twin Accounts – designed to support credit card use. LISC will provide \$25 per month, for each month the client brings a statement to the FOC that shows the person 1) used the card during the billing period, and 2) ended the term of the billing period with a balance of 30% or less of the credit limit.
- 25** Klein, J. and Fischer, L, *Building Assets Through Microbusiness* (FIELD, The Aspen Institute, 2014).
- 26** Klein, J., Gomez, L. & Edgcomb, E., *Asset Building Through Credit Pilot* (FIELD, The Aspen Institute, 2013).
- 27** JP is the primary service provider for LISC’s Twin Accounts and also served as the intermediary in the Asset Building through Credit Building(ABC) Program – a collaborative initiative funded by the Citi Foundation and facilitated by FIELD at the Aspen Institute to pilot and measure the use of secured credit cards as a credit building tool for low- and modest-income entrepreneurs.
- 28** To understand the way this 168 credit score increase total is calculated as well as other compelling social loan impact data, see the reports produced by San Francisco State University’s César E. Chávez Institute detailing the impact and replication of MAF’s Lending Circles at <http://missionassetfund.org/impact/program-outcomes>.
- 29** For more information about the range and diversity of indicators used by many nonprofits that offer credit building see <http://credit-buildersalliance.org/whats-new/resources/how-cba-member-organizations-are-measuring-credit-building-success>.

ASSET FUNDERS NETWORK (AFN)

AFN provides grant makers with valuable opportunities to learn and connect. From veteran practitioners to newcomers with fresh ideas, AFN provides a safe and neutral forum for candid conversations among peers with similar and opposing views. Our programming increases the capacity of our members to more effectively promote economic opportunity and security and make better strategic funding decisions.

Formed in 2005, AFN increases the capacity of its foundation and grantmaker members to effectively promote economic security by supporting efforts that help low- and moderate-income individuals build and protect assets.

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