

Building **Wealth**

In the Classroom

Lesson 8

Build Credit—Understanding Credit Reports and Scores



Federal Reserve
Bank of Dallas



Instructional objectives

You will:

- Distinguish between credit report and credit score.
- Describe the importance of monitoring credit reports.
- Describe how to access and interpret a sample credit report and score.
- Describe how to build credit.
- Discuss how character, capacity and collateral can impact rating and the ability to obtain credit.

**Are there similar characteristics between
grade-point average (GPA) and a credit score?**

Which GPA score is better?

A

Cheyenne

High school student

GPA: 3.8

B

Noah

High school student

GPA: 2.7

**Cheyenne's GPA of 3.8
is higher than Noah's 2.7.**



Cheyenne

High school student

GPA: 3.8

Which credit score is better?

A

Olivia

College student

Credit score: 600

B

Luis

College student

Credit score: 750

**Luis' credit score of 750
is higher than Olivia's 600.**



Luis

College student

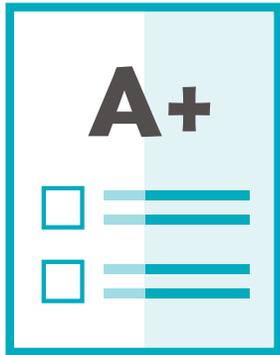
Credit score: 750

Similarities between GPA and credit score



- The higher the score, the better.
- The score is for one person.

Similarities between GPA and credit score



GPA is one piece of information colleges look at when determining acceptance.



Credit score is one piece of information creditors look at to determine a borrower's ability and willingness to repay a loan.

What is a credit score?

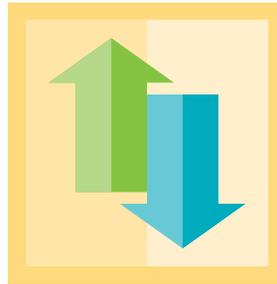


Credit score is a number that predicts the likelihood that a debt will be repaid on time.

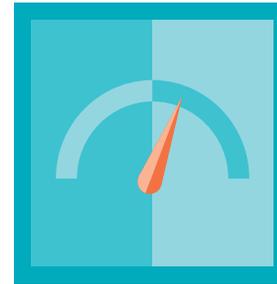
Credit score facts



Credit scores are derived from credit reports.

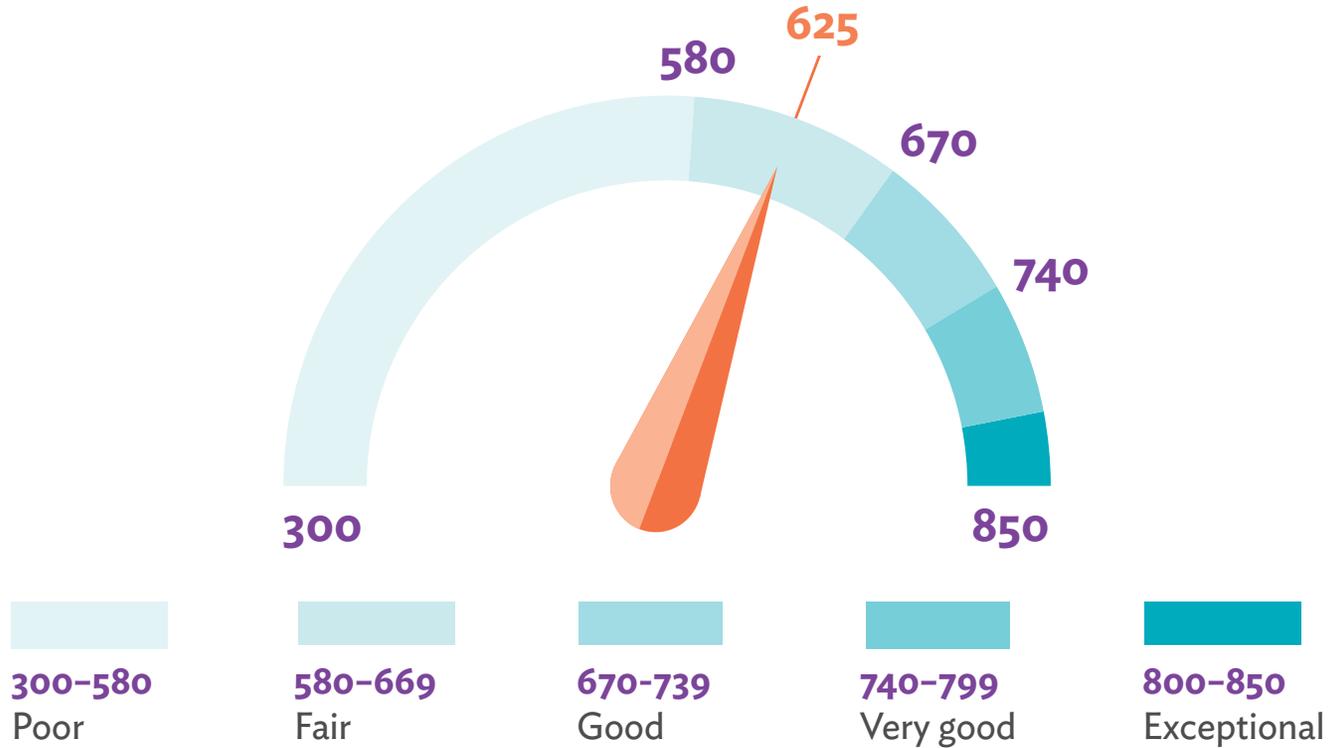


The higher your score, the less risk you represent.



The most widely used credit score is a FICO score.

FICO Credit Score Range



How credit scores are calculated



Payment history



Amount of debt



Length of
credit history



Credit mix



New credit

What else do lenders look at?



Credit reports



Character



Capacity



Collateral



Credit Reports

What's included?

What is a credit report?

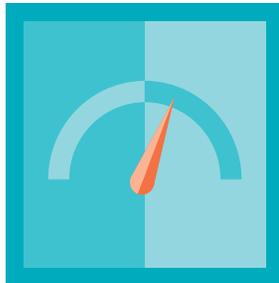


A credit report is a statement that has information about your credit activity and current credit situation.

A credit report shows your:

- Bill payment history.
- Current debt.
- Other financial information.

What's not included in your credit report?



Credit reports do not include your credit score.

Credit reporting agencies use your credit report to calculate your credit score.

How are credit reports used?

Credit reports help lenders decide if they'll give you credit or approve a loan.

The reports also help determine what interest rate lenders will charge you.

Employers, insurers and rental property owners may also look at your credit report.

How can you check your credit report?

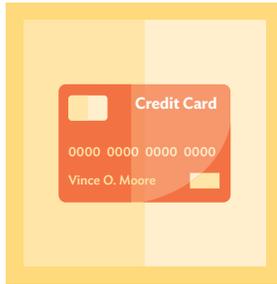
You can get a free report yearly from Equifax, Experian and TransUnion at the official site, annualcreditreport.com.

Equifax, Experian and TransUnion are credit reporting agencies, and they collect and maintain information in your credit report.

Checking your credit report regularly is important to verify that your personal and financial information is accurate.

Do you have a credit report?

How are credit reports created?



A credit report is first created when you open a credit account for the first time and when the creditor reports the information to a credit bureau.

Have you applied for a:



- Credit card?
- Loan?
- Credit account?

If you answered no, then you will most likely not have a credit report.

Three ways to build your credit



Secured credit card
requires a cash deposit that
becomes the credit line.



Credit-builder loan
is a loan where the amount you
borrow is held in an account
while you make payments.



Retail store credit card*
is offered by stores such as
gas stations, retail chains and
department stores.

*Must be 18 to open a retail store credit card



Try it on your own

Use the information contained in handout 2 to review sections found in a credit report.

Name _____ Date _____



Lesson 8—Handout 2

Personal Credit Report

Personal Consumer Credit Report

Personal Identification Information

This section contains the person's name and address, along with the Social Security number and date of birth. It also shows the previous address and employment information.

Name Social Security #: 123-45-6789

1234 Any Street Date of Birth: 07/01/1992

Dallas, TX 75000

Previous Address

Employer: ABC, Inc.

456 Other Rd.

Location: Dallas, TX

Houston, TX 77000

Public Record Information

This section contains publicly available information about legal matters related to credit. It includes bankruptcy history.

None

Importance of checking your credit report

Even if you have never used credit, it is possible that you have been a victim of credit fraud or identity theft.

This can happen if someone has taken credit out in your name or used your Social Security card without your knowledge.

Reminder

You can check your credit report annually for free at annualcreditreport.com.

If you do not have a credit report and are under the age of 18, you can have your parents call each credit reporting agency to manually check if your Social Security number has been reported.



Improve Credit

Explore three ways to improve credit

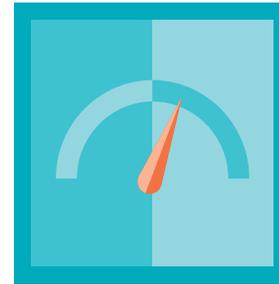
Three ways to improve your credit



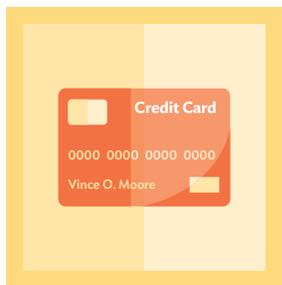
Check your
credit report.



Fix errors.



Know your
credit score.



Character, Capacity & Collateral

How lenders determine a borrower's creditworthiness.

Character



Will you repay the debt?

Character is information that lenders gather about a borrower's willingness to repay a loan.

Creditors will look at:

- Credit history.
- Payment history.
- How much you owe.
- Length of employment.
- How often you borrow.

Capacity



Can you repay the debt?

Capacity is the information lenders gather about a borrower's ability to repay a loan.

Creditors ask for:

- Your occupation.
- Expenses.
- How long you have worked.
- Assets.
- Income.

Collateral



Is the creditor protected?

Collateral is protection for creditors in the event they are not repaid.

Collateral is a real asset such as:

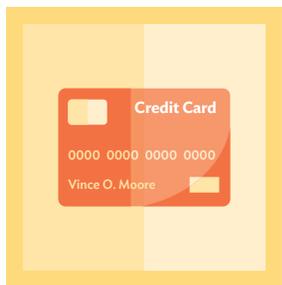
- Savings.
- Property.
- Investment.

What can't be used?

Lenders are **not allowed** to consider certain information when approving credit such as:

- Race.
- Color.
- Religion.
- National origin.
- Marital status.
- Age.
- Receiving money from public assistance.
- Sex.*

* Currently, the law supports arguments that the prohibition against sex discrimination also affords broad protection from discrimination based on a consumer's gender identity and sexual orientation.



Creditworthiness Quiz

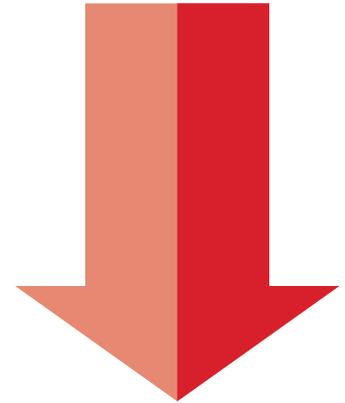
Use the following statements to determine whether the statement would reflect positively or negatively on a person's credit score.

Credit cards are charged to the maximum limit.

Does creditworthiness increase or decrease?



Increase

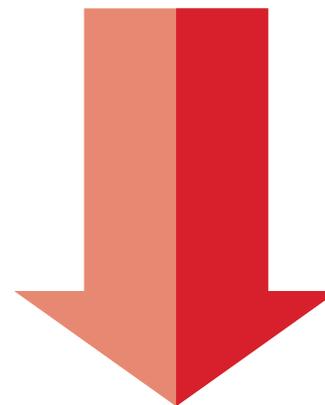


Decrease

Credit cards are charged to the maximum limit.

Creditworthiness will decrease.

Maxing out your credit cards not only hurts your credit, but can make keeping up with payments difficult, especially with interest charges adding up.



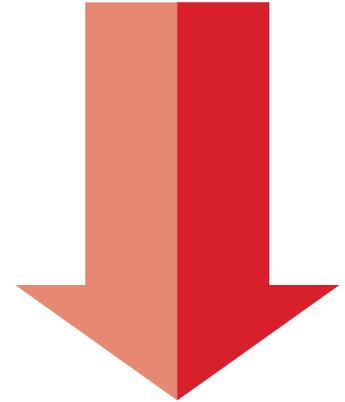
Decrease

Bills are paid on time.

Does creditworthiness increase or decrease?



Increase



Decrease

Bills are paid on time.

Creditworthiness will increase.

Making payments on time every month will help to improve your credit score. Credit scoring models weigh payment history more heavily than any other scoring factor.

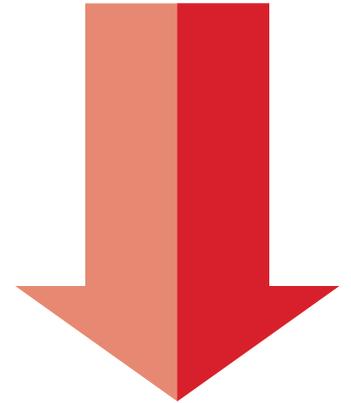


Recently applied for many credit cards.

Does creditworthiness increase or decrease?



Increase

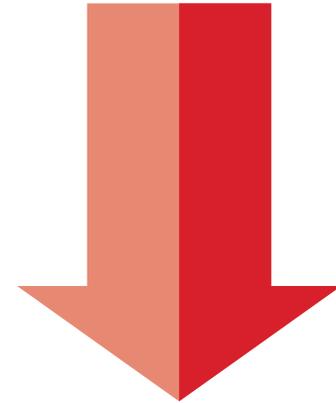


Decrease

Recently applied for many credit cards.

Creditworthiness will decrease.

Too many accounts can indicate increased risk and can decrease your credit score.



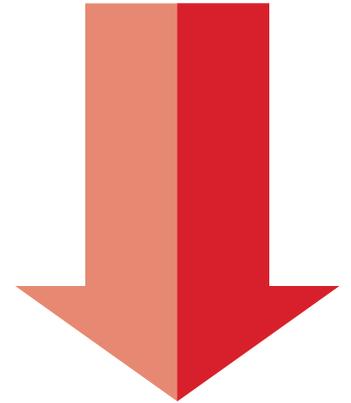
Decrease

Filed for bankruptcy.

Does creditworthiness increase or decrease?



Increase

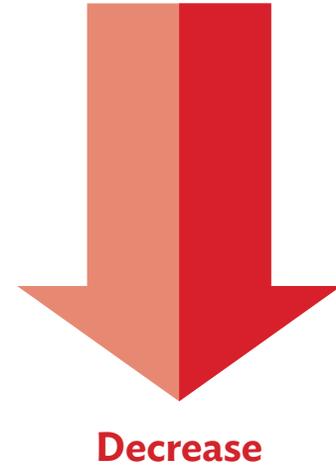


Decrease

Filed for bankruptcy.

Creditworthiness will decrease.

Your payment history is the most important factor in determining your credit score, and filing bankruptcy means that you won't be paying covered debts in full as you initially agreed. As a result, filing bankruptcy will decrease your credit score.

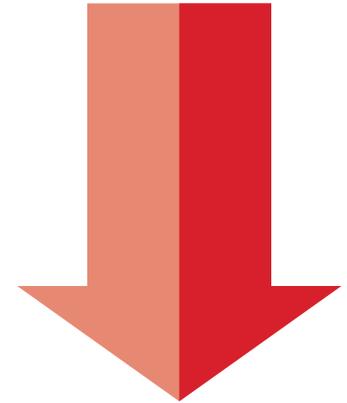


All credit cards are maxed out.

Does creditworthiness increase or decrease?



Increase

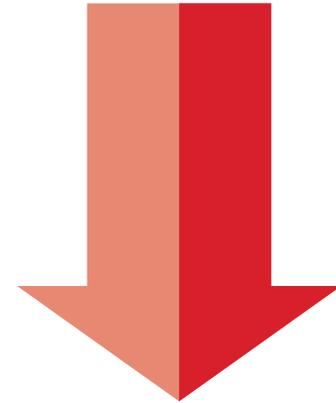


Decrease

All credit cards are maxed out.

Creditworthiness will decrease.

In the eyes of most lenders, a person who constantly charges all the money they can—hitting or going over their credit limit on a regular basis—is more likely to have difficulty repaying that money.



Decrease

Summarize learning objectives

Credit score is a number that predicts the likelihood that a debt will be repaid on time.

A **credit report** is a statement that has information about your credit activity and current credit situation.

Credit scores range between 350 and 850.

Summarize learning objectives

You can **build your credit** using a secured credit card, credit-builder loan or retail store credit card.

You can get a free report yearly from Equifax, Experian and TransUnion at the official site, **[annualcreditreport.com](https://www.annualcreditreport.com)**.

Summarize learning objectives

In addition to credit score and credit report, lenders also look at a borrower's **character, capacity and collateral**.

Character is information that lenders gather about a borrower's willingness to repay a loan.

Capacity is the information lenders gather about a borrower's ability to repay a loan.

Collateral is protection for creditors in the event they are not repaid.

Sources

SLIDES

10, 22–33, 36,
38, 40, 42

Experian

<https://www.experian.com/blogs/ask-experian/credit-education/score-basics/what-affects-your-credit-scores/>

<https://www.experian.com/consumer-products/check-credit-report.html>

<https://www.experian.com/blogs/ask-experian/how-credit-cards-can-affect-your-credit-score/>

<https://www.experian.com/blogs/ask-experian/how-credit-cards-can-affect-your-credit-score/>

<https://www.experian.com/blogs/ask-experian/credit-education/score-basics/what-affects-your-credit-scores/>

<https://www.experian.com/blogs/ask-experian/how-does-filing-bankruptcy-affect-your-credit/>

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FICO

<https://www.fico.com/25years/>

Sources

SLIDES

14, 17, 20,
22-24, 33

Consumer Finance Protection Bureau

<https://www.consumerfinance.gov/consumer-tools/credit-reports-and-scores/answers/key-terms/>

https://files.consumerfinance.gov/f/documents/cfpb_building_block_activities_credit_scores_infographic_handout.pdf

<https://www.consumerfinance.gov/consumer-tools/credit-reports-and-scores/answers/key-terms/>

<https://www.youtube.com/embed/wFTOZollKdk?enablejsapi=1&origin=https://www.consumerfinance.gov>

https://files.consumerfinance.gov/f/documents/201703_cfpb_handout_ECOA_consumers.pdf

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Possible Finance

<https://www.possiblefinance.com/blog/credit-builder-loan/>

44

Credit Karma

<https://www.creditkarma.com/credit-cards/i/credit-card-utilization-and-your-credit-score>

Building **Wealth**

In the Classroom

Up Next: Lesson 9

Take Control of Debt—Choosing the Right Loan



Federal Reserve
Bank of Dallas



Have you explored buildingwealth.org?

The image shows a screenshot of the Building Wealth website. At the top is a teal navigation bar with the 'BW' logo and links for 'About Building Wealth', 'Resources', 'Online Guide', 'Order Building Wealth', 'Acknowledgments', and 'Follow Us' with a Twitter icon. The main header features the title 'Building Wealth' in large green and blue text, followed by the subtitle 'A Beginner's Guide to Securing Your Financial Future'. Below this is a paragraph describing the site as a personal finance education resource for consumers, community leaders, teachers, and students. To the right, a cartoon woman holds a blue sign that says 'Follow us @Budget2Save' with a Twitter icon. The main content area consists of four white cards on a green background with city and house illustrations. Each card has a colored icon: a house for consumers, a podium for community leaders, a graduation cap for teachers, and a backpack for students. Each card includes a title, a short description, and a 'READ MORE >>' link.

BW About Building Wealth Resources Online Guide Order Building Wealth Acknowledgments Follow Us  

Building Wealth

A Beginner's Guide to Securing Your Financial Future

Building Wealth is a personal finance education resource that presents an overview of wealth-building strategies for **consumers**, **community leaders**, **teachers** and **students**.

Follow us @Budget2Save 



For Consumers

I want to learn how to build wealth for myself and my family.

[READ MORE >>](#)



For Community Leaders

I lead a group of adults interested in improving our personal finance skills.

[READ MORE >>](#)



For Teachers

I teach financial education to high school or college students.

[READ MORE >>](#)



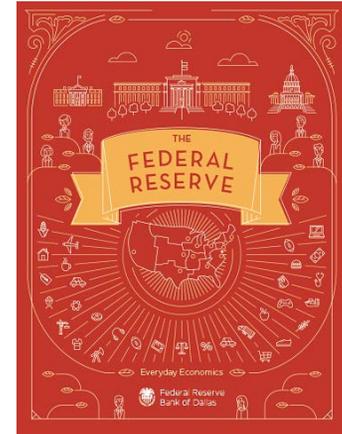
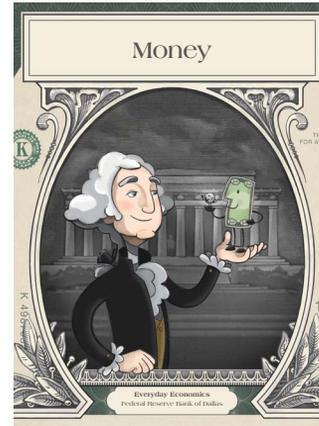
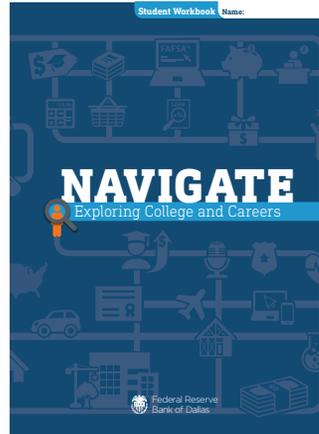
For Students

I am a student and want to learn how to create personal wealth and meet my financial goals.

[READ MORE >>](#)



Explore Dallas Fed Economic Education Resources



@dallasfed

dallasfed.org/educate



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