

CHAPTER 3: UNDERSTANDING CREDIT



OBJECTIVE:

To understand how credit affects our financial life and to learn ways to improve credit.

Credit is your ability to borrow money. Any time a bank, finance company, or business lends you money and you agree to pay it back at a later date, you are using credit. In most cases, there is a charge for borrowing the money, either in the form of fees or interest or both. There are both advantages and disadvantages to using credit.

ADVANTAGES OF USING CREDIT:

- Credit allows you to purchase large items that you might not have enough cash to pay for, such as a house, car, or college education.
- Credit can be a good tool for emergency situations.
- Credit is convenient. Using a credit card is a way to pay for things without having to carry large amounts of cash. Also, your monthly credit card statement provides you with a record of your purchases.
- Some credit card companies may offer protection against your liability in the event that someone uses your card number to make unauthorized purchases.

DISADVANTAGES OF USING CREDIT:

- Credit costs money. There is usually a charge for spreading payments over a period of time.
- Credit can tempt you to spend more than you can afford to repay. You are more likely to purchase items that you do not need.
- Lenders, employers, and landlords often request a copy of your credit report. If you mismanage your credit, it can affect your ability to get additional credit, get a job, rent an apartment, or buy a house in the future.
- When you make a purchase using credit, you commit to using your future income to repay the loan.
- Lenders will report all missed credit payments to the credit bureaus. This will affect your ability to get additional credit in the future.
- If you mismanage credit and are unable to repay the lender, they may repossess, or take back, the item you purchased.

Ask yourself these questions before obtaining and/or using credit:

1. Do I need this or want this?
2. Can I buy this later instead of now?
3. Can I wait until I have cash to pay for it?
4. What does this purchase really cost, with interest?
5. Can I afford the monthly payments?
6. What is the total cost of credit?
7. Are there any fees?
8. What is the annual percentage rate?

Credit Basics

KEY TERMS:

Creditor: The financial institution or business who extends you credit with the agreement that you pay them back with interest (they also have terms and conditions that you agree to meet). Examples are VISA, MasterCard, car loans, retail stores, etc.

Credit Bureaus: Companies that collect information on consumers' credit histories.

WHAT INFORMATION DO CREDIT BUREAUS COLLECT ON A CONSUMERS' CREDIT REPORT?

- Name, previous names, and employment history
- Installment loans (such as car loans, student loans, etc.)
- Revolving accounts (such as credit cards)
- Unpaid medical bills or other bills that have been referred to a collection agency
- Public records
- Bankruptcy
- Any accounts where you are a co-signer (these are considered your debts)
- Inquiries
- Credit Score

ORDERING YOUR CREDIT REPORT

www.annualcreditreport.com

Under the Fair Credit Reporting Act, all consumers can obtain one **FREE** copy of their credit report every 12 months from each of the three credit bureaus at this website.

If you don't have access to the Internet, you can also get your free copy by calling toll free 877-322-8228 or by writing to:

Annual Credit Report Request Service
PO Box 105281
Atlanta, GA 30348-5281

You can also pay for a copy of your report by contacting one of the following credit bureaus*:

www.equifax.com: 800-685-1111

www.transunion.com: 800-916-8800

www.experian.com: 888-397-3742

**The credit bureaus charge \$9 – \$18 for a copy of your report, so show your financial fitness strength and get the free one instead.*

Credit Score Information

Your credit history is used by lenders to determine your ability and willingness to pay back a loan. The lender will review your credit report to see how you use credit and if you pay your bills on time. Lenders usually concentrate on your most recent one- to two-year history unless you've had repeated and serious financial trouble in the past.

FACTORS LENDERS CONSIDER WHEN EXAMINING YOUR CREDIT REPORT

- Derogatory, or negative, credit (collections, charge-off, 30-60-90 day late payments)
- A “pattern and practice” of derogatory credit is evaluated more harshly than a period of time that can be explained by an unusual circumstance (loss of job, hospitalization, etc.)
- Credit score
- Lack of credit history
- Previous bankruptcy or foreclosure
- Public records (liens, judgments, pending legal financial disputes)
- Inquiries (applying for a lot of credit in a short period of time)

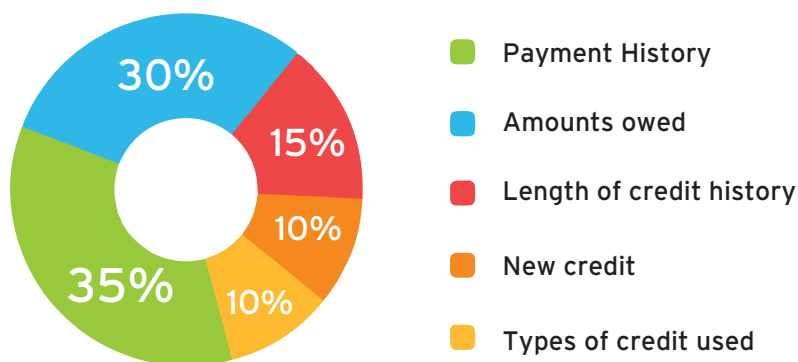
UNDERSTANDING YOUR CREDIT SCORE

A credit score is a number that tells a lender how likely you are to repay a loan, or to make credit payments on time. It is also referred to as a FICO or BEACON score. A credit score is a three-digit number between 350 and 850 that is generated by a computer. It is based on the information in consumer credit reports, including your debt profile and bill-paying history. Each lender will weigh your score in a slightly different way, especially depending on what you are seeking a loan for. The higher the score, the better your eligibility for a lower-interest loan.



HOW YOUR CREDIT SCORE IS CALCULATED

Credit scores are calculated from a lot of different credit data in your credit report. This data can be grouped into five categories as outlined below. The percentages in the chart reflect how important each of the categories is in determining your score.



These percentages are based on the importance of the five categories for the general population. For particular groups – for example, people who have not been using credit long – the importance of these categories may be somewhat different.

Credit Score Information

PAYMENT HISTORY

- Account payment information on specific types of accounts (credit cards, retail accounts, installment loans, finance company accounts, mortgage, etc.)
- Presence of adverse public records (bankruptcy, judgments, suits, liens, wage attachments, etc.), collection items, and/or delinquency (past due items)
- Severity of delinquency (how long past due)
- Amount past due on delinquent accounts or collection items
- Time since (recency of) past due items (delinquency), adverse public records (if any), or collection items (if any)
- Number of past due items on file
- Number of accounts paid as agreed

AMOUNTS OWED

- Balance on accounts
- Balance on specific types of accounts
- Lack of specific type of balance, in some cases
- Number of accounts with balances
- Proportion of credit lines used (proportion of balance to total credit limits on certain types of revolving accounts)
- Proportion of installment loan amounts still owed (proportion of balance to original loan amount on certain types of installment loans)

LENGTH OF CREDIT HISTORY

- Time since accounts opened (typically an account is considered to have history after 12 months)
- Time since accounts opened, by specific type of account
- Time since account activity

NEW CREDIT

- Number of recently opened accounts, and proportion of accounts that are recently opened, by type of account
- Number of recent credit inquiries
- Re-establishment of positive credit history following past payment problems

TYPES OF CREDIT USED

- Number of (presence, prevalence, and recent information on) various types of accounts (credit cards, retail accounts, installment loans, mortgage, consumer finance accounts, etc.)

Credit Affects Your Ability to Borrow Wisely

Your credit is one of the factors that will determine what interest rate you will qualify for with most lenders. In general, a higher credit score rating will mean a lower interest rate loan. Homewise will work with you to help you qualify for the best interest rate possible for your mortgage loan. Whether you are shopping for a mortgage loan to buy a home, thinking about refinancing your current home, or even buying a car or furniture, you need to advocate for yourself and protect your best interest. When shopping for a loan, make sure to find the product with the lowest interest rate and most favorable terms.

Don't borrow trouble!

INTEREST RATE COMPARISON CHART

The following table compares loans at different interest rates for a \$30,000 car loan with a 5 year fixed-interest-rate loan.

RATE	PAYMENT
2.75%	\$535
5.25%	\$570
12.25%	\$671
20%	\$795

A higher credit score will help you get the lower interest rate loan and save you money. In our example, having a higher credit score and getting a loan with a 2.75% interest rate instead of 20% would save you \$260 per month or \$15,545 over the life of the loan!

ESTABLISHING CREDIT

You may not have a credit rating simply because not enough information is available about you. It is important to meet with a Homewise Home Purchase Advisor to see what you should do to establish credit to purchase a home. Here are some steps to build a credit history over time:

1. Start by opening a checking account and do not overdraw it.
2. Make regular deposits into a savings account.
3. Visit your bank to open a secured credit card. They will ask for a deposit or they can freeze funds you may already have in your bank account to secure the card. This deposit amount will be the same as your credit limit. It works just like a normal credit card. After you have paid on time for a few months, they will unsecure the card and un-freeze the deposit.
4. Make sure your rent, utilities, and other bills are in your name and that you pay them on time each month.

Correcting Credit Issues

REVIEWING YOUR CREDIT REPORT

Knowing and understanding what is in your credit report is one of your most important consumer rights. You should order a credit report each year to check for and correct any mistakes or problems. If you have any questions concerning a mistake or credit denial, contact that creditor immediately.

IF THERE ARE MISTAKES IN YOUR CREDIT REPORT OR YOU WOULD LIKE TO DISPUTE SOMETHING IN THE REPORT, TAKE THE FOLLOWING ACTIONS:

Dispute Problem Online - In order to help consumers protect themselves from identity theft, the Federal Government has established a website, www.annualcreditreport.com, for you to obtain your free credit report from the three credit bureaus (Equifax, TransUnion, and Experian). No credit score will be provided, but you don't need it! At this site you can dispute any errors online; just follow the instructions for disputing errors. Each bureau has 30 days to resolve the issue for you.

Should you have a problem disputing errors through www.annualcreditreport.com, you can always dispute errors online by visiting the credit bureaus through their own websites: www.equifax.com, www.experian.com, and www.transunion.com. These sites provide directions on how to "dispute online." Depending on which bureau(s) your creditor reported the account error to, you might need to go to only one or two bureaus. In disputing your credit report, make sure you refer to the Reference Number on the first page of the credit report you obtained for free at www.annualcreditreport.com. After you are finished with the process, your request will be submitted in seconds. Each credit bureau has 30 to 45 days to investigate your request. The results of the investigation will be mailed to you, along with a copy of your credit report.

By Phone - Call 877-322-8228 to request a free credit report from all three credit bureaus. The report will arrive 7 to 15 days after requested. Once you have received a credit report, look for a phone number provided for investigations or filing a dispute. You will need the Confirmation Number or Report Number listed at the top of the report (this is an ID number unique to your report). You will be able to talk to a customer-service representative to place an investigation on any account that the report indicates has an incorrect status. As with disputing online, credit bureaus have 30 to 45 days to investigate and will send you the results by mail.

By Mail - You can send a request letter to the three different credit bureaus; your Homewise Home Purchase Advisor can give you a sample dispute letter and the addresses you should mail it to. Because you are mailing sensitive and important personal information such as your name, date of birth, social security number and perhaps other supporting documents, we recommend sending it Certified Mail with a confirmation receipt which is federally insured and lets you know when your letters have been delivered.



FITNESS TIP

It is important to build a good relationship with credit and not to overextend your borrowing practices. At the first sign of trouble with any creditor, contact the creditor and try to work out a reasonable payment plan to avoid late payments, fees, and referrals to collection agencies.

Sample Dispute Letter

Date

Your Name
Your Address
Your City, NM 87507

Complaint Department
Trans Union
PO Box 2000
Chester, PA 19022
800-916-8800

Complaint Department
Experian National Consumer Assistance
PO Box 2002
Allen, TX 75013
888-397-3742

Complaint Department
Equifax
PO Box 740241
Atlanta, GA 30374
800-685-1111

Dear Sir or Madam:

I am writing to dispute/correct the following information in my file. The items I am disputing/correcting also are circled on the attached copy of the report I received.

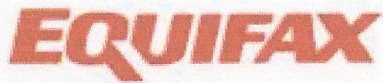
1. (Identify item(s) disputed by *name of source*, such as creditors or tax court, and identify *type of item*, such as credit account, judgment, etc.)
2. **This/these item(s) is/are** (inaccurate or incomplete) **because** (describe what is inaccurate or incomplete and why.) (Or, I do not know what these charges are for and have no record of owing this/these amount(s). Please provide more details on your investigation of the items in question.) I am requesting that the item(s) be deleted (or request another specific change) to correct the information. Enclosed are copies of (use this sentence if applicable and describe any enclosed documentation, such as payment records, court documents) **supporting my position.**

Please investigate this/these matter(s) and (delete or correct) the disputed item(s) as soon as possible. In addition, please send me a free copy of my updated credit report reflecting this/these change(s).

Sincerely,

Your Name

Enclosures: (List what you are enclosing, the proof or backup documentation)



Equifax Credit Report™ for [REDACTED]

Report Does Not Update

Confirmation #:26.

Section Title	Section Description
1. Credit Summary	Summary of account activity
2. Account Information	Detailed account information
3. Inquiries	Companies that have requested or viewed your credit information
4. Negative Information	Bankruptcies, liens, garnishments and other judgments
5. Personal Information	Personal data, addresses, employment history
6. Dispute File Information	How to dispute information found on this credit report
7. Summary of Your Rights Under the FCRA	Summary of Your Rights Under the FCRA
8. Remedying the Effects of Identity Theft	Remedying the Effects of Identity Theft
9. Your Rights Under State Law	Your Rights Under State Law

Credit Summary

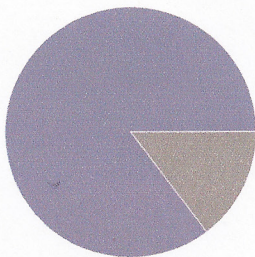
Your Equifax Credit Summary highlights the information in your credit file that is most important in determining your credit standing by distilling key credit information into one easy-to-read summary.

Accounts

Lenders usually take a positive view of individuals with a range of credit accounts - car loan, credit cards, mortgage, etc. - that have a record of timely payments. However, a high debt to credit ratio on certain types of revolving (credit card) accounts and installment loans will typically have a negative impact.

Open Accounts	Total Number	Balance	Available	Credit Limit	Debt to Credit Ratio	Monthly Payment Amount	Accounts with a Balance
Mortgage	0	\$0	N/A	N/A	N/A	\$0	0
Installment	2	\$4,297	\$0	\$7,438	58 %	\$333	2
Revolving	1	\$735	\$49	\$784	94 %	\$15	1
Other	0	\$0	N/A	N/A	N/A	\$0	0
Total	3	\$5,032	\$49	\$8,222	61 %	\$348	3

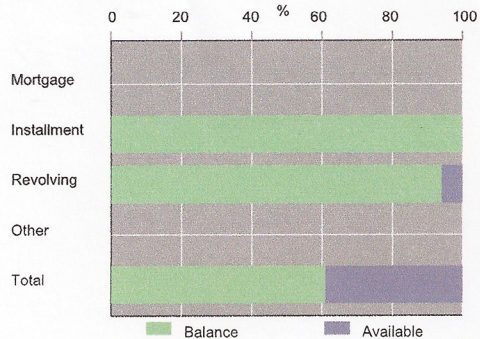
Debt by Account Type



- Mortgage-0%
- Revolving-15%
- Installment-85%
- Other-0%

NOTE: Total may not equal 100% due to rounding

Debt to Credit Ratio by Account Type



Account Age

Usually, it is a good idea to keep your oldest credit account open, as a high average account age generally demonstrates stability to lenders. Also, especially if you have been managing credit for a short time, opening many new accounts will lower your average account age and may have a negative impact.

Length of Credit History

8 Years, 0 Months

Average Account Age
Oldest Account
Most Recent Account

4 Years, 6 Months
 CHASE (Opened 05/2004)
 LOS ALAMOS NTL BANK (Opened 02/2012)

Inquiries - Requests for your Credit History

Numerous inquiries on your credit file for new credit may cause you to appear risky to lenders, so it is usually better to only seek new credit when you need it. Typically, lenders distinguish between inquiries for a single loan and many new loans in part by the length of time over which the inquiries occur. So, when rate shopping for a loan it's a good idea to do it within a focused period of time.

Inquiries in the Last 2 Years
Most Recent Inquiry

.8
 CREDCO::2635255594 (05/08/12)

Potentially Negative Information

Late payments, collections and public records can have a negative impact on your credit standing. The more severe and recent they are, the more negative the potential impact might be.

Public Records
Negative Accounts
Collections

0
 10
 1

Mortgage Accounts

Mortgage accounts include first mortgages, home equity loans, and any other loans secured by real estate you own.

You have no mortgage accounts on file.

Installment Accounts

Installment accounts are credit accounts in which the amount of the payment and the number of payments are predetermined or fixed, such as a car loan.

Open Accounts

Account Name	Account Number	Date Opened	Balance	Date Reported	Past Due	Status	Credit Limit
CITIFINANCIAL	CITIFINANCIAL	12/2006	\$731	12/2008	\$731	120+ DAYS PAST DUE	

CITIFINANCIAL

300 Saint Paul St
 BSP13A
 Baltimore , MD-212022120
 (800) 922-6235

Account Number:		Current Status:	120+ DAYS PAST DUE
Account Owner:	Joint Account	High Credit:	\$ 2,501
Type of Account :	Installment	Credit Limit:	
Term Duration:	24 Months	Terms Frequency:	Monthly (due every month)
Date Opened:	12/2006	Balance:	\$ 731
Date Reported:	12/2008	Amount Past Due:	\$ 731

Credit Basics: Know Your Privacy Rights

HOW TO "OPT-OUT"

Credit Bureaus sell your name and address to companies who want to solicit your business. You have the right to opt out of having all three Credit Bureaus sell your information by calling **one** national number: **888-5-OPT-OUT**.

THE NATIONAL DO-NOT-CALL REGISTRY

You can also protect yourself from unwanted phone calls from predatory lenders and other telemarketers. As of October 1, 2003, the Federal Communications Commission (FCC) established the National Do-Not-Call Registry. Telemarketers may not call registered telephone numbers or they will be subject to large fines. The registry **will not** prevent calls from organizations or businesses with whom you have an established relationship (for example, your current long distance company), calls which are not commercial, or calls from non-profit organizations.

To register, call 888-382-1222 or go to www.donotcall.gov. You must call from the telephone you wish to register.

HOW TO PROTECT YOURSELF AGAINST IDENTITY THEFT

1. Never provide your personal information in response to an unsolicited request whether over the phone or internet.
2. Shred unnecessary documents that have your address and/or social security number listed on them as well as any credit offers you receive.
3. Do not carry identification that has your social security number in your purse or wallet. If your wallet is stolen, you can notify credit card companies but you cannot control what credit accounts will be opened in your name with your social security number.
4. Order a copy of your credit report every year. Catch mistakes and fraud before they ruin your personal finances.
5. Pay attention to your statements. If your bills don't arrive on time, contact your creditor. A missing credit card bill might mean that the identity thief has changed your billing address and is using your account.
6. Guard your mail from thieves. Pick up your mail from your mailbox as soon as possible. Place outgoing mail in post office collection boxes.

For more information on identity theft, visit the following:
www.consumer.gov/idtheft/ or 877-IDTHEFT (438-4338)
www.fraud.org 800-876-7060

For more information on credit:

www.fico.com

www.consumersunion.org

www.ftc.gov

www.cardtrak.com

www.bankrate.com