



UNIT 3-2

Building Your Credit History

Now that we have examined the types of credit, the C's of credit, and using credit wisely, it is time to turn our attention to building your **credit history**. Credit history is the official record of the way you use your credit and repay your debts. It provides another piece of information to creditors about your creditworthiness. Without a good credit history, it is very difficult to get the credit that can lead you to financial well being and along the pathway to home ownership.

As we discovered in the first lesson of this unit, credit is not something that is given lightly. Consumers must apply for it. Banks, retailers, and finance companies consider many factors before they are willing to lend you money. You would not lend money to a stranger without hesitation—lenders are the same!

Your credit history is used by creditors or lenders to determine your creditworthiness. They use it to determine your willingness and ability to repay your debts. The benefits for businesses who lend to applicants with a good credit history include a lower risk of nonpayment, enhanced profits as revenue will be paid on time, and the granting of credit is less time consuming and less expensive. When lenders offer credit to those with poor credit history, the application process is more complicated and time consuming which is ultimately more costly for the lender, the lender runs the risk of the loan or credit not being fully repaid, therefore reducing profits, and the costs for collecting and servicing the loan will increase which reduces the lender's profits.

Case Study Application

In this lesson, we will be examining credit histories and how you can build your own credit history in order to pursue the pathway to home ownership. Review the following case study which introduces us to the importance of a building a strong, positive credit history.



CASE STUDY: ANDREW'S CREDIT HISTORY

Andrew is a full-time college student and works part-time at the local pizzeria for a little more than minimum wage. Recently, Andrew began his first steps toward building his credit history so that he can purchase a home in the future. He began by putting his car and renter's insurance in his name. He also opened a cellular phone account and has been paying all of the bills on time each month. He has started a savings plan and is slowly moving toward financial independence while working on his educational skills as well. He knows that the investment in his education will help him with his financial well-being.

Now that Andrew has begun to build his credit history, he wonders why it is important; how can he develop a positive credit history; and how do lenders decide who gets the credit?

Why is a Credit History Important?

Let's face it—today's economy is based on credit. Having a strong credit history makes it easier for you to get loans, lines of credit, and lower interest rates. Your credit history comes from information you supply on loan and/or mortgage applications as well as from your credit history. It shows any credit-card accounts or loans that you have, the balances, how regularly you make your payments and if any action has been taken against you due to unpaid bills.

Lenders acquire your credit history from one of the three major credit reporting agencies (Experian, TransUnion, or Equifax). These agencies collect information about credit activities and store it in large databases. They then provide reports to creditors regarding your history. These agencies provide information to:

- Creditors who are considering giving you credit;
- Employers considering you for employment;
- Government agencies reviewing your financial status in regard to issuing you certain licenses or government benefits;
- Insurers considering you for an insurance policy; and
- Anyone else with a legitimate business reason for acquiring the information related to a business transaction that you have initiated.

Your credit history includes four types of information: identifying information, credit information, public record information, and inquiries. Identifying information includes your name, nicknames, current and previous addresses, year of birth, social security number, employers. The credit information includes the accounts



you have with banks, retailers, credit-card companies, and other lenders. This includes the type of account, the date you opened the account, your credit limit or loan amount, co-signers of the loan, and your payment patterns over the past two years. The public record information includes state and county court records on tax liens, bankruptcy, or monetary judgments. Finally, the inquiries are a listing of the names of those who have obtained copies of your credit report within the last six months.

Why does this information matter? A record of good credit history has the benefits of: obtaining future credit can be quick and easy; positive information stays on your credit report indefinitely, continuing to build your creditworthiness; your costs of borrowing will be lower because you can select from many different lenders and can choose those with lower interest rates; likewise, more lenders will be interested in lending to you. A poor credit history will lead to the situation of not being able to obtain future credit; you will have fewer lenders willing to lend to you; your costs of borrowing will be higher because you will not have as many wishing to lend to you; your interest rates will be higher; and the negative information remains part of your credit history for seven years.

- What other benefits might result from having a good credit history?
- What other costs might result from having a poor credit history?

Developing Your Credit History

The decisions you make today regarding your finances will affect your ability to borrow money in the future. It will also affect the rates you will pay to borrow that money. If you have a strong history, your rates will be lower. In contrast, if you have a weak history, you will pay higher rates. Your credit history can also impact your ability to rent or buy a place to live, get insurance, or *even* get a job!

How can you begin to establish your credit history? Consider applying for a secured credit card. This type of card requires you to open an account at the financial institution as security for your line of credit. Your credit line will then be a percentage of the deposit. For example, the account may require you to make a deposit of \$500. You will then have an account with a \$500 line of credit. You may be able to add to the deposit and therefore add more credit, or sometimes the lender will reward you for good payment history and add to your credit line without requesting additional deposits. These cards usually have higher interest rates than traditional cards and have higher application and processing fees.

Another idea is to apply for a credit card issued by a local store or gas station. Local businesses are sometimes more willing to extend credit to someone with no credit history. Once you begin to establish a positive credit history, major creditors might be more willing to offer you credit. Just be careful not to charge more than you can pay in full each month and be sure to make the monthly



payments on time. Finally, you may want to consider asking someone with an established credit history to co-sign the account if you don't qualify for credit on your own. Be careful, the co-signer must pay your debts if you don't!

Other things you can do include: pay your bills on time. Be sure to select credit cards that have low rates and no fees. Do not lend your credit cards to ANYONE. Limit your credit card purchases to those you can pay in full each month. Report a lost or stolen card immediately to avoid any credit history complications. Finally, be sure to obtain a copy of your credit report annually to check its accuracy.

- What are factors that Andrew should consider in developing his credit history?
- What steps can you take today to build a positive credit history?

Deciding Who Gets the Credit

Now that we have examined why credit history is important and the development of your credit history, we are going to review several credit applications from the viewpoint of a lender. The appended credit applications have been submitted to the Crittenden Bank and Trust. It is your job as a loan officer for the bank to decide whose applications should be awarded and those you would not award.

Use the PACED decision making model to assist in your analysis of the applications. Begin by thinking about the evaluation criteria that you will use to evaluate the applications—capital, capacity, and character, then read each of the applications based on this criteria. Place a “+” or “-“ in each corresponding box for each of the criteria.

- Based on your analysis, which credit applications would you approve? Why/why not? What are the benefits of lending to these applicants?
- Did you reject any of the applications? If so, why? What are the potential costs and risks of lending money to these applicants?
- What could the applicants who were not approved for credit do to improve their credit histories to enable them to receive credit in the future?



Activity Sheet 3-3: Who Gets the Credit? Using the PACED Decision Making Model



Directions: Use the PACED Decision Making Model below to contrast the advantages and disadvantages of your problem. After you have evaluated to the issue, discuss the choice you would make. Complete the analysis by using these five steps in the decision making model:

Step 1: State the **Problem**: _____.

Step 2: List the **Alternatives** in the first column.

Step 3: List the **Criteria** in the first row.

Step 4: Evaluate each alternative by placing a “+” or a “-” in the box below each criterion.

Step 5: Make your **Decision**: To whom do you make the loan?

Criteria ↓ Alternatives →	1. Capital	2. Capacity	3. Character
1. Jackie Kidd			
2. Katie Battaglia			
3. Matthew Smith			

Using the space below, explain why the decision in step 5 above is the best choice to receive the credit approval. What are the benefits of lending money to this applicant? What are potential costs and risks?



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Loan Application #1

Loan Type: Personal

Loan Purpose: Debt Consolidation—I would like to use this loan to consolidate my debt.

I have multiple lines of credit that I would like to combine into one line so that I don't have so many to track and can have one interest rate rather than the multiple rates.

Individual Details:

Applicant's Name: Jackie Kidd **Date of Birth:** 10-14-1980

Co-Applicant's Name: **Date of Birth:**

Address: 35 Bedinger Lane Creekswitch, KY 41052

Phone: (859) 564-1258

Time at Current Address: 1 year **Living Situation:** Renting

Monthly Mortgage/Rent: \$750

Previous Address: 48 Alta Vista Drive Taylor Mill, KY 41097

Time at Previous Address: 10 years

Number of Dependents: 2

Ages of Dependents: 14, 10

Education: (Highest Level of Education Attained)

Master's Degree in Education, Crittenden State University

Name and Address of Employer: Crittenden Elementary School

Current Occupation: Teacher

Nature of Occupation: Full time

Time in Current Occupation: 6 years

Gross Annual Income: \$48,000

Other Income: \$ 2,000

Name/Address Previous Employer: McDoogle's Restaurant, Server and Hostess

Years in Previous Occupation: 5 years

Liabilities Details:

1. 7/5th National Bank Auto Loan \$15,600
2. Crittenden Express Credit Card \$ 7,456
3. Nancy's Retail Credit Card \$ 1,362
4. Student Loan, Cougar Lenders \$12,340
5. Other Liabilities:

Assets Details:

1. Crittenden Bank and Trust Savings \$ 750
2. 7/5th National Bank Checking Account \$2,500
3. KPC Mutual Funds \$5,500
4. Real Estate:



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Loan Application #2

Loan Type: Auto

Loan Purpose: We would like to buy a new car. We would like to borrow \$30,000 to buy a new Luxist sedan. We would like a 60 month loan. This would give us monthly payments of \$567 for the car.

Individual Details:

Applicant's Name: Katie Battaglia **Date of Birth:** 2-10-1983

Address: 1345 Walton Nicholson Road Independence, KY 41086

Phone: (859) 897-5487

Time at Current Address: 5 years **Living Situation:** Own

Monthly Mortgage/Rent: \$1,134

Previous Address: 26 Upland Court Newport, OH 45202

Time at Previous Address: 2 years

Number of Dependents: 0

Ages of Dependents:

Education: (Highest Level of Education Attained)

(A) Law Degree, Crittenden State University

(S) BS Degree, Graphic Design, Valley View College

Name and Address of Employer: Dewey, Smith, and Howe Law Firm

Current Occupation: Lawyer

Nature of Occupation: Full time

Time in Current Occupation: 4 years

Household Gross Annual Income: \$115,000

Other Income: None

Name/Address Previous Employer: Chase Law Firm, Paralegal

Years in Previous Occupation: 3 years

Liabilities Details:

1. Hunters National Bank, Auto Loan \$ 11,200
2. Vita Credit Card \$ 256
3. Dollard's Retail Credit Card \$ 762
4. Student Loan, Upstate Lenders \$ 22,750

Assets Details:

1. Crittenden Bank and Trust Savings \$ 350
2. 7/5th National Bank Checking Account \$ 1,500
3. GEC Mutual Funds \$ 8,500
4. Norse Corporation Stock \$ 3,324
5. 26 Upland Court, Real Estate \$156,000



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Loan Application #3

Loan Type: Education

Loan Purpose: I would like to pursue further education and am requesting funding to do so. This education will be used to increase my job skills

Individual Details:

Applicant's Name: Matthew Smith **Date of Birth:** 12-03-1975

Address: 129 Pentunia Lane, Apt B

Phone: (859) 475-1721

Time at Current Address: 3 years **Living Situation:** Renting

Monthly Mortgage/Rent: \$760

Previous Address:

Time at Previous Address:

Number of Dependents: 0

Ages of Dependents:

Education: (Highest Level of Education Attained)

Associate's Degree in Computer Science, Walton Community College

Name and Address of Employer: Adco Design Associates

Current Occupation: Computer Programmer

Nature of Occupation: Full time

Time in Current Occupation: 4 years

Gross Annual Income: \$42,000

Other Income: none

Name/Address Previous Employer: Walton Community College, IT support

Years in Previous Occupation: 2 years

Liabilities Details:

- | | |
|-----------------------------------|--------|
| 1. Crittenden Express Credit Card | \$ 235 |
| 2. Express Gas Card | \$ 75 |
| 3. Other Liabilities: | |

Assets Details:

- | | |
|---|---------|
| 1. Crittenden Bank and Trust Savings | \$1,750 |
| 2. 7/5 th National Bank Checking Account | \$ 872 |
| 3. TMQ Mutual Fund | \$2,500 |

