



# Bridging the Capital Access Gap

A Curriculum for Lenders, Business Development Organizations, and TA Providers



LSC



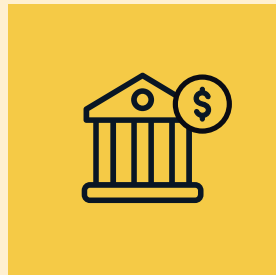
# Main Topics



## CHAPTER 1

### **Lending Landscape**

(Modules 1 - 4)



## CHAPTER 2

### **Underwriting Basics**

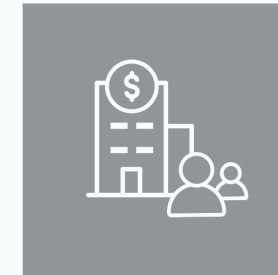
(Modules 5 - 8)



## CHAPTER 3

### **The Best Version of the Business**

(Modules 9 - 14)



## CHAPTER 4

### **Preparing for the Next Level**

(Modules 15)



## CHAPTER 5

### **Resources for Professional Development**

(Modules 16)



## CHAPTER 2

# Underwriting Basics (Modules 5 - 8)

**What is Underwriting?** (Modules 5)

**Five C's of Credit** (Modules 6)

**Understanding Credit** (Modules 7)

**Debt Service Coverage** (Modules 8)



# Understanding Credit

7

# Understanding Credit: What You'll Learn

- What is a credit report.
- Why is it important.
- What information does it contain.
- How lenders use it when making a loan decision.
- Why credit can be challenging for underserved, disadvantaged borrowers.



# What is a Credit Report?

- Identifying information: Name, SSN, addresses, employers.
- Credit scores.
- List of all loan and credit accounts, and payment record.
- Collections and bankruptcies.
- Inquiries, AKA a credit check. Inquiries happen when there is a legally permitted request to see your credit report from a company.
- Public records, such as tax liens, unpaid child support and lawsuits.



**A detailed history  
of someone's  
information and  
performance on  
several fronts**

# Credit report detail

**Your personal statements**

General personal statements currently displaying on your personal credit report at your request appear below.

FILE FROZEN DUE TO STATE LEGISLATION. [+ Options](#)

Add statement(s)

Add personal statement

[back to top](#)

**Potentially negative items**

No **Public Records** appear on your report.

-

**Account name**  
123 CREDIT CARDS  
  
2000 MAIN ST  
ANYTOWN, USA 12345  
*No phone number available*  
**Address identification number**  
0122868651

**Account number**  
40034424804....

**Type**  
Credit card  
**Terms**  
Revolving

**Recent balance**  
\$273 as of  
06/03/2015  
**Credit limit or  
original amount**  
Not reported  
**High balance**  
\$14,219  
**Monthly payment**  
\$10  
**Recent payment  
amount**  
\$0  
**Past due amount**  
\$20

**Date opened**  
11/2013  
**Date of status**  
06/2015  
**First reported**  
12/2013  
**Responsibility**  
Individual

**Status**  
**Open.** [+ Dispute](#)

**Account history**

2015	May	Apr	Mar	Feb	Jan	2014	Dec	Nov	Oct	Sep	Aug	Jul	Jun	May	Apr	Mar	Feb	Jan	2010	Dec	Nov	Oct	Sep	Aug	Jul	Jun	May
30	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	OK	

**Payment history guide**  
30 days past due as of Jun 2015

Type of account  
and date opened:  
credit card, auto  
loan, mortgage

Credit limit or  
original loan amount,  
and current balance

Monthly payment  
amount

# Credit report detail

Accounts in good standing

Account name

HOMETOWN AUTO

15520 E ELM ST STE 300  
ANYTOWN, USA 12345  
866 555 5555

Address identification number

0122868651

Account number

1032911005...

Type

Auto

Terms

60 Months

Recent balance

\$11,616

Credit limit or original amount

\$19,118

High balance

\$19,118

Monthly payment

\$350

Recent payment amount

\$350

Date opened

03/2013

Date of status

05/2015

First reported

04/2013

Responsibility

Individual

+ Dispute

Account history

2015

May

Apr

Mar

Feb

Jan

2014

Dec

Nov

Oct

Sep

Aug

Jul

Jun

May

Apr

Mar

Feb

Jan

2013

Dec

Nov

Oct

Sep

Aug

Jul

Jun

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Account name

AMERICAN APARTMENTS

PO BOX 981400  
ANYTOWN, USA 54321  
800 555 5555

Address identification number

0122868651

Account number

48886031311....

Type

Rental

Terms

12 months

Recent balance

\$4,000

Credit limit or original amount

\$12,000

High balance

\$12,000

Monthly payment

\$1,000

Recent payment amount

\$1,000

Date opened

10/2014

Date of status

05/2015

First reported

11/2014

Responsibility

Individual

+ Dispute

Payment history –  
25 months

Collections

Bankruptcies



# Credit Bureaus

- Credit bureaus compile credit reports and credit scores about individual borrowers.
- Credit bureaus are private companies that are regulated under the Fair Credit Reporting Act.
- Banks, financing companies, retailers, and landlords send consumer credit information to the credit bureaus.
- Three companies – Equifax, Experian, and TransUnion – dominate the market for collecting, analyzing, and disbursing information about consumers.



# Fair Credit Reporting Act

Federal legislation to promote the accuracy, fairness, and privacy of consumer credit information.

- Lenders and employers must disclose if a credit file was used to deny a loan or a job.
- You can get free access to your credit reports.
- The credit bureaus must give you access to your scores as well (for a fee).
- You can file a dispute if there are errors. Errors must be corrected in 30 days



# Fair Credit Reporting Act *continued*

- Agencies must remove most negative credit information after seven years and bankruptcies after seven to ten years.
- Only those with a valid need (banks, nonbank lenders, landlords, employers) can access your credit reports with signed authorization from you.



# Credit Report Role in Small Business Lending



- Most likely a personal or consumer credit report for small business loans.
- Lenders take many different approaches to the credit report, but here are the most common:

- **FICO Score**
- **Payment history**
- **Slow pays**
- **Collections**
- **Amount of credit used/available\***
- **Total debt service\***

\*These topics will be covered in more detail in Modules 8 and 12

# FICO Score

- A FICO® score is a three-digit number ranging from 300 to 850
- A FICO score is a model using credit history and is a shorthand way to determine credit worthiness.



# FICO Formula

**30%**

## **Amounts Owed**

Do you have a reasonable amount of debt relative to limits?

**10%**

## **New Credit**

How much credit have you added or applied to recently?

**15%**

## **Length of Credit History**

How long have you had credit?

**10%**

## **Credit Mix**

Do you have credit cards, auto loans, and mortgages?

**35%**

## **Payment History**

Have you paid on time?



# What is a “good” FICO score?

- Commercial banks and traditional lenders consider 680 and above a good score.
- CDFIs and other nontraditional lenders often work with borrowers who have scores in the mid 500s.
- Some CDFIs work with “credit invisibles” or those with no credit report or score.



# Payment History

- Whether you've paid your accounts: on time or late.
- Many creditors, vendors and service providers report monthly payments to the three consumer credit bureaus.
- Payment history is built month by month.
- Credit reports have many formats for displaying payment history.

**Credit reports have many formats for displaying payment history.**



## Account history

2015						2014
May	Apr	Mar	Feb	Jan	Dec	
30	OK	OK	OK	OK	OK	

## Pay History:

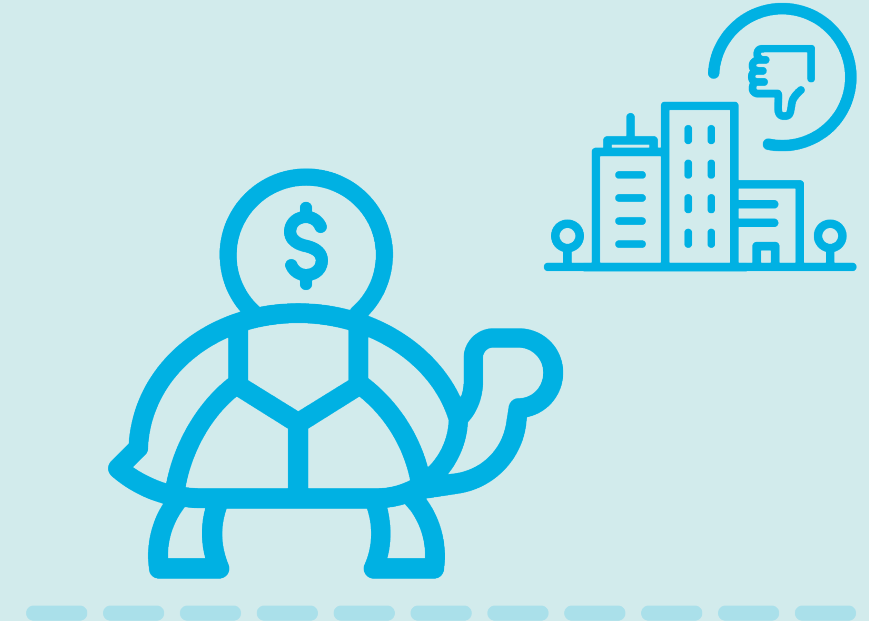
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Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2010	*	*	*	*	*	*	*	*	*	*	*	*
2009	*	*	*	*	*	*	*	*	*	60	*	*



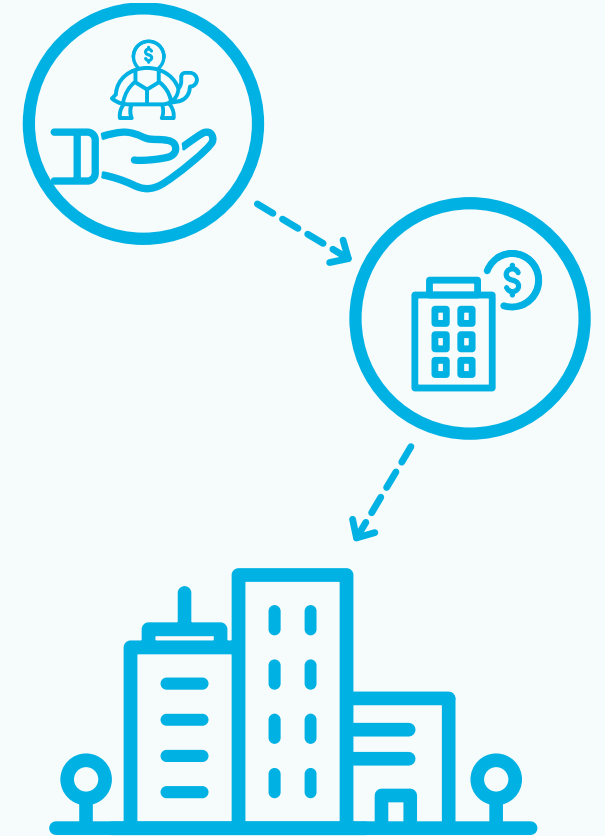
# Slow Pay vs Collection

- Most lenders will allow late payments and charge fees when payments are late.
- Late payments, also called slow pays, are reported to credit bureaus and affect the FICO score.
- Every lender has policies and procedures for late payments and late fees.
- At some point of payment delinquency, a lender will sell the loan to a collection agency.
- Then a 'slow pay' becomes a 'collection' which is a more serious credit report problem.



# Collections

- When an account is seriously past due, the lender sells it to a collection agency which usually reports to the credit bureaus.
- Person owing the debt can negotiate a payment plan, sometimes for a reduced amount.
- While settling an account is much better than not paying it at all, it is still considered negative because it means the debt was not paid as agreed upon.
- All types of accounts can be sent to collections, including phone & utility bills.



# The impact of collections

- Credit reports show accounts reported to collection agencies.
- A history of collections (and slow pays) increase risk assessment.
- Successful completion of a payment plan could mitigate the negative impact of a collection.
- Please watch **Module 12 – Improving Credit** – for more about how to address collections.



# Amount of Credit Used/Available

Lenders will look at how much debt the applicant has taken on.

Lender will perceive higher risk if the applicant:

- Is highly leveraged – has a lot of debt relative to income
- Has maxed out or has high balances on several credit cards
- Total monthly debt payments are high\*



\*Please view Modules 8 and 13 to learn more about understanding monthly debt service.

# Type of Debt

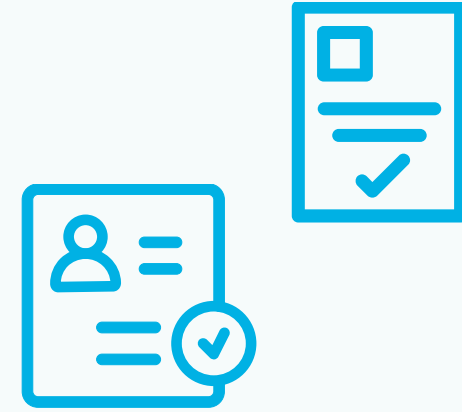
A lender will also look at what type of debt the applicant has:

- **Credit cards** – how many, how recent, balance/limit, what stores, total monthly payments
- **Mortgages** – how much, outstanding balance, monthly payment
- **Car loans** – how many, how much, monthly payment
- **Student loans** – how much, but often discounted because of terms
- **Medical** – some lenders overlook or discount medical debt



# Credit report examples

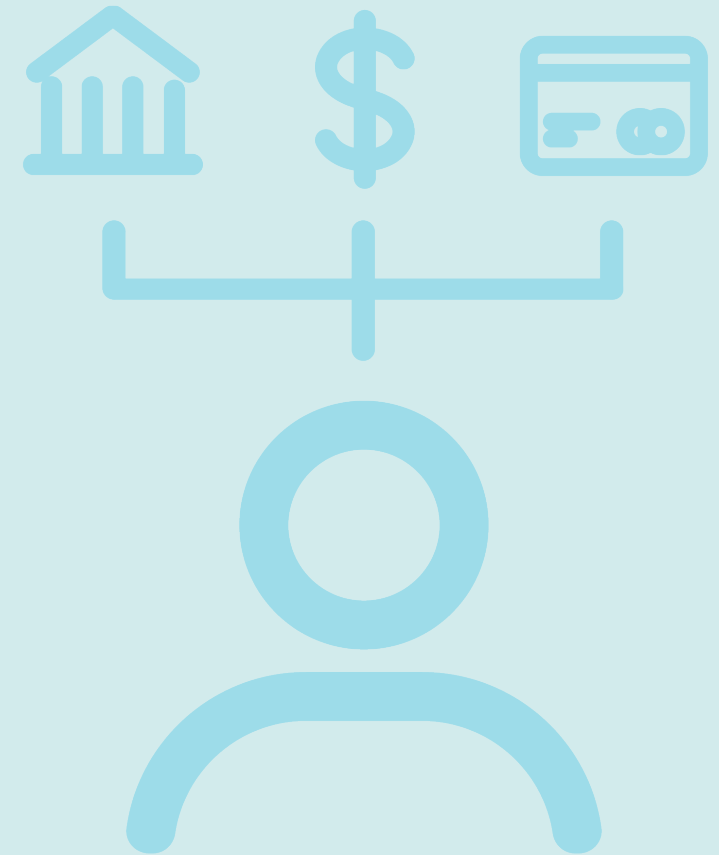
- See Module 6 for examples of different credit reports.
- The bureaus format their reports differently and have their own codes.
- Google “user guide” for each bureau to get details.
- It takes time to learn how to read these reports and how to interpret the information.
- Be patient with yourself and your clients!



is your resource for  
detailed training:  
[www.creditbuildersalliance.org](http://www.creditbuildersalliance.org)

# Given our mission...

- The credit report is a document embedded in traditional financial institutions and systems.
- Given that many people we serve are outside of these systems, their credit reports are affected adversely.
- It is important for those supporting BIPOC, underserved, and disadvantaged communities to understand the bias built into the credit reporting and financial systems.
- It is our job to help clients surmount the bias to access capital.



# Credit Infrastructure

**E**ven though these generic credit scoring systems [FICO, et al] are a vast improvement from the subjective assessments behind lending decisions made prior to 1974, they still reflect longstanding disparities in U.S. credit infrastructure. The incorporation of these disparities into credit scoring models results in communities of color, low-income individuals, young adults, and immigrants having disproportionately low credit scores, high rates of credit invisibility, or thin files.

Unscoreable: How The Credit Reporting Agencies Exclude Latinos, Younger Consumers, Low-Income Consumers, and Immigrants  
Unidos US

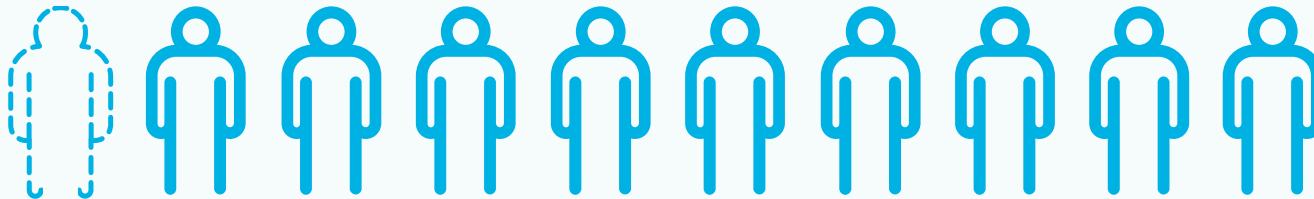




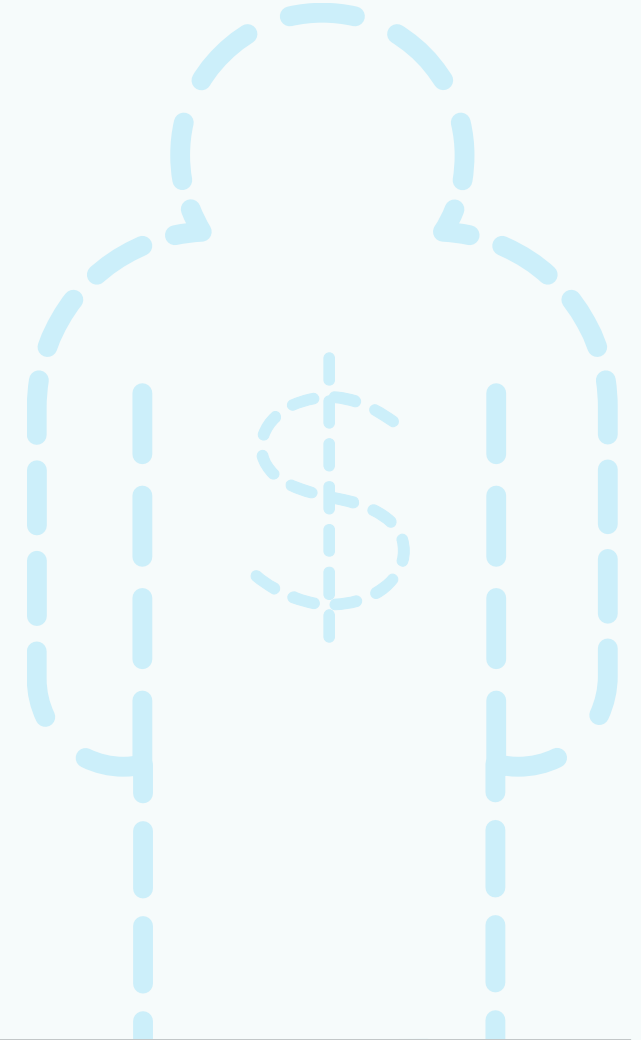
# Credit Invisible

- A person is said to be "credit invisible" if they have no credit history or report at any of the three national credit bureaus.
- The Consumer Financial Protection Bureau (CFPB) estimates that 26 million U.S. consumers are credit invisible—that's roughly 11% of the adult population.

**1 in 10 adults do not have any credit history with a nationwide consumer reporting agency.**



Consumer Financial Protection Bureau Learn more at [consumerfinance.gov](https://consumerfinance.gov)



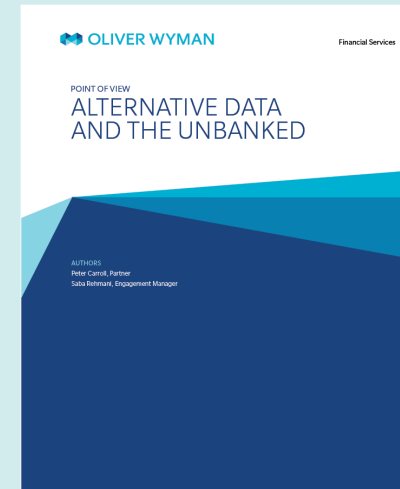
# Credit, Access, and Wealth



Poverty and Environment Center

[www.PERC.net](http://www.PERC.net)

<http://vimeo.com/43396643>



Click [here](#) to download

# Credit Invisibility Realities



**30%**

OF CONSUMERS  
IN **LOW-INCOME  
NEIGHBORHOODS** ARE  
CREDIT INVISIBLE

Consumers in low-income neighborhoods are more likely to be credit invisible. Of the consumers living in low-income neighborhoods, 30 percent are credit invisible.



**4%**

OF CONSUMERS  
IN **UPPER-INCOME  
NEIGHBORHOODS** ARE  
CREDIT INVISIBLE

In upper-income neighborhoods, only four percent are credit invisible.



**15%**

**BLACK AND  
LATINX PEOPLE**

**9%**

**WHITE PEOPLE**

About 15 percent of Black and Latinx people are credit invisible versus 9 percent of Whites.



CFPB's analysis suggests that these differences across racial and ethnic groups materialize early in the adult lives of these consumers and persist thereafter.

*May 2015, the Consumer Financial Protection Bureau*

# Wealth and net worth gap

- African Americans earn only 64 cents for every dollar earned by whites, and Latinos earn only 73 cents.
- African American families own less than seven cents for every dollar in wealth owned by white families; Latinx households own less than eight cents.
- These gaps make it far more difficult for these Americans to recover from a financial setback (or to qualify for loans in the first place).



*Past Imperfect: How Credit Scores “Bake In” Past Discrimination*  
National Consumer Law Center

# Wealth and net worth gap *continued*

- Credit history is used as a gatekeeper for many important necessities – employment, housing (both rental and homeownership), insurance, and of course, affordable credit.
- Because of poor credit histories, minority consumers are denied jobs, credit, insurance, housing and other services, or are forced to pay more.



*Past Imperfect: How Credit Scores “Bake In” Past Discrimination*  
National Consumer Law Center

# Non-traditional credit assessment

- While credit-underserved consumers have participated little or not at all in the traditional credit market, they are meeting other types of payment obligations....[such as] rent and utility services.
- Many also regularly pay for insurance, savings plans, childcare, health care, or interest and principal on alternative loans, such as payday loans.
- This final point has led many in the community development and financial services industries to look at the possibility of ... augmenting credit histories for credit-underserved consumers by collecting ... data related to alternative, noncredit-based payment obligations.



*Credit scoring and the credit-underserved population*  
*Federal Reserve Bank of Minneapolis*

# Improving Credit

- One of the most important services BDOs can offer to help improve their clients' access to capital.
- **Watch Module 11** to understand the difference between being “loan ready” and “not qualifying” for a loan.
- **View Module 12** for ideas on how to help clients improve their credit reports.





## CHAPTER 2

# Underwriting Basics (Modules 5 - 8)

**What is Underwriting?** (Modules 5)

**Five C's of Credit** (Modules 6)

**Understanding Credit** (Modules 7)

**UP  
NEXT**

**Debt Service Coverage** (Modules 8)



# ***Bridging the Capital Access Gap Modules***

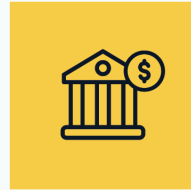


## CHAPTER 1

### **Lending Landscape**

(Modules 1 - 4)

- 
- 1** Lending Landscape
  - 2** When to Borrow
  - 3** Finding the Right Lender
  - 4** Building Relationships with Lenders



## CHAPTER 2

### **Underwriting Basics**

(Modules 5 - 8)

- 
- 5** What is Underwriting?
  - 6** Five C's Overview
  - 7** Credit
  - 8** Debt Service Coverage

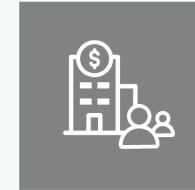


## CHAPTER 3

### **The Best Version of the Business**

(Modules 9 - 14)

- 
- 9** Quality Applications
  - 10** Startups vs Existing Businesses
  - 11** Loan Ready vs Not Qualified
  - 12** Improving Credit
  - 13** Improving Debt Service Coverage
  - 14** Collateral



## CHAPTER 4

### **Preparing for the Next Level**

(Modules 15)

- 
- 15** Preparing for the Next Level



## CHAPTER 5

### **Resources for Professional Development**

(Modules 16)

- 
- 16** Resources for Professional Development

# Thank you for joining us!

**Presenter: Susan Brown**

Business & Nonprofit Development

Microlending & CDFI Capacity Building

Online Program Design

**[susanrileybrown.com](http://susanrileybrown.com)**

## LISC

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