



# Credit Basics

## Understanding Credit

Credit has two definitions—borrowed money that allows you to purchase things, and the likelihood that you will pay back these loans and be approved to take out new ones (this likelihood is demonstrated through a credit score).

Borrowed money can take many forms, such as a car loan, home mortgage, student loan, or credit cards for product purchases.

Your credit score is determined by the three credit agencies and helps lenders determine how much money you'll be able to borrow and what interest your loans will have. The interest is additional money that you are charged and will need to pay back so the lender can profit on your loan.

## Borrowed Money as Credit

Having access to credit means you can buy something before you pay for it. This ability to borrow gives you, the borrower, flexibility in planning your purchases and makes it possible to pay for a large purchase over time—however, you also pay interest on the purchase amount, so use credit wisely, and only borrow money to make necessary purchases. Tuition can be a large expense, so many students and parents of students choose to take out loans to fill in the gap after scholarships and other financial aid have been awarded.

Some education loans, such as GradPLUS and parent PLUS loans, require a credit check. Credit plays a big role in your life, which is why having good credit, making payments on time, and minimizing your debt are so important.

# Your Credit

Creditors (and credit agencies) look at three factors to determine your credit score, which determines your eligibility for a loan. The factors are typically referred to as the three C's of credit: character, capacity, and collateral.

**Character.** How you've handled debt in the past (whether you pay bills on time, pay off lenders early, carry a balance month to month, etc.) tends to determine how you will handle it in the future. When reviewing your character related to credit, lenders look at payment history, lengths of credit history, and types of credit used.

**Capacity.** Based on your income and other debt responsibilities (credit cards, car loans, mortgage, etc.), lenders determine whether you can afford an additional loan. They also take into account amounts owed on different accounts, how much available credit you have (or if you carry a balance over from month to month), new credit accounts, and how many lines of credit you've applied for recently.

**Collateral.** As a borrower, you will often need to list collateral, or something of value (like a car, fine jewelry, or property), to secure repayment of the loan. If you cannot repay the loan, the creditor will seize your collateral as repayment.

Using these three factors, credit agencies assign you a FICO credit score, which ranges from 300 to 850. This is essentially a rating of the likelihood of you being 90 or more days past due on your bill.

In the past, lenders reviewed these three criteria simply by looking at your credit report. But now, most lenders use an electronic system that assigns numbers to your credit score. The number you are assigned dictates what type and how much credit you can receive. This technique is referred to as credit scoring. A credit score tells the lender how likely it is that you will pay back the loan and adhere to the loan terms.

## Credit Agencies and Credit Reports

To determine your creditworthiness, potential lenders will acquire your credit report from credit agencies. You have a right to request a copy of your credit report at any time and can get one for free from each agency once a year. The three credit agencies are:

### **Equifax**

P.O. Box 740241

Atlanta, GA 30374-0241

800.997.2493

[Equifax.com \(http://www.equifax.com/\)](http://www.equifax.com/)

### **Experian**

P.O. Box 949

Allen, TX 75013-0949

888.397.7654

[Experian.com \(http://www.experian.com/\)](http://www.experian.com/)

## Trans Union

P.O. Box 390

Springfield, PA 19064-0290

800.888.4213

[Transunion.com \(http://www.transunion.com/\)](http://www.transunion.com/)

# Your Credit Report

Your credit report includes the following information:

- Name
- Address
- Telephone number
- Social Security number
- Date of birth
- Place of employment
- Tax liens, judgments, and bankruptcies
- Current loan balances, original amount borrowed, amount of payment, status, and number of late payments
- All credit inquiries for the past 24 months

Negative credit reporting stays on your file for seven years, with the exception of bankruptcy, which stays on your credit for 10 years. NOTE: It is illegal for information regarding race, gender, religion, national origin, checking or savings accounts, medical history, purchases paid in full, and business accounts to appear on your credit report.

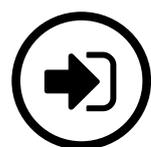
The Equal Credit Opportunity Act (ECOA) guarantees equal access to credit. It is unlawful for a creditor to:

- Discriminate on basis of sex, race, marital status, or national origin
- Ask if you are divorced or widowed
- Ask about future plans to have or raise children
- Not consider public income as reliable income
- Not consider alimony, child support, or other payments as income

It is legal to ask for some personal information on a loan application, such as:

- Name
- Telephone number
- Social Security number
- Employer
- Length of employment
- Marital status
- References
- Current income
- Prior debt
- Current debt
- Bank account balances

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