



Advancing Equity

The Power and Promise of Credit Building

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Introduction

Credit is an essential ingredient for economic security and mobility. Without a high credit score and affordable, available capital, it is nearly impossible to get by financially, let alone get ahead. Our economic system, and the American Dream it is supposed to feed, is based on the belief that anyone has access to credit and can build economic security, wealth, and intergenerational transfer.

In reality, our credit system does not serve all people equitably. We know that higher interest rates resulting from lower, invisible, or no credit scores can translate into thousands of dollars over the life of the loan, but the added costs and missed opportunities from navigating through life without a visible and positive credit score are more difficult to calculate.

People of color and immigrants work hard to build and sustain wealth. With a sense of optimism and a strong commitment to supporting their immediate families and leaving a legacy, people of color and immigrants have a long history of overcoming obstacles and achieving their financial dreams. Black people are 4 times more likely than the general population to want to start their own businesses. Latinx millennials are 1.4 times more likely to support family members financially while being more future-focused and more likely to be taking action toward their financial goals than non-Latinx millennials.¹

People of color have been blocked from realizing their high aspirations by structural racism and failures across multiple systems that have barred them from accessing and using credit and the intergenerational wealth-building opportunities access to credit makes possible. At the same time, financial systems have disproportionately encumbered people of color with debt. For instance, people without visible and positive credit scores are far more likely to be denied a needed loan or cell phone plan, get charged higher rates to borrow money, and be rejected for a job or housing. The result is even further erosion of financial stability and lower credit scores. As a consequence, these communities have been left behind in the drive to build economic security and wealth.

Philanthropy has an unprecedented opportunity to transform credit from a tool for exclusion to one that supports equity for Black, Latinx, Indigenous, Asian and Pacific Islander, and Southwest Asian/Middle Eastern/North African (MENA/SWANA) people¹ and immigrants to the United States.

This brief will analyze what is not working within our credit system and identify what philanthropy can do to reimagine a system that builds economic security and mobility for everyone, especially people of color and immigrants. An equitable credit system would create pathways to narrow the racial wealth gap instead of continuing to widen it. Solutions include nonprofit organizations and community development financial institutions (CDFIs) delivering financial products that are designed for the people who have been most excluded from the credit system, seeding their journey toward economic security, as well as systemic changes to make economic security and mobility more fairly attainable.

ACCESS TO CREDIT IS UNEVENLY DISTRIBUTED

- Those who live in predominantly nonwhite areas in more than 50 major cities are more likely to have low credit scores (below prime).²
- An estimated 45 million people are credit invisible or unscored, and Black and Hispanic individuals are twice as likely to be credit invisible.³
- Those in majority Native communities are more than three times as likely to use alternative financial services and twice as likely to have debt in collections.⁴

I This paper uses Black, Latinx, Indigenous, Asian & Pacific Islander, and Southwest Asian/Middle Eastern/North African (SWANA/MENA) and immigrants to the United States to describe people who have experienced systemic racism and economic inclusion. Where research is cited, demographic terms will remain consistent with the original research. In some instances, the term “people of color” is used to also mean Black, Latinx, Indigenous, Asian & Pacific Islander, and SWANA/MENA people. SWANA is the decolonized naming for the region of Southwest Asian/North African. However, as there may be less familiarity with this term, the paper uses SWANA/MENA.

Background

Credit's Role in Wealth

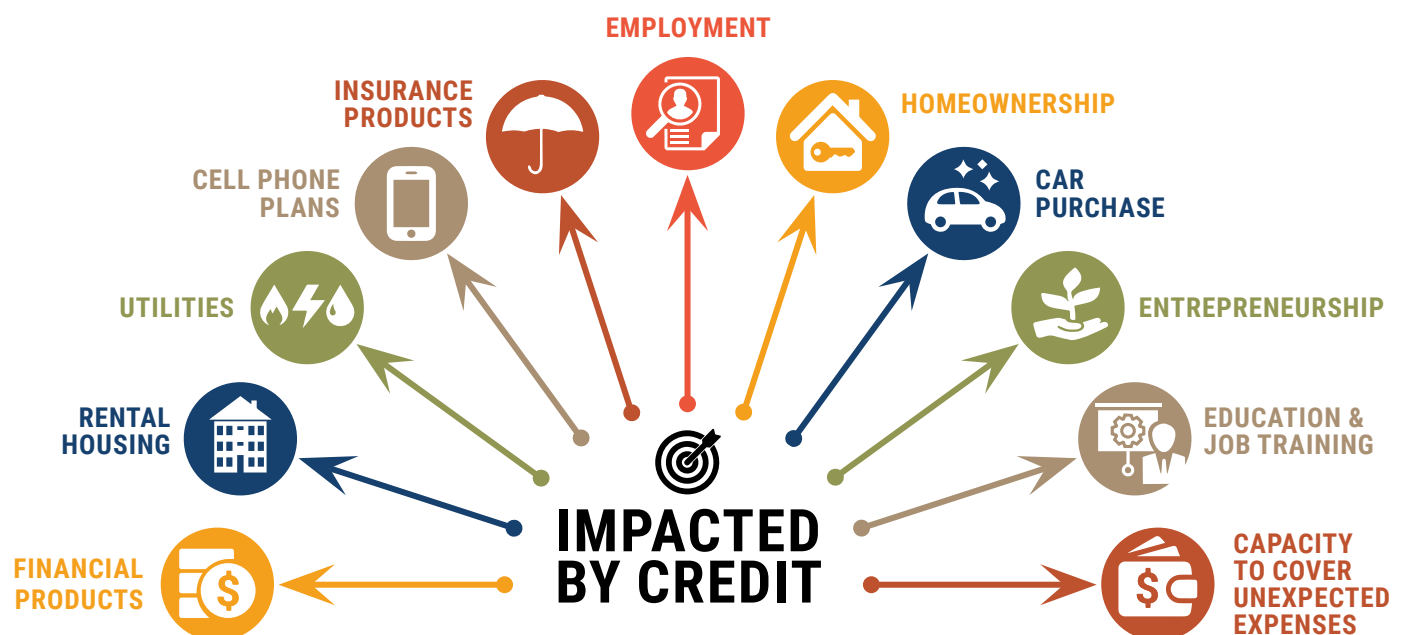
Wealth is the value of personal assets minus debts. Credit plays a role on both sides of the equation. Credit is a systemic measure of financial health, a necessary gateway for accessing other economic opportunities, and an essential ingredient for economic security and mobility. Credit scores are ubiquitous in the U.S. economy. A positive credit history and score can be leveraged at different moments throughout a lifetime—to obtain affordable financing for a home or business, rent an apartment, improve employment options, or manage a financial emergency.

As much as credit helps people get ahead, it also holds people back, especially people of color and immigrants. People who are Black, Latinx, Indigenous, Asian and Pacific Islander, or Southwest Asian/Middle Eastern/North African (MENA/SWANA) and immigrants to the United States face credit systems that have blocked access and discriminated against them in other ways for generations. Structural racism reflected in legal prohibitions, continued disadvantage, and bias across multiple systems (including credit, housing, health, employment, education, and justice)

have resulted in widening racial-ethnic wealth gaps. That bias includes how risk is conceptualized and what factors build credit.

The credit gap is reflected in the wealth gap between Black, Latinx, and White households, which is substantial and persistent. The typical White household has at least 8 times the wealth of the typical Black household and at least 5 times the wealth of the typical Latinx household.⁵ The wealth gap extends to other races and ethnicities, as well. Asian American households overall hold equivalent wealth to White households, but the big-picture number conceals huge intragroup disparities. The wealthiest Asian and Pacific Islander households have nearly 175 times the wealth of the poorest.⁶ Although data about Native American wealth is troublingly sparse, research shows that Native American households experience the highest poverty rate of any ethnic group in the United States.⁷

Staying the course will not close the gap. In fact, over the last 30 years, the wealth gap between White and Black households has grown.⁸



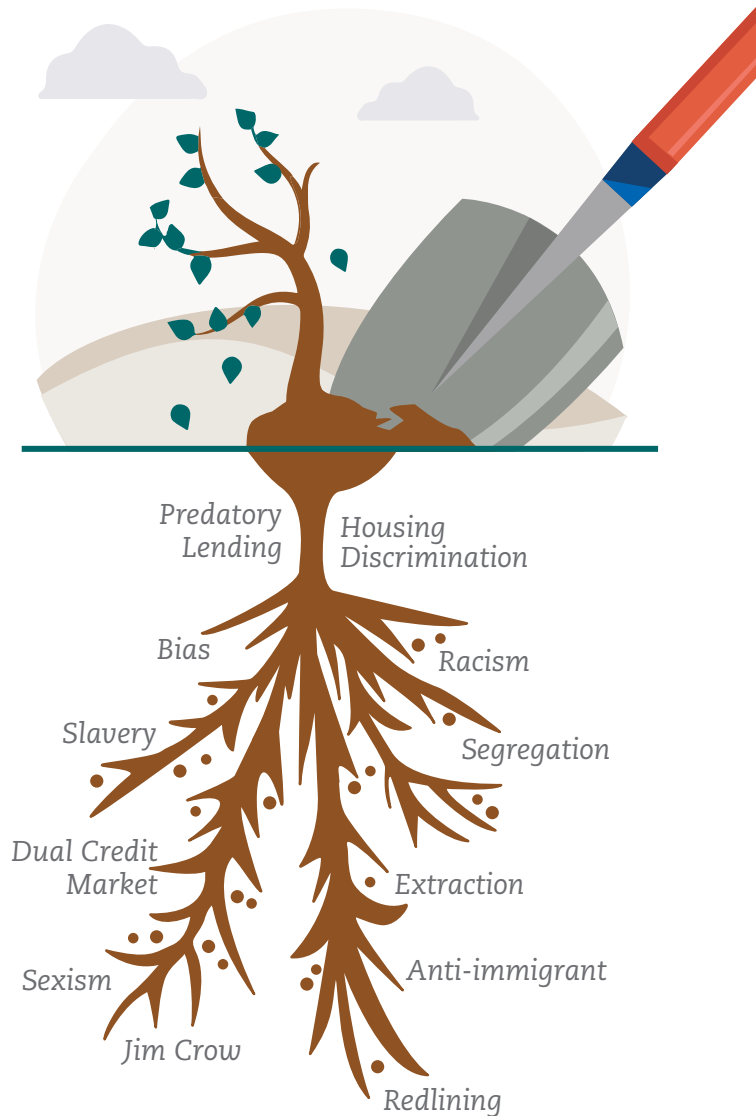
The Roots of Our Credit System

Our credit system allows people to obtain loans, goods, and services based on credit history. The risk assessment measures that enable this process have been deemed appropriate across generation, but they incorporate centuries of bias. Two key types of players are central to the development of this system: financial services companies that offer credit (regulated financial institutions, fintech companies, alternative financial services companies) and credit reporting agencies (CRAs) that warehouse and profit from individuals' financial transaction data.

CRAs sell data, in reports and as proprietary score models, to an ever-expanding base of corporate users. Three national CRAs—Equifax, Experian, and TransUnion—handle the lion's share of data, each carrying credit files on over 200 million U.S. residents.⁹ They operate with inconsistent oversight and a high prevalence of errors, which impacts individuals negatively and unfairly. The Federal Trade Commission found that one in five consumers have an error on their report, and one in twenty have errors that would result in a credit denial or higher credit costs.¹⁰

In reimagining the system to reduce harm, fixing errors in the credit system is just the beginning. Credit scores do not formally take race into account, but the associated data draw on individual borrowing and payment histories that are profoundly shaped by generations of discriminatory public policies and private practices that limited access to generational wealth.

Our credit system is inequitable by design, a by-product of a history of racialized exclusions (enacted in slavery, White supremacy, Jim Crow laws, redlining, and anti-immigrant discrimination); damage wrought by laws and industry practices that tie race, gender, and ethnicity to higher loan risk; and self-reinforcing "neutral" credit assessments that continue to disadvantage people of color.¹¹



These disparate impacts are significantly rooted in housing discrimination and the dual credit market that resulted from it. Established in the 1930s, the Home Owners Loan Corporation (HOLC) provided mortgages predominantly to White people and institutionalized redlining to discriminate against communities of color. HOLC, the Federal Housing Authority (FHA), and the Veterans Administration (VA) continued this discrimination through the 1960s.¹² These federal policies and practices result in high homeownership rates (and better credit scores based on the mortgage and building equity) for White people and higher rental rates for people of color (who could not get mortgages and in many cities were subjected to fraudulent lease-to-buy arrangements that did not build equity). They also resulted in segregated neighborhoods whose access to any affordable credit at all was limited.

Similarly, formal business capital was primarily granted to White men by law until the late 1980s, when access for women was expanded. By practice, business capital continues to be concentrated among White men: 82% of small businesses are owned by White people, and 65% are owned by men. White-owned businesses were 1.5 to 2 times as likely as Black- and Latinx-owned businesses to use bank financing in the past five years.¹³

These impacts are amplified by credit assessments that reinforce bias in the choice of data they include or exclude. Mortgage payments count, but rent payments do not in most cases. Formal business loans are included, but informal credit such as lending circles, which are commonly used by immigrant people, have not been. Utilities are included only when the individual defaults. Credit cards have a more positive impact on credit scores when the utilization rate is lower—a status generally more associated with people who have higher income and greater wealth. On the other hand, high credit card balances, higher-cost debt, use of alternative financial services, and medical debt can create a cycle of low credit scores, higher costs for credit, and debt turmoil. In other words, decades of discrimination have created a system that disproportionately sees Black and Latinx people as risky or invisible.

Even as overt discrimination has begun to be addressed, the system's legacy of discrimination continues to have outsized consequences for people of color. That legacy manifests in lower credit scores for non-White people, differences of up to 100 points in average credit scores between predominantly White and non-White areas.¹⁴ Lending and other credit decisions rely on those current scores, perpetuating the inequities that created them.

A low credit score brings a range of impacts that affect not just economic security, but nearly every financial decision.

Lack of access to a credit system that accurately measures risk and risk tolerance is both a symptom and cause of the racial-ethnic wealth gap. Without the ability to borrow and invest affordably, many people of color and immigrants continue to struggle to translate income into wealth. The compounding effects of generations of exclusionary and harmful policies and practices continue contributing to the racial-ethnic wealth gap.

Investments in credit building, safe and affordable credit access, and systemic change are needed to counter the persistent lack of access.

CONSIDERATIONS FOR ASSESSING CREDIT

Positive Impact on Credit

- Mortgage Payment
- Formal Business Loans
- Credit Cards with Low Balances

No Impact on Credit

- Rent Payments
- Lending Circles
- Utility Payments

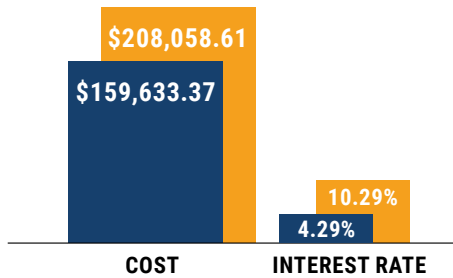
Negative Impact on Credit

- High Credit Card Balance
- Alternative Financial Services
- Late Utility Payments
- Medical Debt

THE COST OF A LOW CREDIT SCORE

■ HIGH CREDIT ■ LOW CREDIT

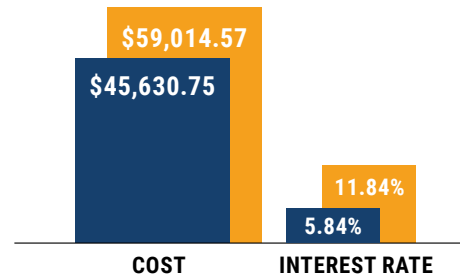
UNDERGRADUATE DEGREE



Low credit could cost you an additional

\$48,425.24

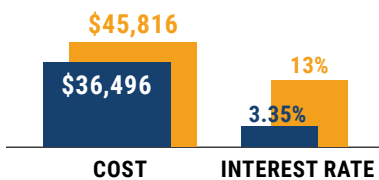
GRADUATE DEGREE



Low credit could cost you an additional

\$13,383.82

CAR



Low credit could cost you an additional

\$9,320

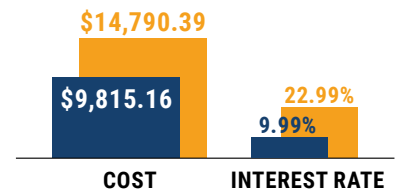
APARTMENT



Low credit could increase your security deposit by an average of

\$1,006

CREDIT CARD



Low credit could cost you an additional

\$4,975.23

HOMEOWNERS INSURANCE



Low credit could cost you an additional

\$590.50

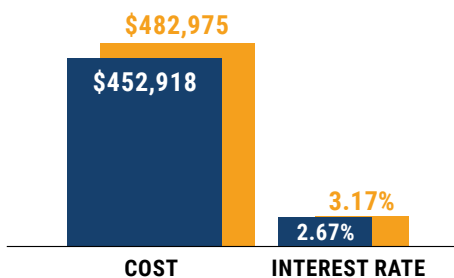
CAR INSURANCE



Low credit could cost you an additional

\$1,374.10

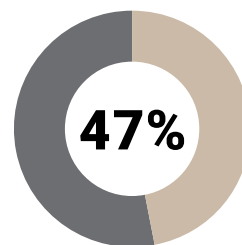
HOUSE



Low credit could cost you an additional

\$30,057

JOB



of employers run credit checks on new hires.



unemployed Americans have been denied a job due to negative information on their credit reports.



The Current Context

Continued discrimination against, divestment in, and extraction from communities of color leads to credit invisibility and low credit scores. Since the Great Recession of 2008, 93% of all bank closures have been in low-income communities made up primarily of residents of color.¹⁵ Given that banking services are critical entry points to affordable credit and capital distribution, this trend has contributed to the rise of “credit deserts” across the United States.

To fill the void for capital, an unregulated alternative financial service industry has grown up that replaces traditional banking services with high-cost financial products. This industry primarily serves communities of color and immigrants who have no other options. Credit products from alternative financial service providers typically do not give borrowers credit for positive payments. However, they are likely to report delinquent ones. The business models of these lenders perpetuate a cycle in which a consumer borrows more funds to repay the loan. The models also include aggressive collection practices—debt in default is sent to collections or to court, for a default judgment, negatively impacting credit scores, and forceful collection efforts, including garnishments, bleed away needed savings and household income. Credit from alternative financial service providers thus adds to credit score disparities, both due to the costs of the credit and the aggressive, intentionally disruptive collection practices.

Limited access to safe and affordable credit and debt is damaging in three ways: it erodes income, deters accomplishment of financial goals, and severely constrains asset accumulation, limiting the ability to start a small business or buy a home. Those with limited credit access often have little choice but to turn to costly options from alternative financial services providers such as payday lenders, car title lenders, rent-to-own stores, and pawn shops. Without access to a system that allows them to build wealth gradually and affordably over their lifetimes, people of color and immigrants are consigned to this dual

track of costly credit options and limited opportunities for asset building. These choices, in turn, impair financial security and upward mobility.

Disparities and discriminatory practices contributing to lack of access are interconnected across credit scores, bias, alternative financial services, and debt.

Internalized Barriers

The dominant financial narrative of personal responsibility has two destructive effects: it fails to acknowledge the structural and intergenerational barriers to access that are outside an individual person's control, and it reinforces the internalization of negative beliefs and feelings of self-doubt and shame.³⁴ In reality, the financial system provides limited access to safe and affordable credit products to people of color because of interrelated barriers and biases rooted in structural inequities—not individual choices and actions. People excluded from the credit system face misinformation from a variety of sources³⁵ and psychological barriers from decades of discrimination, impeding access to safe and affordable credit-building opportunities.³⁶

To make way for more equitable wealth-building opportunities to use credit as a powerful tool, credit building requires new access pathways through the sticky web of alternative financial services, credit scores relying on the wrong measures of risk, and spiraling debt (including from government and the courts). Funders can make the environment more equitable both by expanding access to affordable credit products and by providing navigational support as they act to invest in a reimagined, just credit system.

CREDIT SCORES

THE CFPB REPORTS

approximately **1 out of 10** or **26 million** adults



are considered to be “credit invisible,” meaning they have no credit history because they do not have credit cards, loans, and other lines of credit.

Another **19 million** have a credit record but no score because their history is **too thin** or **out-of-date**.¹⁶

FICO SCORES REVEAL

11.1% of American consumers have **poor scores**.¹⁷

INDIVIDUALS WITH SUBPRIME FICO® SCORES (UNDER 620) BY RACE:



Black



1 in 9 Latinx



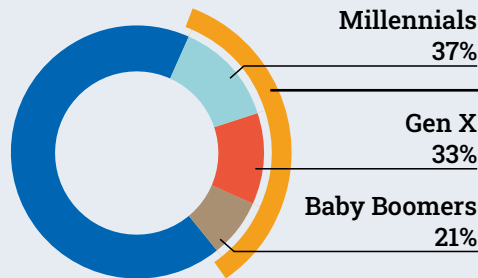
1 in 2

individuals in predominantly **Native American** communities.¹⁹



only **1 in 19** White individuals.¹⁸

SUBPRIME SCORES IMPACT YOUNGER GENERATIONS



34.8%

of Americans have subprime FICO scores **between 580 and 669**.²⁰

PEOPLE IN LOW-INCOME AREAS

are

240%

more likely to become credit visible due to a negative record such as an item in collections.²¹

Credit scoring models can be between **5 AND 10% LESS ACCURATE FOR PEOPLE OF COLOR AND PEOPLE WITH LOW INCOMES** than White people and people with higher incomes.²²

BIAS

IN 2020,
AN ESTIMATED

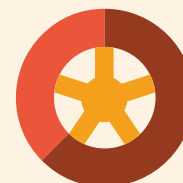
24%

of adults who applied for credit within the last 12 months from mainstream lenders **were denied or approved for less than requested**, with much higher denial rates for people with **lower incomes and Black (51%) and Latinx (46%)** people.



ALMOST HALF of credit applicants with incomes **below \$50,000** experienced denials.

At every income level, **BLACK AND LATINX** applicants were denied credit at approximately **TWICE THE RATE** of the White population.²³



PEOPLE OF COLOR SHOPPING FOR CARS

who are **more qualified** than their White counterparts are **62.5%** more likely to be offered costlier pricing options—**adding up to \$2,662 in extra fees and interest** over the life of the loan.²⁴

ALTERNATIVE FINANCIAL SERVICES (AFS)

IN 2019,
an estimated **5%**
of households

USED HIGH-COST NON-BANK CREDIT

(i.e., rent-to-own service or payday, auto title, pawn shop, or tax refund anticipation loan).

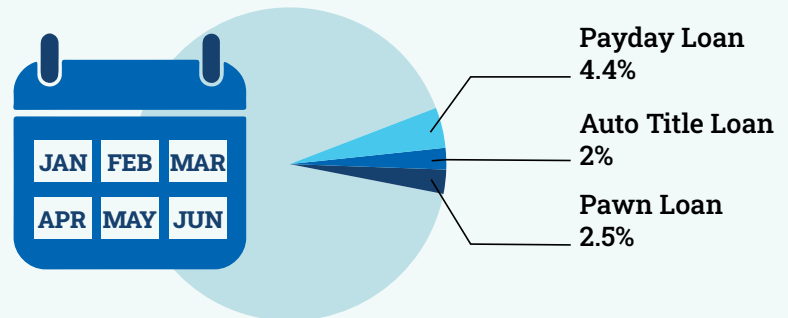
Black & Latinx households were **10% more likely** to use non-bank credit than White households.²⁵

ANNUAL PERCENTAGE RATE (APR)

391% TYPICAL
PAYDAY
LOAN

15% AVERAGE
CREDIT
CARD²⁷

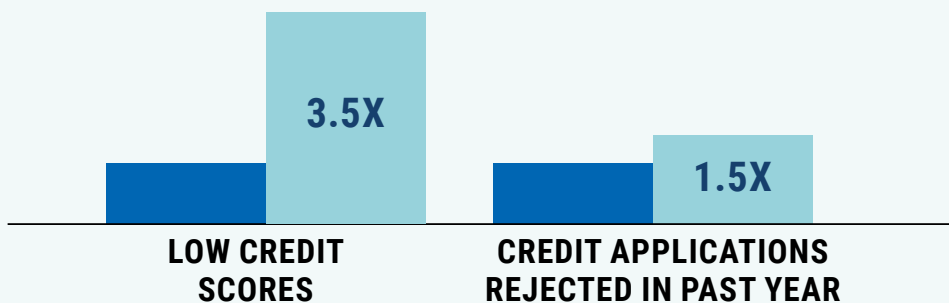
LOANS TAKEN OUT DURING THE FIRST HALF OF 2019²⁶



CONCENTRATED USE OF AFS

■ Non-AFS Users

■ AFS Users



Use of AFS is more concentrated among **Black and Latinx** people.

ALTERNATIVE FINANCIAL SERVICES COSTS

On average, payday loans of \$300 cost the borrower \$500 over a few months in fees and interest,²⁸ stressing that household's tight budget, leading to cycles of debt, and hampering access to safe and affordable credit.

USED BY
12 MILLION
HOUSEHOLDS
ANNUALLY

64% HOUSEHOLDS
SURVEYED THAT
STRUGGLED WITH FINANCIAL
HEALTH IN 2020

\$255 billion spent on fees and interest on everyday financial services, including bank and non-bank services.

BLACK & LATINX CONSUMERS

are approximately **3 TIMES MORE LIKELY** than their White borrowers to use high-cost forms of credit, including payday loans and pawn shops.²⁹

DEBT

The level of debt, including accruing interest relative to the available credit and income, reported to a credit bureau **reduces a credit score**, as does **high balances, late or missed payments, or collections**. For example:

BLACK HOUSEHOLDS

ARE 10% MORE LIKELY

to have student loan debt than white households

WITH
BALANCES

\$7,000

greater than White households³⁰

FOR RECENT COLLEGE GRADUATES

\$30,000 is the average student loan debt³¹

The **balances** as well as **any problems repaying** could negatively impact credit scores.



GOVERNMENT FINES AND FEES

create unaffordable debt that affects people with low incomes and people of color.³²

UNPAID FEES IN COLLECTIONS,

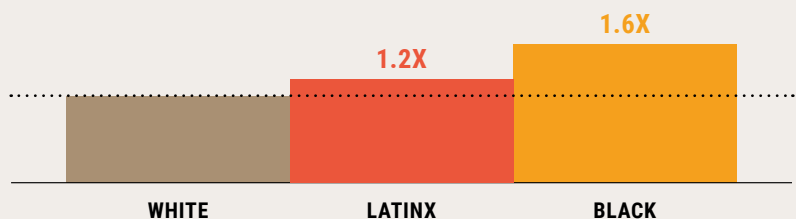
in or outside of the judicial system, can be reported to credit reporting agencies and increase the unpaid debt total.



AT LEAST
\$88 BILLION
IN MEDICAL
DEBT

was reported in consumer credit records as of June 2021

LIKELIHOOD OF MEDICAL DEBT



PEOPLE WITH LOW INCOMES ARE 2.8 TIMES MORE LIKELY to have difficulty paying medical bills than people with incomes over \$100,000.³³ Recent reforms **delay** the reporting of this debt for a year; the impact is as yet unknown.

What is Credit Building?

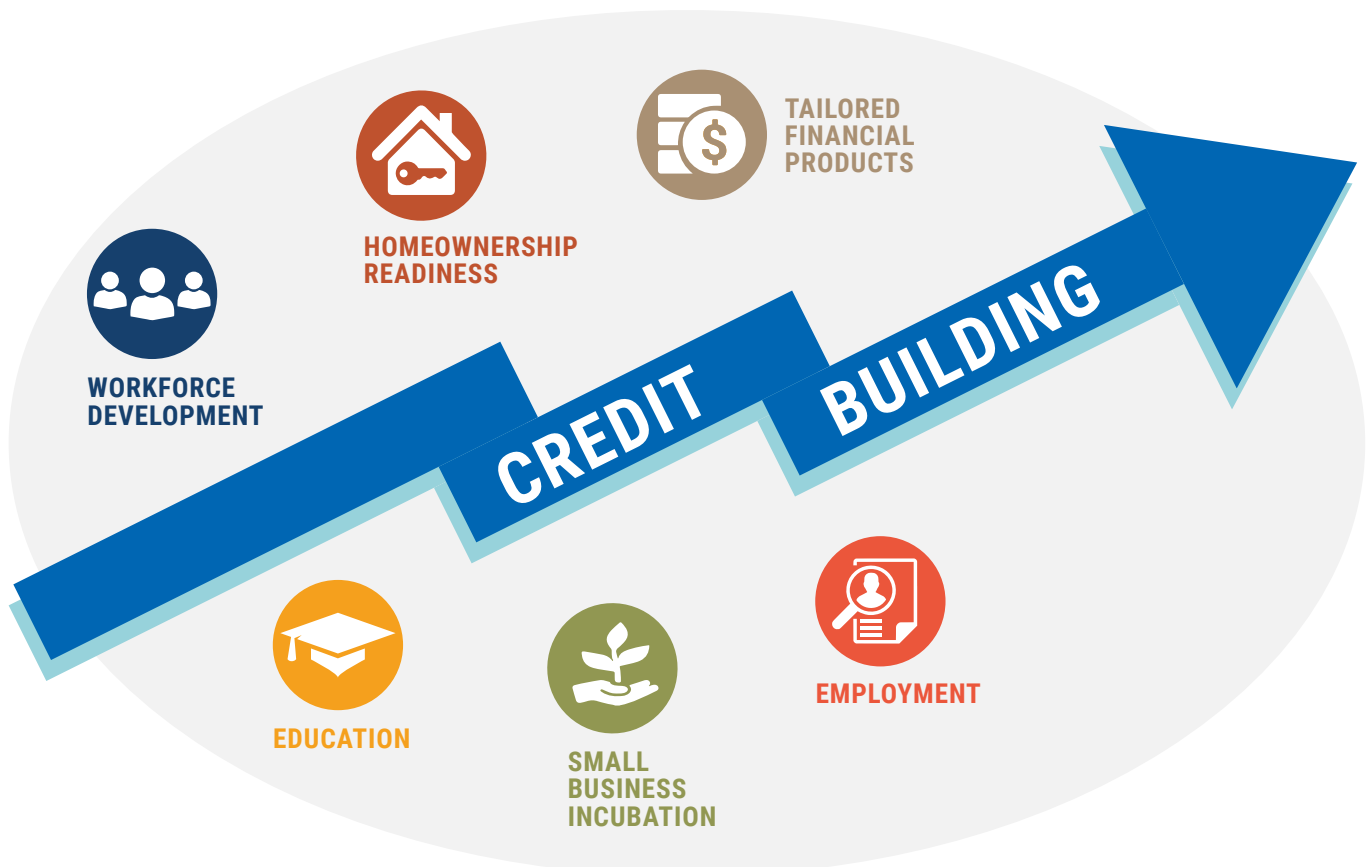
Equitable credit building expands access to credit for people of color and immigrants who have been excluded from the credit system for far too long.

Active use of traditional credit-building products that rely on the creditor's report of monthly payments is essential to any individual's ability to establish, improve, and sustain a traditional credit score and expand credit choices. A track record of using and managing credit products makes up credit history, and enough traditional credit history begets a credit score. A prime credit score—and low-risk status—is the result of time and positive payments. But the traditional products reflect choices tied to past and current systemic discrimination.

With the systemic challenges people of color and immigrants continue to face in accessing credit, credit building must go beyond the traditional definition to overcome the barriers and expand access to credit.

Credit building for people who are excluded from traditional reporting (for instance, renters), who have no credit record, or who have a negative record requires more than establishing a new record of on-time payments; it also necessitates understanding the rules, managing debt carefully to maximize credit-score impact, and avoiding credit repair scams.¹¹ Credit building with an equity lens is a tested intervention offered by community-based organizations and others in the financial services industry that has yielded relatively quick, yet impactful results. It is future and hope oriented and strengths based.

Credit-building programs are often linked to housing, employment, and other economic security programs, as the table on page 14 illustrates.



CREDIT BUILDING ACROSS NONPROFIT SECTORS

	Education, Workforce Development and Employment	Affordable Housing and Homeownership Readiness	Small Business Incubation and Pre-Development	Population-Tailored Financial Products and Services
The power of credit	Improves ability to pay for training and education, reducing barriers to well-paying jobs	Increases housing options for renters and homeowners	Provides access to capital at planning, start up, and expansion	Improves access to quality, affordable credit products for excluded populations
Specific instances in which credit is used	<ul style="list-style-type: none"> ▪ Qualifying for some student loans ▪ Paying for a certification or job supplies ▪ Passing an employer credit check ▪ Acquiring a reliable car in good repair to get to work 	<ul style="list-style-type: none"> ▪ Accessing housing ▪ Passing tenant screening ▪ Reducing security deposit amounts ▪ Qualifying for a mortgage and getting a lower rate ▪ Applying for homeowners insurance ▪ Opening utility accounts 	<ul style="list-style-type: none"> ▪ Accessing capital for startup and ongoing financing for expansion ▪ Renting a business space ▪ Acquiring or financing equipment and materials, production, and inventory storage ▪ Weathering economic shocks ▪ Managing cash flow ▪ Attracting investors ▪ Establishing a business credit profile 	<ul style="list-style-type: none"> ▪ Accessing consumer credit (loan or credit card)^{III} ▪ Avoiding predatory options ▪ Addressing where traditional risk assessments discriminate ▪ Increasing the ability to address unexpected costs affordably
Case study examples	Working Credit offers credit coaching at colleges and employers.	Foundation Communities offers affordable housing, rent reporting, and credit-building education to tenants.	Change Labs prepares offers for business development support and financing to Native entrepreneurs.	International Rescue Committee's Center for Economic Opportunity and The Fountain Fund offer culturally responsive, safe financial products to refugees and justice-involved individuals, respectively.

III Establishing direct relationships with credit-reporting agencies to purchase soft-inquiry consumer credit reports allows programs to offer consistent and inclusive access, especially for those without social security numbers or impacted by the justice system, who experience barriers to accessing credit reports and scores online.

The Opportunity for Philanthropy

Rooted in systemic inequities, today's milieu includes persistent racial-ethnic wealth gaps and disparities in various markers of financial security (e.g., savings rates, debt levels, and credit scores). This backdrop urgently demands radical change in our credit system. As part of reimagining the system, pathways must be created to level the ability to access credit.

Systems change efforts provide an opportunity to disrupt and confront racialized inequities while investing in efforts towards a more inclusive credit system. Funders, working with a range of stakeholders, can ensure that everyone has equitable access to quality and racially just credit opportunities by investing in and advocating for a more inclusive credit system. Such a reimagined system is a critical ingredient for equitable wealth building and economic security.

At the same time, people who have historically been excluded from credit building need help now with access to safe and affordable credit products and guidance

to navigate the existing system. Community-based strategies offer tangible ways to help people navigate our current credit system and build higher credit scores.

Asset-building grantmakers have the opportunity to shift the paradigm of credit, from a tool of exclusion to a tool of opportunity and greater economic equity for people of color and immigrants in any community. That opportunity includes balancing investments in on-the-ground credit-building strategies that provide near-term relief and policy-change efforts that transform our credit system over the long term.



Promising Credit-Building Programs

Nonprofits and community development financial institutions (CDFIs) with credit-building programs play a critical role in helping people of color and immigrants to both access safe and affordable credit and navigate the credit system.

With close ties to local communities, these organizations craft programs that incorporate the community's strengths and existing practices, such as through trust-based lending and community wealth building.

The [appendix](#) features case studies of programs from seven diverse nonprofits that are working on the ground to improve the economic security of people who have historically been locked out of the credit system. The programs provide a range of direct and indirect safe and affordable products: small-dollar loans, credit-builder loans, and loans for asset building. They also include attempts to affect the credit score system through affirmative actions ranging from rent reporting to culturally appropriate lending.

The case studies illustrate how to design and deliver credit-building programs for specific populations. Together, these nonprofits have demonstrated that a combination of relationship building, trustworthy and relevant information, and access to quality products can not only positively impact participants' finances and confidence in a short amount of time but also influence community and system-level changes. People affected include Native entrepreneurs, renters living in affordable housing, formerly incarcerated individuals, immigrants and refugees, and people of color.

Each case study offers an evidence-informed credit-building program with quality, culturally responsive products and financial coaching. At the same time, each nonprofit is informing or working directly on system changes by centering the lived experiences of their participants in solutions. Holistic credit-building programs that center individuals' needs and goals for economic security include four core components:



Access to credit products that are vetted and do not use traditional factors, such as credit, to determine eligibility, and take a relationship-based approach to supporting borrower success.



Culturally responsive interventions with coaching and information sharing that is relevant to participants' needs.



Client outcomes and data tracking mechanisms that build the evidence base needed to understand the impact that any given strategy has on participants' lives.



Systems change efforts through community organizing, cross sector collaboration, and advocacy reflecting participant centered design, avenues for participant leadership, data collection, and story sharing to counter harmful narratives.

Funder Recommendations

This section is a call to action for funders to invest in strategies that support families directly via credit-building programs and seed larger systems change. Funders can introduce strategies to new communities, expand the reach of equitable credit tools, and creating sustained change to advance equity through access to credit. Specific recommendations include:

1. FUND PROGRAMS IN THE COMMUNITY to ensure access to safe and affordable credit for Black, Latinx, Indigenous, Asian and Pacific Islander, MENA/SWANA, and immigrant people in the short term, with the understanding that supporting individual change is a long-haul investment. Nonprofits that offer credit-building programs, including racial equity–driven credit unions and CDFIs, create critical access to high-quality credit-building opportunities; provide guidance, credible information, and culturally responsive interventions in specific communities; and counteract predatory products with safe and affordable credit options.

Funders can support local programs by:

- Exploring with grantees how to design and implement nontraditional products to match the needs of the community.
- Prioritizing community-centered programs that share decision making and build feedback with those most impacted into the process.
- Targeting funding to organizations with deep expertise and lived experience in, and meaningful ties to, the communities they serve.
- Providing multi-year funding to organizations, especially those led by people of color.
- Facilitating collaboration and integration of credit building within workforce development, small business development, housing, reentry programs, and unions or large employers to expand reach.
- Elevating research and evaluation that includes local data disaggregated by race to inform program design and delivery and enables the efficient tracking of longitudinal credit and wealth outcomes data disaggregated by race to ensure equitable impact.

As an example of a community-centered program, Boston Builds Credit, which aims to reduce the racial wealth gap

in Boston, uses a community advisory council of Boston residents who receive paid stipends to inform its strategy and policy agenda, provide feedback, and build a pipeline for resident participation across all governance committees.

2. SCALE A SUCCESSFUL PROGRAM TO OTHER COMMUNITIES. Grantmakers can support the expansion of credit-building programs that meet participants' needs and create positive outcomes by scaling promising practices and increasing the capacity of the organization that honed the practices. For instance, Working Credit's plug-and-play program expands wealth-building opportunities by integrating credit building into partnerships with employers, community colleges, and other institutions.

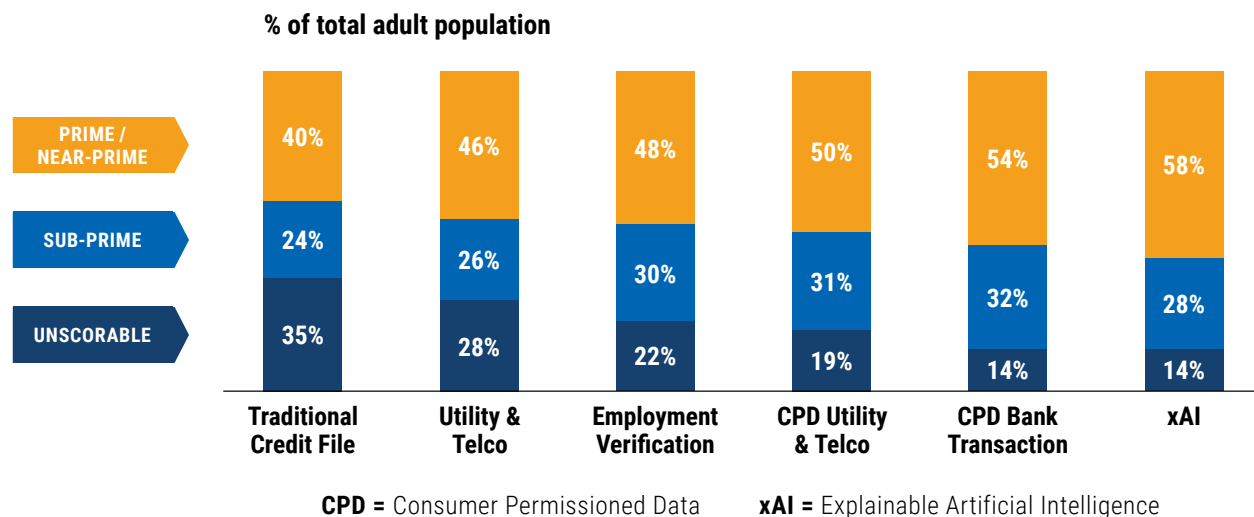
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When scores increase and people are able to take steps towards their goal—whether getting a car loan at a low interest rate, renting an apartment, getting a mortgage, etc.—it starts to open up the social imagination that other things are possible—starting a small business, helping friends and family do the same thing, . . . and just having the confidence it can happen is really important.

KRISTIN SCHELL
Chief Program Officer, Working Credit NFP

MORE DATA HELPS REVEAL OPPORTUNITIES

When you layer in alternative credit and consumer-permissioned data, you get **21% MORE SCORABLE CONSUMERS.**



SOURCE: Equifax Data & Analytics

3. ADVANCE SYSTEMIC CHANGE THAT BENEFITS CONSUMERS IN THE SHORT TERM using nontraditional risk measures or by innovating with the application of credit-score methodologies. Providing more access to credit for more Americans requires altering policies and practices. As it is now, the predominant credit-scoring model leaves out many people who are creditworthy but lack traditional proof.

Funders could support products that include the responsible use of nontraditional credit inclusion strategies, such as lending circles or rent reporting through fintech companies for mortgage qualification.³⁷ Ways to support the responsible use of nontraditional credit include investments in technology and innovation, as well as evaluation to make the case for scaling promising practices and assure that the impacts of inclusion do not have unintended deleterious consequences for people of color and immigrants.

On a national level, funders could sponsor research, pilots, and advocacy related to new risk assessment models that expand the use of nontraditional data (bank account information or rent and utility payments, for instance) to increase access and inclusion for consumers previously excluded from the financial system.

4. ADVANCE BIG SYSTEMIC CHANGE THAT FUNDAMENTALLY RETHINKS THE USE OF THE CREDIT SCORE. To counter historical and current exclusion from credit for wealth-building opportunities, many credit-building programs are redefining loan qualification guidelines to reduce dependence on credit in underwriting. For instance, character/relationship-based lending considers someone's involvement and ties to a community or reputation, rather than relying heavily on financial criteria. This underwriting practice has been gaining some traction in the nonprofit small business lending space.

Funder investments could provide capital investments to support character-based lending. Funders could also support evaluation to document success, which in turn could be leveraged for scaling and narrative change efforts as a way to address inequities and provide culturally responsive lending.

As an example, with funding from the CDFI Fund, banks, and private foundations, the multistate International Rescue Committee's Center for Economic Opportunity (IRC-CEO) built a responsive, trust-based, and data-driven lending program for refugees. Acknowledging inequities in credit algorithms, IRC-CEO considers borrowers' cash-flow position, including assessment of income volatility, to

determine product eligibility rather than using traditional credit-scoring models. To support borrower success and counterbalance some expected financial turbulence, IRC-CEO incorporated automatic payments and other mechanisms. IRC is the leader in refugee credit building among the nine national nonprofits resettling refugees.

Another way to increase inclusion in wealth-building opportunities is to ban or limit the use of credit scores for non-lending purposes, such as employment or insurance pricing. Funders could spark new or support current state or local policy efforts involving advocates, credit-building organizations, community members, and policymakers to remove the role of credit in decision making and pricing not directly related to a financial transaction. To date:

- Eleven states and three cities have banned or restricted the use of credit in employment decisions.³⁸
- Four states have successfully ended the use of credit scores in the calculation of auto insurance premiums.³⁹
- Other localities have banned landlords from rejecting applicants due to low or no credit scores.⁴⁰

On a national level, funders could support research and advocacy that reimagines the privately controlled credit reporting system as one that reduces harm, centers equity, and is more responsive and accountable to consumers. One emerging idea is to create a publicly run credit reporting agency within the Consumer Financial Protection Bureau.⁴¹ Other policy agenda items include limiting the reporting of negative information, safeguarding consumer data, and reducing bias within the credit reporting system. More evaluation and research using disaggregated credit score and wealth data by race are needed to identify innovative system change that targets inequities, scales effective interventions, measures longitudinal impact, and ensures that change is happening equitably.

5. SUPPORT OR DEVELOP PROGRAMS AND ADVOCATES AND USE YOUR INFLUENCE TO EXPAND AFFORDABLE LENDING. Increasing access is about both seeding affordable programs and weeding out predatory products and practices.

To increase access to affordable lending programs, funders can help capitalize community lenders, credit unions, and CDFIs committed to rectifying a credit desert. This capital

investment will help individuals simultaneously build credit or gain loans to acquire assets—via quality, affordable products rather than high-cost, extractive products—and expand wealth. Funders can assert leadership by taking the opportunity to support programs that offer affordable credit to traditionally excluded communities in a number of ways, including providing operating funds; long-term, affordable capital; program-related investments, and risk mitigation investments:

- To compete with alternative financial services companies and very high interest credit cards, organizations need operating funds for general capacity, relationship building, technology, and visibility.
- Capital investments might include contributing to loan funds, making capital injections into a CDFI with flexible lending terms, or providing a grant to buy down interest rates to lower the costs of loans.
- Program-related investment and other grantmaking strategies could shape partnerships between nonprofits and financial institutions or fintech companies to ensure that credit-building products and other technological innovations are equitable and inclusive.
- For risk mitigation, funders could consider investing in an organization's loan loss reserve or a loan guarantee pool to help it scale, be flexible, absorb risk, and support organizational sustainability. Risk mitigation is particularly important for risky but vital products, such as affordable small-dollar loans, which have low profit margins and often higher losses than other credit-building products.

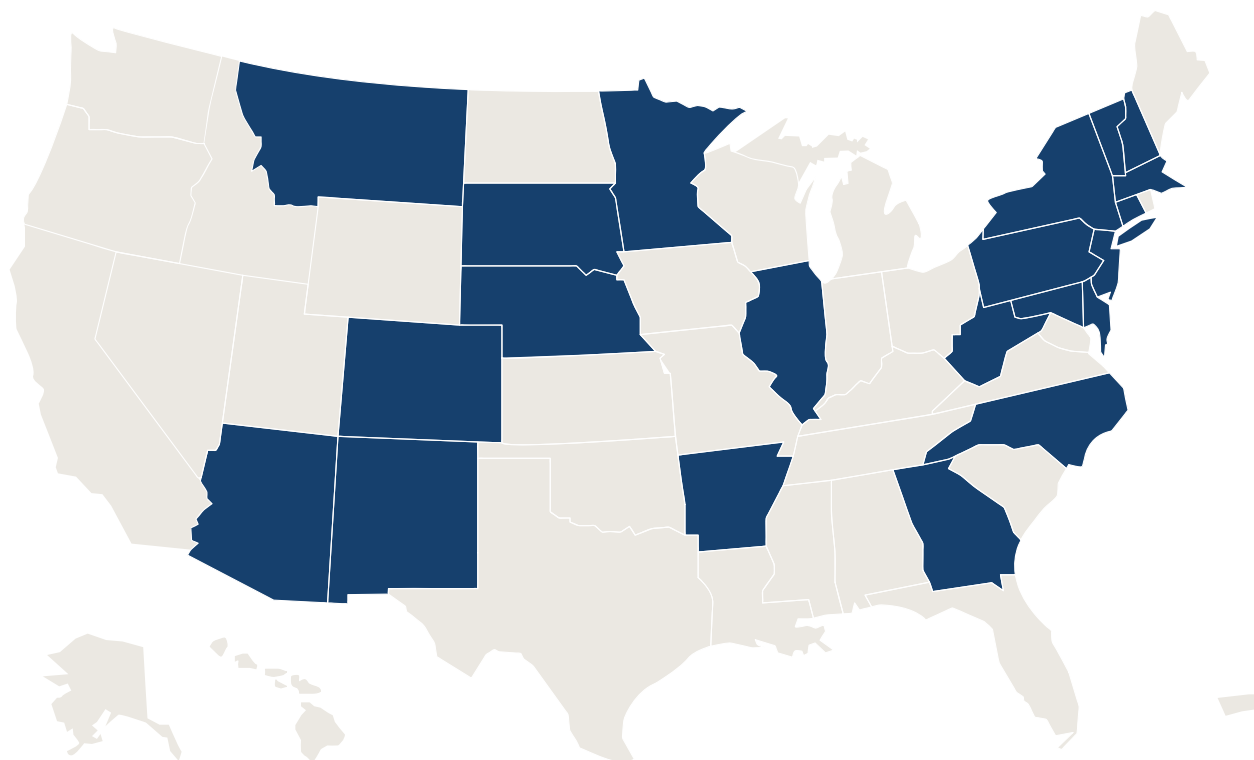
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Funders can collaborate and support innovation and systems change to ensure that families aren't held hostage by a system that was never designed with them in mind.

RAQUEL HATTER
Kresge Foundation

STRICTER STATES

20 STATES HAVE INTEREST RATE CAPS OF 36% OR LESS ON \$300 CONSUMER LOANS (12/31/21)



SOURCE: Center for Responsible Lending; staff research

To decrease access to predatory products and practices, funders can support legislative reform to cap interest rates and reduce high-interest rate debt. In spite of existing consumer protections, improvements are needed to make our credit system more just and safer for everyone—especially people of color.

On a state level, funders could support advocacy campaigns and associated data collection to restrict predatory products or practices through interest-rate caps. Several states have passed legislation to curb predatory lending. In Ohio, research shows that such reform is

correlated with borrowers turning to safer and more affordable options.⁴² There is opportunity to learn from jurisdictions with pioneering legislation and to support more of it.

Inequities in credit scores and debt burdens are intertwined. Debt loads are heavier for people of color due to higher interest rates, justified under traditional credit scoring with its embedded bias and coupled with additional fees. The combination can be especially dangerous for people of color who have low or variable incomes. Debt can erode economic security and impede opportunity.

Nonconsensual debt, such as fines and fees, and medical debt, both of which disproportionately impact people of color, can negatively impact credit scores if they result in court collections or judgments. Outdated credit models that overestimate the predictiveness of medical debt as a risk factor, as well as the additional burden of fees imposed when the debt is reduced to a judgment, further thwart credit access.⁴³

To help mitigate the harmful impacts of debt, funders can support reforms to the judicial debt collection system and the health care coverage system, or invest in preemptive debt relief funds like RIP Medical Debt.

6. CREATE BROAD EMPATHY AND UNDERSTANDING AND REDUCE INDIVIDUAL FEELINGS OF LOW SELF-WORTH THROUGH NARRATIVE CHANGE EFFORTS. The belief that “hard work alone changes outcomes” is prevalent within society. This conviction dismisses historical and current racist systemic policies and can degrade people’s self-confidence, rather than boost it.

To address this broadly shared misconception, narrative change efforts can help shift beliefs about deservedness and worthiness related to credit. Funders can engage with and invest in intentional campaigns with organizations or communities seeking to shift the credit and wealth-building narrative to one that focuses on systems change to increase opportunity and prosperity instead of blaming wealth inequity on personal responsibility. Even for organizations or leadership not yet there, funders can encourage reflective efforts that dismantle harmful narratives.

Along with direct investments in narrative change campaigns, grantmakers can fund or elevate associated research to inform those efforts. More information is needed to make the un- and undercounted visible and disaggregate data by race to understand who has been impacted by structural inequities and to what degree.





Conclusion

Access to credit is an asset that allows people to pursue economic opportunity and enhance financial security. However, access to credit occurs within a system built upon the foundation of structural racism.

History shows us that, left to its own devices, the credit system will continue to perpetuate the racial-ethnic wealth gap. To break this cycle and create true equity, funders and their grantees will have to work together on a multitude of fronts simultaneously. Ultimately, reenvisioning a fairer credit system will involve cross-industry efforts and collaboration across funders, nonprofits, financial institutions, fintech, and other stakeholders.

To truly harness the power and promise of credit building, funders and grantees need to understand and address the current context. A good credit score and access to quality financial products are likely to continue to be foundational ingredients for economic security and prosperity. Credit building is a critical support, opening up more opportunities for people, but more access to safe, affordable, and sustainable products and systemic reform are needed to create truly equitable conditions.

People need a system that offers safe and affordable products and uses alternative, nontraditional metrics to show reliable payment and reduced risk for capital.

They need financial institutions with funder backstops to reassess risk tolerance and invest capital in persons and communities of color. People need a system in which credit scores are not the key for good jobs with living wages or quality housing. And people need a fair economic system that is culturally competent and responsive to foster economic growth that benefits us all, regardless of race, ethnicity, or other identity factors. Finally, our communities and leaders need to understand that economic prosperity can be shared and grown through equitable credit access. The narratives supporting fear and scarcity need to be upended so that everyone can have the opportunity to achieve stability, economic security, and wealth.

Philanthropy has the chance to invest more intentionally in intersectional services, system change, policy reinvention, and narrative change to realize a just, equitable system and create greater prosperity for Black, Latinx, Indigenous, MENA/SWANA, Asian and Pacific Islander, and immigrant people. In that way, we all will benefit from a stronger economy that works for everyone.

Advancing Equity

The Power and Promise of Credit Building

CREDIT TERMINOLOGY

Alternative Financial Services: A broad term that encompasses financial services operating outside of federally insured institutions (examples: pawnshops, car title lenders, and stores offering payday loans, rent-to-own, check-cashing, money transmitting services).

Community Development Financial Institutions (CDFI): A lender with a mission to provide fair, responsible financing to rural, urban, Native, and other communities that mainstream finance does not traditionally reach.

Credit Builder Loan: A small dollar loan that is secured by the loan proceeds themselves. Rather than issuing the loan funds to the borrower at loan closing, the money is released to the borrower upon repayment. Since the loan is secured by loan payments, the loan is low risk to the lender and low risk to the borrower.

Credit Building: Activities that expand access to credit to people of color and immigrants who have been historically and presently excluded from the credit system. Traditionally, credit building has been defined by products that facilitate making on time monthly payments on a financial product that is reported by the creditor to the major credit bureaus.

Credit Desert: A term used to describe geographic areas with limited access to traditional financial service providers, and often with a prevalence alternative financial service providers.¹

Credit History/File: Record of transactions involving the use of credit – and other products/services.

Credit Invisible: No credit report or score due to a lack of credit history.

Credit Repair: A service provided that disputes tradelines on a consumer's credit report, regardless of validity. Credit repair should not be used to mean 'accurately disputing incorrect information on a credit report,' as that is a legitimate service. Avoid using this terminology except for in the context that is appropriate.

Credit Report: Summary of credit history.

Credit Reporting Agencies: Companies that compile and sell credit reports, also known as credit bureaus.

Credit Score: A number used by lenders to determine a consumer's level of risk (i.e., how likely it is that their debts will be repaid). Credit scores are generated by a credit scoring model utilizing the data from a credit report; there are many different credit scores. Also known as credit rating.

Debt Management: Any strategy that helps a debtor to repay or otherwise handle their debt better. Debt management may involve working with creditors to restructure debt or helping the debtor manage payments more effectively. Also known as credit remediation.

Financial Coaching: An approach to helping clients develop skills and behaviors that focuses on the client's goals; in financial coaching, the client defines goals and solutions with the support of a coach.

Rent Reporting: The monthly reporting of tenant rent payments to at least one of the major consumer credit bureaus for inclusion on a traditional consumer credit report to help renters improve their credit history.

Secured Credit Card: A card that requires a small cash security deposit that is equal to the credit limit when the account is opened.

Small Dollar Loan: Broadly speaking, this is a form of short-term credit via loans of less than \$5,000, with terms ranging from as little as two weeks to as long as three years, with robust consumer protections in place that prohibit unfair, deceptive, and abusive practices and acts (e.g., payday loan alternatives).

Subprime Credit: A credit score below 659.²

Thin File: Limited credit history (may be scored or unscored).

Unscored: No credit score due to limited credit history (could have a credit report).

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