Credit Management: Using Credit Wisely

TRAINING TECHNIQUES

MODULE DESCRIPTION

Credit Management: Using Credit Wisely is a 60-90 minute program designed to help participants to use credit wisely, establish and maintain a good credit rating, and avoid excessive debt. There is more information in the content than can be presented in the session. However, it is included to deepen the presenter's knowledge of the topic. Be sure to leave enough time in the presentation for participants to calculate their Debt-to-Income ratio.

LEARNING OBJECTIVES

At the conclusion of this program, participants will be able to:

- List two wise and six unwise uses of credit.
- Identify three factors affecting the cost of credit.
- Develop a basic understanding of credit reports and credit scoring
- Calculate their debt-to-income ratio.
- State three warning signs of too much debt.
- Identify three sources of help in answering questions about credit and managing personal indebtedness.

REFERENCES

- SECNAVINST 1754.1, Family Service Center Program.
- OPNAV Instruction 1740.5B, Personal Financial Management Education, Training and Counseling Program.
- Command Financial Specialist Training Manual, NAVPERS 15608D (or later).
- Bamford, J. et. al. 1997. *The Consumer Reports Money Book,* 3rd ed. Yonkers, NY: Consumer Reports.

- Federal Reserve System. 2001. *Consumer Handbook to Credit Protection Laws.* www.federalreserve.gov.
- Federal Trade Commission. 2005. *Credit Repair: Self Help May Be Best.* www.ftc.gov.
- Detweiler, G. 2003. *The Ultimate Credit Handbook,* 3rd Ed. New York: Plume.
- Garman, E.T. and R.E. Forgue. 2007. *Personal Finance,* 9th Ed. Boston, MA: Houghton Mifflin Company.
- Loonin, D. and J. Rao. 2006. *NLCC Guide to Surviving Debt.*, 6th Ed. Boston, MA: National Consumer Law Center.

- www.aafes.com (Army Air Force Exchange System)
- www.abiworld.org (American Bankruptcy Institute)
- www.aiccca.com (Association of Independent Consumer Credit Counseling Agencies)
- www.annualcreditreport.com (Free annual credit report from the three major agencies)
- www.bankrate.com (Bankrate Website for Comparison Shopping)
- www.bea.gov (Bureau of Economic Analysis)
- www.bls.gov (Bureau of Economic Statistics)
- www.consumerlaw.org (National Consumer Law Center)
- www.creditpage.com (Consumer Credit Guide)
- www.cuna.org (Credit Union National Association)
- www.federalreserve.gov (Federal Reserve System)
- www.ftc.gov (Federal Trade Commission)
- www.legalconsumer.com (Bankruptcy Information)
- www.lifelines.navy.mil (Lifelines Services Network)
- www.myvesta.org (Non-profit Debt Management Counseling)
- www.ffsp.navy.mil (Fleet and Family Support Program)
- www.nfcc.org (National Foundation for Credit Counseling)

MODULE PREPARATION

Handouts:

- Test Your Credit Knowledge
- Empty Pockets/Wise Use of Credit
- Debt-to-Income Ratio Worksheet
- Choosing Credit Cards
- Credit Reports

Materials (varies depending on activities chosen):

- Pens and Pencils
- Items for the Empty Pockets Activity
- Newsprint and Markers
- Calculators for Debt-to-Income Ratio Activity

SUMMARY OF OPTIONAL PARTICIPANT ACTIVITIES

- **Test Your Credit Knowledge:** A series of ten questions introducing students to module content and providing a means to review the content after presentation.
- **Empty Pockets:** A brainstorming activity that helps participants understand the difference between a living expense and a debt, and recognize wise and unwise uses of credit.
- **Debt-to-Income Ratio:** Participants calculate their debt-to-income ratio. (Not optional)

CURRICULUM OUTLINE

1. Welcome and Introduction (5 minutes – 10 minutes)

   a. Optional Participant Activity: Test Your Knowledge

2. Using Credit (5 minutes – 20 minutes)
    a. Optional Participant Activity: Empty Pockets
    b. Wise Use of Credit
    c. Unwise Use of Credit
3. Qualifying for Credit (15 minutes)
    a. The Three "C's" of Credit
    b. Credit Reports
    c. Your Credit Score
4. Establishing a Credit History (2 minutes)
5. Reducing the Cost of Credit (15 minutes)
    a. Credit Worthiness
    b. Comparison Shopping
    c. Where to Borrow
    d. How Much to Borrow
    e. How Long to Repay
    f. Minimum Monthly Payment
    g. Minimizing Interest Charges
    h. Credit Card Tips
    i. Other Costs and Features
6. Military Cards (3 minutes)
    a. Star Card
    b. Government Credit Cards
    c. Navy Cash Card
7. Debt: How Much is Too Much? (10 minutes)
    a. Calculating your Debt-to-Income Ratio
    b. Warning Signs
    c. Other Indicators

d. Critical Point

8. Recovering from Debt (10 minutes)

   a. Take Charge

   b. Use a Power Payment Plan

   c. Talk to your Creditors

   d. Beware of …

   e. The Last Resort: Bankruptcy

   f. Identity Theft

   g. Talk to a Pro

   h. Sources of Help

9. Summary (5 minutes)

INSTRUCTOR TECHNIQUES BY SLIDE NUMBER

Optional Participant Activity: Test Your Credit Knowledge Part I

Time: 5 Minutes

Preparation: Distribute the handout, "Test Your Credit Knowledge" and pens and pencils as needed.

Procedure: Tells participants that we will begin the class with a quick questionnaire on key credit issues. Distribute the handout and ask students to answer the questions to the best of their knowledge. Explain that you will give them the answers at the end of the session.

Statistics are included as a point of interest and motivation. The statistics are current as of June 2007. When presented after January 2008, presenter should update relevant statistics wherever possible. Note that the drop in the bankruptcy rates was due to the change in the law, making the rules more stringent. As of publication of this curriculum, the rates

for personal bankruptcies were increasing at a fast rate. Check bankruptcy statistics at www.abiworld.org.

In lieu of the lecture on slides 4 and 5, the following activity can be done by the class.

Optional Participant Activity: Empty Pockets

This exercise will help participants discern the different between living expenses and debt, and indicate whether their use of debt was "wise" or "unwise".

Time: 20 minutes

Materials: Handout "Empty Pockets", one for each group, and one page of newsprint and markers for each group.

Preparation: Have available a collection of items commonly carried in a purse or pocket such as car and house keys, pictures of family members, band aids, pens and pencils, lipstick and makeup, credit cards, money, etc. Have one piece of newsprint and markers for each group.

Procedure: There are four steps to this activity.

Step One: Living Expense or Debt? Working in groups of four to six, have participants empty their pockets, wallets, and/or purses and place the contents on their group table. Ask them to create a list of expenses the items represent. For example, car keys obviously would represent a car loan, a house key would represent a mortgage, utility expenses, upkeep expenses, etc. A Band-Aid might represent medical expenses, pictures of children could represent the cost of raising children, student loans, clothing, etc. Allow about three to five minutes for each group to write a list of answers on newsprint. If participants are short on items, provide them with typical items from your own collection.

Step Two: Living Expense or Debt? After the groups have completed Step One, have them go back through their list and determine whether it is a living expense or a debt. This will require you to explain the difference — if they had to borrow money or use any form of credit for the item, it is a debt. They can use the handout "Empty Pockets" to list the type of expense or each item on the newsprint can be labeled "LE" or "D". Allow about three minutes for this part of the activity.

Step Three: Wise or Unwise Use? Have each group determine whether the items they labeled as a debt was a wise or unwise use of credit. Allow about three minutes for this discussion.

Step Four: Debrief. When all groups have finished, go around the room asking for input from each group as to what was a wise or unwise use of credit and why. Comment and commend as appropriate and conclude by briefly showing slides 4 and 5 with the following discussion of wise and unwise use as necessary.

Provide participants with the handout "Credit Reports". A lot of the information covered on the slides is included on this handout. If you are able to contact participants ahead of time, have them bring in their own credit report from www.annualcreditreport.com. If a classroom internet connection is available, show them the website.

This information is covered on the handout. If time is short, you can simply refer them to the handout and not spend a lot of time on this slide.

Reinforce the final bullet, and warn participants away from predatory lending practices. Explain that one way to tell if they should get the credit or not is by considering who is willing to lend to them. If their own bank or credit union will not lend to them, that is a danger sign in and of itself. Extensive additional information on Predatory Lending can be found in the "Consumer Awareness" module.

These are very simple slides that show how a bigger down payment and shorter repayment period can reduce the total cost of borrowed money.

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Give each participant a copy of the handout "Choosing Credit Cards". Note that a lot of the information you are about to cover is on this handout, including many helpful websites. If time is short, you can skip spending a lot of time on any of the information included in the handout.

Additional information has been included regarding balance computation methods. You should be thoroughly familiar with the topic in case specific questions come up.

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Participant Activity: Calculating your Debt-to-Income Ratio

Time: 10 Minutes

Preparation: Distribute the handout, "Debt-to-Income Ratio", pencils and calculators

Procedure: Explain that an important part of avoiding excessive debt is calculating your debt-to-income ratio. This number tells you what portion of your income goes to pay debt each month. Once calculated, the scale at the bottom helps you determine if you have too much debt or can afford additional monthly payments. Lenders use the debt-to-income ratio to help them decide if they will extend credit. Explain that in this program they will estimate their income and payments if they don't know specific figures, and when they go home they can fill in the correct amounts.

Step 1. Ask participants to estimate their net monthly income (all of their pays and allowances minus just their taxes).

Step 2. Next, ask participants to list each of their creditors and the monthly payment that goes out to each creditor. Be sure they include any money owed to the government and any payments that are taken right out of the paycheck. Tell them not to include rent or mortgage amounts. (A different debt-to-income ratio scale is used when including mortgage debt, usually with 36% being the "safe" level. For purposes of the PFM program, only non-mortgage debt is used in this ratio. Assure participants that this non-mortgage debt scale is a valid financial planning ratio.) Participants should put the total of all monthly payments in the space provided.

Step 3. Using the formula in step 3, ask participants to divide their total payments by net income ("big number into the little number"). The result is their debt-to-income ratio. You can do a simple computation on a whiteboard or newsprint for an example.

Net Income = $2000

Total Monthly Payments = $500

500/2000 x 100 = A Debt-to-Income Ratio of 25%

Tell participants that the last thing to do is compare their debt-to-income ratio with the scale at the bottom to determine their level of debt. Explain what the various percentages mean.

There is more information in this section than can or should be covered. The information is included to deepen the presenter's knowledge of the topic in case specific questions arise.

Information on Identity Theft is included on the "Choosing Credit Cards and Credit Reports" handout. You can also provide participants with the Identity Theft handout from the "Consumer Awareness" module.

Reinforce that all websites are included on the handout "Choosing Credit Cards".

Conclusion and Review

Optional Participant Activity: Test Your Credit Knowledge Part II

Time: 5 Minutes

Preparation: Be familiar with the answers to the "Test" below.

Procedure: Ask participants to get out their "Test Your Credit Knowledge" handout. Review the answers and ask if there are any other questions to be answered or clarifications needed.

Test Your Credit Knowledge*

1. True or False? Your purchases are not interest-free, even if your card offers a grace period, when you carry a balance from month to month.

   True. If you carry a balance, the issuer will charge interest from the date of posting or purchase (depending on its policy) on all new purchases. Generally, your purchases are interest-free only when your card offers a grace period, you start the billing cycle with a zero balance and you pay all new purchases in full by the due date. (Most cards do not offer a grace period on cash advances.)

2. True or False? A creditor cannot turn your account over to a collection agency if you are paying something, even $1.00, on the account.

   False. A creditor can turn your account over to a collection agency if you do not meet the terms of the account. That means if you are late with a payment or make a partial payment, the creditor has the ability to turn your account over to a collection agency.

3. True or False? Your credit will look better after a bankruptcy since you no longer owe any debts.

   False. Bankruptcy is one of the most serious marks on a credit report and it can stay there for up to ten years, making it more difficult and expensive to get credit. In addition, bankruptcy does not always wipe out all debts, so you may still owe some debts depending on your situation.

4. True or False? The best use of credit is to purchase things that grow in value (assets) or for convenience.

   True. And the key to avoiding the unwise use of credit is planning and behavior.

5. True or False? You get one free credit report each year from each of the three large Credit Reporting Agencies.

True: Go to www.annualcreditreport.com. Check your report once a year.

6. If you are turned down for credit, lenders are required to provide you with which of the following?

   a. Information about how to order a free copy of your credit report, if one was used in the evaluation of your application.

   b. The specific reasons you were turned down or instructions on how to obtain those reasons.

   c. A written notice that your application has been turned down.

   d. All of the above.

   The correct answer is d., all of the above.

7. True or False? Because most credit card issuers use some form of the average daily balance method for calculating interest, you'll save the most money (when you carry a balance from month to month) if you send in your payment early, rather than waiting until the due date.

   True. Because the interest "clock" is ticking daily, the sooner the lender posts your payment, the less interest you have to pay.

8. True or False? Most Americans have a FICO score in the 600 to 699 range.

   False. 27% have FICO scores in this range. The majority of Americans are in the 700 and above range.

9. True or False? Seeking help from a non-profit counseling agency will ruin your credit rating.

   False. If you enter a debt repayment program with a counseling agency, most creditors will bring your account up-to-date as long as you stick with the program. A very few creditors may report your account as late or being repaid through counseling. Those remarks, however, are not considered as serious as bankruptcy, legal judgments or tax liens.

10. Which of the following are good ways to help protect yourself from identity theft, where someone uses your personal information to apply for credit in your name?

    a. Check your credit report at least once a year. Investigate if you find accounts that aren't yours.

    b. Rip up, or better yet, shred, any credit card applications, bank or billing statements, and any other sensitive documents.

    c. If you don't get a bill for one of your credit cards in any given month, call the issuer immediately. Don't just assume you're off the hook that month.

    d. Use a locked mailbox for incoming and outgoing mail (especially bills).

    e. All of the above.

The correct answer is e., all of the above.

*adapted from Gerri Detweiler, *Test Your Credit Knowledge*

Conclude by noting that credit is a valuable tool, something we will use throughout our lifetime. However, it can also be a source of long lasting difficulty; the availability and over-extension of credit has contributed significantly to the rise in personal bankruptcy rates in the past twenty years.

Ask yourself the following questions before using credit:

- Will your budget be able to handle the increased payment months or years down the road?
- What will the extra payment do to your debt-to-income ratio?
- Have you shopped carefully for credit; are you getting the best rate?
- What will you have to show for all that money after the loan is repaid?

Credit isn't a right, it is a privilege. Wise use of credit is a key element in achieving financial independence; misuse is a ticket to financial ruin. If you abuse it, you will lose it. It is your decision.