CREDIT AND DEBT BASICS: TABLE OF CONTENTS

Why Take This Course?

Do you ever wish you knew more about personal finance? No matter where you are in your financial journey, there always is more to learn.

SAM's free online courses are not intended as financial advice, but as a starting point to raise awareness, to increase skills and knowledge related to personal finance, and to guide you to helpful resources.

Research shows that financial education is most effective when it is relevant to a decision you are faced with right now. This course covers:

- How credit works and how to assess your debt load.
- Checking and correcting your credit report.
- Pros and cons of common debt management options.

Disclaimers

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INTRODUCTION

What's Your Credit and Debt Plan?

If these questions sound familiar or keep you up at night, then here is a source for answers. This course will help you navigate through some common credit and debt issues:

- Borrowing and using credit wisely
- Working with lenders
- Getting help with credit card issues
- Improving credit scores

Having a good plan for using credit and debt will help you feel more secure, and possibly less stressed about your spending decisions.

GETTING STARTED

Good vs. Bad Credit

Using credit is not a bad thing — it's how you use credit that can be good or bad. Some upsides of using credit include:

- It's convenient and safer than carrying cash.
- You can spread payments out.
- It's helpful for emergency situations.
- Using credit can help build a strong credit history.

Credit also can have its downsides if you don't understand when and why to use it. Using credit to "buy now" without thinking about "paying later" can cause you to pay more than you intended through interest and fees. This can happen when:

- You use credit to buy things you can't afford and don't really need.
- You take advantage of special offers such as "no interest for 12 months" without planning to pay the debt before the special offer expires.
- You don't understand the terms of the lending agreement.

SAM Tips Use caution with two costly types of borrowing:			
Loan	**Pros**	**Cons**	**Do This Instead**
Payday Loans are used to bridge a short-term gap between your current needs and your next paycheck.	• Application for the loan is easier. • Usually doesn't involve a credit check. • Can provide immediate cash, if used wisely.	• Works like a cash advance against your next paycheck. The cycle usually ends up repeating itself. • High interest rates (often up to 300 percent). • This is a legally binding loan agreement, and lenders will aggressively pursue borrowers for repayment.	• Put off purchases, if possible. • Ask friends or family for short-term help. • Consider a credit card cash advance.
Cash Advances allows you to borrow cash on your credit card, up to a certain limit.	• Money can be withdrawn at an ATM if using a credit card. • Pre-authorized checks can be deposited or cashed at your bank. • Offers quick cash, up to a certain limit.	• High interest rates apply, and lenders are not required to apply minimum payments (if combined with a credit card) to the cash advance portion. • Flat fees for the advance amount and ATM charges may apply. • Borrowing through cash advances can create a cycle of bad borrowing habits.	• Put yourself on a spending plan and look for money through cutbacks in your expenditures. • Use your credit card for purchases instead. • Ask family and friends for short-term help. • Shred all pre-authorized checks to avoid temptation. "

Why Use Credit

View credit as a tool—It's part of the way you conduct your financial life to get the things you need, such as cars, homes, technology, furniture and appliances. And of course, credit can be a necessary cushion in emergencies.

Using credit also spurs the economy:

- Many small businesses rely on loans to fund their start-up costs. By employing a few workers, a new shop owner boosts the income for families in the community. These families then use their earnings to buy goods and services from other businesses, making those businesses grow.
- Borrowing also allows consumers and businesses to spend when their income isn't increasing. That can help the economy grow.

However, if too many businesses and consumers borrow more than they can afford, it can end up hurting the economy.

Consumer Spending and the Economy

Consumer spending fuels 70 percent of our nation's economic growth, and this can boost consumer confidence. When confidence increases, the economy usually expands, and that is good for everyone.

When consumers spend more money, demand for products and services increases. To meet the new demand, companies buy more equipment, hire more workers and give more pay raises. That means employees now have more money to spend — and the cycle of economic growth continues.

[Source: Flow of Funds Accounts in the United States, Federal Reserve 2011]

Who Can Use Credit

When you apply for credit, you need to consider your borrower profile — that is, how you appear as a borrower to potential lenders. Typically, lenders look for borrowers who:

- **Are over 18**. In some cases minors can be extended credit as an authorized user or joint account holder on an adult's account.
- **Have capital** in another checking or savings account, showing the ability to maintain healthy relationships with lenders and to make on-time payments on a loan or credit line.
- **Have credit capacity**, meaning that the amount of unused credit available is in good balance with the amount of current debts.
- **Display good credit character**, which is shown in a credit report as on-time payments and paying off debts to other creditors.
- **Possess collateral** that can be used to offset the lender's risk in case of nonpayment (this applies more to business, home and auto loans, not credit card issuers).
- **Have stable life conditions** such as steady income, employment and a reasonable debt load, increasing the likelihood of paying off debts.

Even if you have had previous credit issues, your lender may overlook these if you can show that you are working through them. This is especially important when you are working to repair credit after a bankruptcy or if you have been a victim of fraud or identity theft.

Calculate Your Debt-to-Income Ratio

Many financial advisors suggest that your total consumer debt load (not including housing debt) should be less than 20 percent of your annual net (after-tax) income.

The debt-to-income ratio looks only at your "consumer debt" and does not include money spent on a mortgage, rent, utilities or taxes. Consumer debt does include credit card payments, car loans, student loans and any other debts that you repay monthly.

Don't forget to include debts that you are repaying to friends and family members in your debt-to-income ratio calculations. Even though debts like these don't show up on a credit report, they still are part of your monthly debt responsibilities.

Divide your monthly consumer debt payments by your net (after-tax) monthly income. For example:

Total monthly consumer debt payments ($400) ÷ Monthly take-home pay ($2,500)

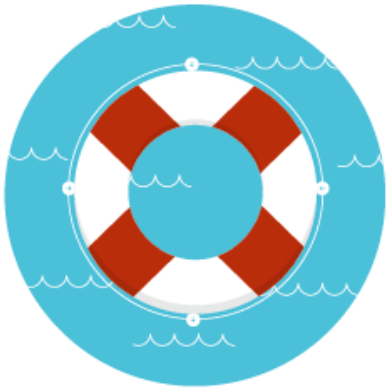
400 / 2,500 = .16

Move the decimal point two places to the right to get the percentage:

Your debt-to-income ratio is 16%

Crunch the Numbers

Use a debt-to-income ratio calculator to assess your debt load.



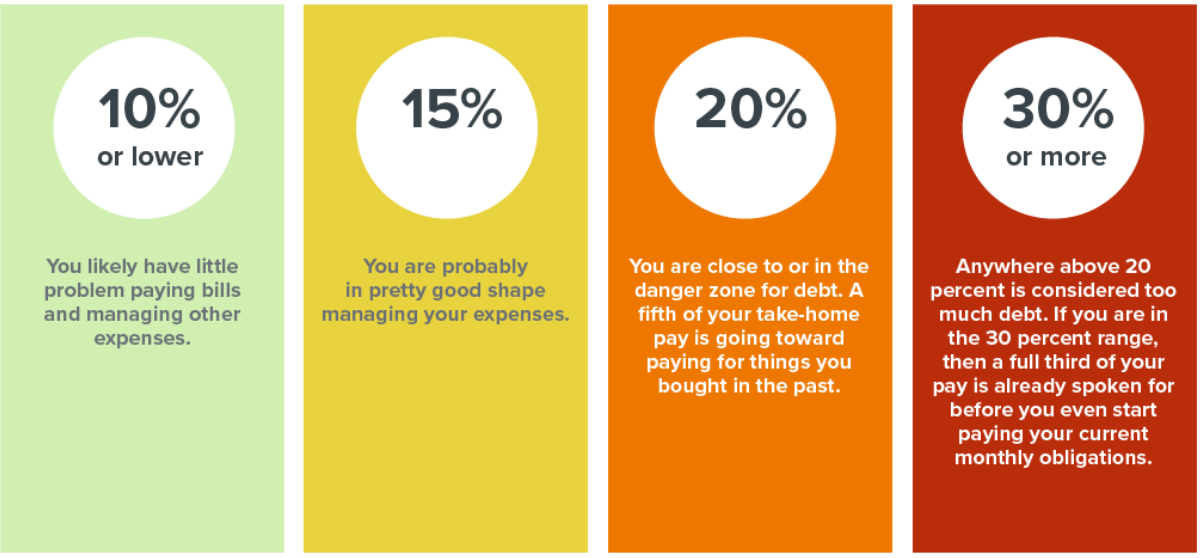
How Much is Too Much Debt?

When you charge a purchase or take out a loan, you are borrowing from two people: the lender and your future self.

Every dollar borrowed today is a dollar less to spend from your next paycheck. Knowing how much debt you can manage is crucial to avoiding problems with debt management — and it also impacts your cash flow.

Debt-to-Income Ratio Guidelines

Here are some general guidelines to assess your ratio, but keep in mind that everyone is different. You might have other factors, such as anticipated irregular income, mortgage payments, home costs or emergency reserve funds that influence how much debt you can afford to carry at a given time.



Not All Debt Is Equal

A smart credit shopper doesn't need to be at the mercy of lenders. It pays to have knowledge of options and shop around to compare interest rates and repayment terms.

For example, a home loan or mortgage usually is one of the better forms of debt because most homes increase in value over time. Also, the interest paid on the loan may be tax deductible. A student loan is another type of "better" debt because educated workers generally earn higher wages. (Assuming that you are able to turn your degree into a lucrative job.)

Consumer debts such as balances on credit cards and car loans generally do not increase in value over time, making them less favorable types of debt. The interest paid on consumer debt is likely to be high and not tax deductible.

Before using credit to make a purchase, it's good to know the costs and benefits of that particular type of debt. Some of these costs and benefits are outlined below.

Type of Debt	Example	Typical Costs	Benefits
Revolving Credit	Credit card	– Interest on outstanding balances – Late payment fees – Annual fees – Over-the-limit fees	– Allows purchases to be made now – Reduces the need to have cash – Offers a record of purchases – Consolidates debt into one payment – Has purchase protections
Installment Loan	Car loan	– Interest on outstanding balances – Finance charges to originate the loan – Prepayment penalty (varies) – Late payment fees	– Monthly payments can help afford a better car than a cash transaction – Generally a fixed interest rate – May be able to negotiate extras if the loan is through the car company
Installment Loan	Federal student loan	– Loan fees (depending on your loan type) – Interest fees (depending on your loan type) (Use this information from Federal Student Aid to get a complete picture of interest and fee charges.)	– Lower interest rates than private loans – Payments can be deferred up to three years – Offer forgiveness, if you meet the guidelines – Can be consolidated without the need for good credit – Can be obtained without a credit history – May be able to deduct interest payments

Mortgage Loan	Home loan	– Upfront fees to secure loan: ▪ Fees to lock in rates ▪ Origination fees ▪ Appraisal/inspection fees ▪ Title search fees ▪ Escrow and recording fees ▪ Prepaid interest (also known as "points") ▪ Closing costs – Fees on loan: ▪ Interest on outstanding balance ▪ Late payment fees ▪ Prepayment penalty (varies)	– Tax deductions on interest paid for the year (this also applies to home equity loans) – Closing cost deduction (first year of ownership) – Property tax deduction

HOW IT WORKS

How Do Lenders Make Money?

Banks and other lenders are in a business to make money. Financial institutions pay a low interest rate on depositor accounts such as savings and money market accounts, then use that money to lend money to borrowers at a higher interest rate in the form of loans and credit cards.

It may sound like lenders are the bad guy, but they actually serve a purpose in the economy. However, because lenders have an interest in maximizing their profits, lending also comes with costs and cautions.

Lending makes the world go 'round!

Think about your own situation: You go to the bank to get a car loan. The lender issues the loan, with some fees of course, enabling you to get your car. The car dealer now has more money to employ people and get more inventory. The employees of the dealership have income to spend and buy other goods from other businesses. Other businesses and the economies of many other families grow.

Borrowing Has Costs

For many years, credit card users were left in the dark about all the fine print in their credit card agreements. Reforms and regulations such as the 2009 Credit CARD Act, also known as the "Credit Cardholders' Bill of Rights," now provide some protection to credit cardholders, but it's still important to understand the basics of the fine print in your credit card agreement.

Interest:

Interest is what you pay for the privilege of using someone else's money. Interest can be as much as 25-30 percent on some credit cards.

Fees:

Some credit card companies, banks and department store or big box store credit card issuers charge annual fees as well as fees for late payments. You can avoid late fees by making on-time payments, but annual fees must be paid each year whether you use the card or not.

Finance charges:

Finance charges include all interest and fees added together and is expressed as an annual percentage rate (APR).

How do you figure your interest?

The Annual Percentage Rate (APR) is a yearly figure, but you're not charged interest on a yearly basis. You actually get charged interest on a daily basis. The company offering you credit is legally obligated to disclose the APR. Here's how you can calculate it:

Divide the APR by 360 or 365 (look at your agreement for the number of days).

This is the periodic interest rate that will compound every day. Keep in mind that interest builds on itself — that's why it's called "compound" interest. Each time the interest is calculated as a percentage of the total, that added interest becomes part of the new total for the next time the interest is calculated.

Credit Card Definitions

Before you sign up for a credit card, be sure to compare the APR charged by several companies and know the terms of the agreement. The Consumer Financial Protection Bureau has a thorough list of credit card contract definitions.

Compound Interest Works for the Lender (Not You)

When you use credit, but don't pay off the entire amount by the initial due date, you are setting yourself up to pay compound interest. Here's a very simple example showing how it works:

Payback Period (Month)	Principal	Interest Charge for Period at 15%	Balance
1	$500	($500 × .15) ÷ 12 = $6.25	$506.25
2	$506.25	($506.25 × .15) ÷ 12 = $6.33	$512.58
3	$512.58	($512.58 × .15) ÷ 12 = $6.41	$518.99

You can see how adding the interest back to the balance and then charging interest on that new balance can add up quickly. Of course, this is very oversimplified. No payments are made in this example, so the balance continues to rise. In the real world, you would make payments so the balance would decrease some. The important part is to make sure you know what your lender is charging and over what period.

Making only minimum payments

Use this calculator to figure out what you will end up paying in interest and how long it will take you to pay off a loan when you make only minimum payments on your credit card debts. Use the figures from your credit card(s) for balance, APR and minimum payment percentage:

- To see how long it would take you to pay off your debt paying only the minimum each month.
- To calculate what you really can afford to pay for a minimum payment based on your budget.

Consequences of Not Paying On Time

Falling behind or missing loan payments can have serious effects. The consequences of delinquent accounts start with simple late charges, but eventually can lead to long-term problems. When you do not pay a bill, you might experience:

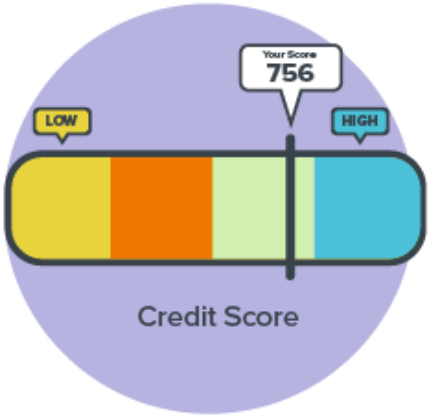
- Fees for late payment(s).
- Potential damage to your credit history, making future borrowing tougher and more expensive.
- Being denied credit or sent to collections.
- Having your wages garnished or items repossessed to repay your debt.
- Added stress and decline in overall well-being.

Authorized User vs. Joint Account Holder

When you allow someone else to be an authorized user on your credit card account, you are letting them use the account without any legal accountability to pay back the debt. If that credit card account went into default, the authorized user would not be responsible. However, if you make someone else a joint account holder, then both you and that person are equally responsible for the debt. If the account goes into default, a joint account holder is just as accountable to pay it back as you are.

How Well Do You Know Borrowing Terms?

Term	Definition
Interest	What you pay a lender as compensation for borrowing money as a loan, credit card or line of credit. Calculated as either a fixed or variable rate, expressed as a percentage of the amount you borrow over a specific time period.
Fees	Additional charges you pay for using a line of credit or specific transactions such as cash advances, foreign transactions, balance transfers and penalties for late payments.
Finance Charges	The total amount you pay to borrow, including the interest plus any fees for arranging the credit, if applicable. Also expressed as an annual percentage rate (APR).
Authorized User	Someone who can use another person's available credit, but who is not legally liable for the balance due.
Joint Account Holder	A person who shares responsibility for payment with other users of the account and is legally liable for the balance due.
Compound Interest	The amount paid on the combined value of the original principal (balance) you owe and any interest that has been added to the principal.



Your Credit Life, Your Credit Score

Have you ever been denied credit because of your credit score? Do you need to know how to improve your credit history? You're not alone. The Corporation for Enterprise Development (CFED) reports that 56 percent of consumers have subprime credit scores, translating to a higher credit risk for lenders.

What's a Credit Score?

Your credit score is a number that is calculated using information in your credit report. Lenders use a credit score to assess how risky it would be to lend to you, and the interest rate they will offer you if they agree to lend you money. The best (or lowest) interest rates go to applicants with the highest scores.

Most lenders use credit scores rather than credit reports because the scores reduce extensive, detailed information about your financial history to a single number.

The tricky part is that not all lenders use the same credit score. A "good score" depends on the scoring model used to calculate it. Most consumers are familiar with the FICO score, which is the standard, but there is another competing credit scoring system, VantageScore, which was developed by the three major credit bureaus.

Both FICO and VantageScore emphasize paying your bills on time and maintaining a favorable credit capacity (the amount of credit you are using in relation to your credit limit), but the two systems give different weights to particular types of credit-related behavior.

Understand Your Numbers

FICO Score Ranges	What It Means
800+	**Exceptional**. You likely will have little trouble getting approved for credit and will qualify for the best loan terms.
740 – 799	**Very Good.** You likely will qualify for better interest rates.
670 – 739	**Good.** Lenders see you as an "acceptable" borrower, but may require answers to additional questions about your credit history.
580 – 669	**Fair.** You might have difficulty getting credit. When you are approved, it likely will be at a higher interest rate.
579 and lower	**Poor.** This reflects some real hardships, such as bankruptcy, or a borrower who has not built up credit yet. Now is the time to make a plan to get your rating higher. If you are granted credit, you might need to put down a deposit or pay a fee.

Want More on Credit Scores?

Learn more about how your score affects your credit worthiness here.

What's In Your Credit Score?

Different lenders use different scoring methods, and your score can change over time. Your credit score will reflect:

- How much credit you have used compared to what is available for you to use
- How often you apply for new credit
- How long you've used credit
- The types of accounts you have and the number of accounts you have
- How you've used credit and handled the credit approved to you in the past
- Any legal proceedings against your credit

Keep in mind that regardless of your current circumstances, you can put together a plan immediately to strengthen your credit history, so you are positioned to secure credit in the future.

Your Borrowing Habits Are Not Secret

Your ability to borrow depends on your reputation for repaying your debts. A credit report is a record of how you have paid your credit card debt and other loans over time. Creditors rely on your credit information to see how you've handled your loans in the past and to decide how likely you are to repay a new loan. Review your credit report on a frequent basis; look for errors that need to be corrected.

Who Can Access Your Credit Report?

Your credit report can be accessed by:

- A credit lender, based upon your application for credit

- Collection agencies who are collecting a debt from you
- Your insurance company for underwriting purposes
- Your employer, but only if you grant permission
- A potential landlord, but only if you grant permission

Other entities can access your credit report if they have a "permissible purpose" as defined by the Fair Credit Reporting Act.

Review Your Credit Report

The Fair Credit Reporting Act (FRCA) gives you the right to pull your own, free credit report once a year from each of the three nationwide credit reporting agencies: Equifax, Experian and TransUnion. Because you can request up to three per year (one from each of the three major agencies), it is recommended that you request one every four months to keep a continuous track of your record. You can order your free credit report at **Annual Credit Report**

What To Look For On Your Credit Report

According to the Consumer Financial Protection Bureau, you should review your credit report for the following:

- Only items about you
- Inaccurate or incomplete information
- Accounts that do not belong to you
- Addresses of places you have never lived
- Employers you have not worked for
- Information that should no longer be on your credit report, such as negative information that occurred more than seven years ago.

In particular, review your credit report for items that lenders typically look for:

Late payments

Debt-to-credit ratios (The total of outstanding balances in comparison to the total credit you can borrow. The lower the ratio, the better.)

Collection items or write-offs due to bad debt

Liens and bankruptcies

Accounts that should have been closed or that you don't remember opening

Hard inquiries on your credit (such as when you apply for a new loan or credit card)

What's Not On Your Credit Report: Your Credit Score

Your credit score is not included in your free annual credit report. Many credit card companies today provide free credit scores on billing statements or online as a way to attract and retain your business.

Many mobile banking and personal finance apps will tell you your credit score for free, but keep in mind that lenders use different versions of your credit score. For example, there are dozens of different versions of your FICO score, used for different types of credit inquiries.

When you're checking your free credit report, you may be asked if you also want to see your credit score. Before you agree, be sure you understand the terms of the offer.

Disputing Items on Your Credit Report

If you find errors in your credit report, contact the reporting agency and the creditor that provided the information. The credit report should contain information about disputing information contained within the report. It is very important to contact both the reporting agency and the creditor.

How can I correct an error?

Provide information and documentation supporting your dispute. Then you need to wait to see if the creditor will remove or amend the item in dispute.

- If the error involves a false credit card charge for something you never ordered or never received, you must contact the creditor (the business or entity that mischarged you) within 60 days of receiving the bill with the first error. Learn more about disputing credit card errors at the Federal Trade Commission (FTC) website.
- If the creditor resolves the disputed item(s) in your favor, the creditor must notify all of the credit reporting agencies to which it submitted the erroneous information.
- If the creditor does not resolve the disputed item(s), you can ask for a statement of the dispute to be included in your file for future reporting. This applies only to items you have submitted to the reporting agency and the creditor. That is why it's important to file disputes with both parties.
- If you are still not satisfied with the result of the dispute, you can file a complaint with the Consumer Financial Protection Bureau (CFPB).
- Keep your original documents when filing a dispute. Keep a file of any disputed items along with dated original documents, dated copies of letters or other written correspondence, dated notes about conversations, etc.

Know Your Rights: The Fair Credit Reporting Act

The credit reporting companies and the entities that provide information about you are responsible for correcting errors on your report. Use this sample dispute letter and learn more about credit report disputes on the FTC website.

Make a Plan to Improve Your Credit

To keep a good credit rating, or to improve your credit:

- Pay your bills on time, all the time – even if it's just paying the minimum due.
- Use existing credit wisely to establish a good payment history.
- Don't hit your credit limit.
- Pay at least the minimum due on all debt and put any extra money toward high-interest debt.
- Avoid taking out new credit when you don't need it — pay cash instead.
- Keep track of your credit by getting a new credit report every four months.

Pay Down Debts Faster

Accelerate debt repayment using a program such as PowerPay (www.PowerPay.org), which calculates "power payments" by adding paid-off debts to the balances of remaining debts.

THINGS YOU SHOULD KNOW

Know Your Consumer Rights and Responsibilities

Knowing your rights and responsibilities as a borrower helps you deal with your lender. Even if you seek help to manage debt or handle disputes, or if you file for bankruptcy, you have rights as a borrower.

Your Rights

The Fair Credit Reporting Act (FCRA) gives you certain rights with respect to your credit report, including the following:

- The right to know what your file contains.
- The right to ask for a credit report.
- The right to dispute information in your credit report.
- The right to have inaccurate information corrected or removed.
- The right to have older, negative information excluded from your credit report.
- The right to have access to your credit report limited.
- The right to have your credit report given to your employer (only with your consent).

The Federal Trade Commission offers more information, including additional right for military personnel and victims of fraud.

Your Responsibilities

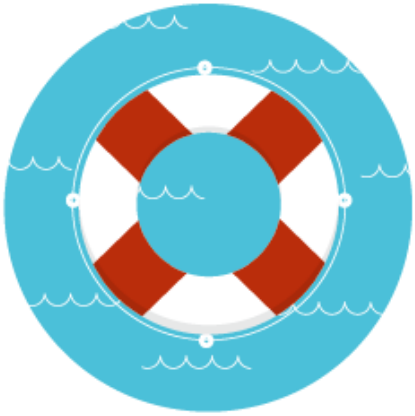
As a borrower, you have certain responsibilities to the companies issuing you credit. Upholding these responsibilities is your obligation to your creditors and also helps you maintain a good credit score. Be familiar with your basic responsibilities when using credit:

- **Understand the terms of the agreement**. It is your responsibility to understand what you are signing up for when it comes to borrowing. Read the fine print regarding interest, fees and other charges.
- **Check your statements**. Ensure the information on your statement is correct. If not, notify your creditor immediately. Keep your receipts and reconcile to your monthly statements.
- **Pay on time**. The creditor has loaned you money so you can "buy-now-pay-later." You are obligated to pay that money back on the scheduled time frame to which you have agreed. Missing payments or continually paying late will damage your credit rating.
- **Update your contact information**. If you move or temporarily change your address, notify your lender(s). Sometimes lenders will give you a break if the bill doesn't reach you in time, but this good-naturedness won't last long.
- **Repay the full debt.** When you borrow, you are borrowing a set amount and you are agreeing to pay interest on the outstanding balance. In the long run, you have to pay the full amount borrowed (principal) plus interest to satisfy the debt. This also includes any associated fees.
- **Notify creditors if cards are lost or stolen.** Always notify your credit card issuer if your cards are lost or stolen. Your liability is limited to $50, but the creditor has a right to know if someone else is using your card(s) to make fraudulent purchases.

When to Worry About Debt

Having some debt isn't necessarily bad, but having excessive debt is. Worrying about debt can affect your behavior, your relationships and your dreams. You probably already know whether you are in over your head when it comes to debt.

Remember that even if you're carrying too much debt, you can reduce it over time. It will take patience, and it won't always be easy, but you can regain control.



Get Help Managing Debt

Don't give up hope If you have problems with debt. There are ways to get out of debt and repair your credit. Remain positive and take action to:

Call your creditors to discuss your options (ideally, call them before you miss a payment). Quite often, you can work out favorable repayment terms with your creditors. Be sure to get any agreement in writing.

1. You can ask your creditors to:
    - Divide payments into smaller amounts
    - Forgive some of your debt
    - Suspend payments
    - Lower payments
    - Waive late fees
2. Go to a nonprofit credit counseling service such as the National Foundation for Credit Counseling (NFCC) or Financial Counseling Association of America to put you on a budget and help you negotiate with lenders.
3. Be wary of credit repair companies that offer to fix your credit history for a fee. Only you can repair your bad credit by repaying your debts and paying your current bills on time.

Debt Consolidation

Debt consolidation combines several debts into one new loan, often with more favorable terms for the borrower. After you speak with a credit counselor or a financial advisor, debt consolidation may be your way to improve your debt management strategy.

Some cautions when considering debt consolidation are:

- You have to change your habits. It works only if you will also reduce your spending and credit purchases.
- Taking out a home equity line of credit to consolidate debts puts your home on the line. Think carefully before you do this.
- Consolidating your debt can look like new debt on your credit history and can end up hurting your overall credit score.
- The total interest cost of your debt may increase if payments are spread over a longer time period

Debt Settlement

Be careful of debt settlement offers you see on television or that show up in your mail (or email). An offer that says "you can be debt free!" might be loaded with high fees and might not offer you any real progress on your debt relief.

Click on the image below to watch this video (https://www.youtube.com/watch?v=PPepWtlvgok) and learn more about debt settlement.

Bankruptcy

Wouldn't it be nice just to wipe away your debts and just file for bankruptcy? Sure, your credit report will take a hit, but you'll get past it … right? Well, actually you might want to think twice before taking this route. Here's some information you need to know.

Types of Bankruptcy

As an individual, you likely will file for one of the following:

- Chapter 7 bankruptcy in which a court appointed trustee essentially sells most of your valuable possessions to pay your debts, or
- Chapter 13 bankruptcy in which you can keep your property and pay off your debts according to a court-approved repayment plan.

Depending on your eligibility, other bankruptcy options may be available to you.

Need more information?

The U. S. Courts offers substantial information about bankruptcy on their website.

What Bankruptcy Doesn't Address

If you file for bankruptcy, it will not address some kinds of debt. Among these are:

- Most tax debts
- Student loans (with rare exceptions)
- New debt incurred after the bankruptcy
- Payments for alimony or child support
- Debts to others as a result of personal injury from intoxication
- Fines or penalties due to government agencies

Also, when you file bankruptcy, any debt forgiveness does not extend to others (such as a parent or spouse) who has co-signed on your borrowings. So, even if you relieve the debt, your co-signer is still responsible.

The Long-Term Impacts of Bankruptcy

Although filing for bankruptcy can help wipe away your debts, it can have longer-term impacts.

- A bankruptcy filing will stay on your credit history for seven to ten years (this might affect your ability to get credit).
- Your credit report will be marked as "charged off" for any accounts filed with the bankruptcy.
- Insurers, employers, landlords and anyone else who pulls your credit report may see your bankruptcy as an indication of mismanagement.
- If you can obtain credit afterward, you may be charged higher interest rates, asked for higher down payments or asked to put up collateral until your credit is repaired.

Following a bankruptcy, you will need to be diligent to pay your debts on time, every time, for a long time to help rebuild your credit history.

MAKE A "SAM" PLAN

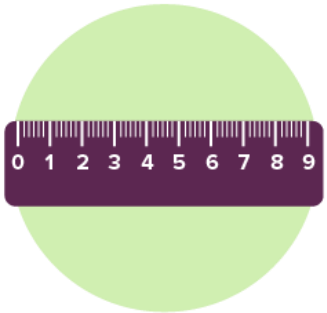
No matter what your credit and debt goals are, your plan begins where you are right now.

Use the SAM action steps to analyze your current credit and debt situation and take purposeful steps toward identifying or making changes.

What does your current debt situation look like? Do you have a good plan for using credit?

What is your credit score? Is there anything in your credit report that needs to be corrected?

Set intentional goals such as improving your credit score or lowering your debt-to-income ratio.



Size Up Your Situation

Use this set of guidelines to see how you compare in your debt management. Remember though, these are just guidelines and statements of debt management; they aren't meant to make a judgement on where you stand.

How Do You Compare?

Guideline	I meet this guideline	I don't meet this guideline
Maintain a credit score of 700 or more to show good credit management. (According to US News/Money)		
Maintain a debt-to-income ratio of less than 20 percent.		
Spend under 43 percent* of take-home pay each month on fixed costs (expenses that don't change month-to-month). This would include debt plus utilities, gym memberships and any subscriptions such as cable, Amazon Prime, etc.) *According to Consumer Finance, borrowers who spend more than this are more likely to run into trouble making monthly payments.		
Know the length of time it will take to repay debts making monthly payments.		
Know the costs associated with making monthly payments.		
Know the total amount to be paid over the life of a credit extension. This includes principal, interest and any fees.		

Analyze Your Circumstances

Almost everyone has debt, but having too much debt can lead to problems financially, emotionally and physically. Check in with your debt on occasion to see where you might be leaning toward too much borrowing.

Check Your Debt Management

Use the *10 Warning Signs of Too Much Debt* from earlier in this course to assess yourself as a debt manager.

You spend more than 20 percent of your monthly take-home (net) income on consumer debt.	Yes	No
You miss payments or pay them late.	Yes	No
You have been refused credit.	Yes	No
You have overdrawn your checking account more than three times in the year.	Yes	No
You borrow to pay off other debts	Yes	No
You only make the minimum payment on bills.	Yes	No
Collectors are calling.	Yes	No
You borrow from retirement accounts or use credit cards to pay monthly bills.	Yes	No
You have to take an extra job just to pay your bills.	Yes	No

It really doesn't matter right now if you answered yes or no for most items, no one is judging your debt management, and most of us can use some help in certain areas.

To stop most credit card offers from arriving in your mail, go to Opt Out Prescreen.

Make Your Credit and Debt Plan

Good credit and successful debt management don't just happen overnight. It takes time and energy to monitor your spending and put together a plan to increase your credit profile.

1. **Set goals to improve your borrower profile**. Remember to make your goals attainable and based on where you are, not where you wish you were or where you think you should be.
2. **Describe what you will do to reach your goals**. What stands out as the first thing you can do? For example, can you get a credit report and begin paying off low balances over the next six months while maintaining (at least) minimum payments on larger balances?
3. **Monitor your progress.**
   - If you reach your goals, celebrate your successes and make more. Remember, one step at a time.
   - If you have trouble reaching your goals, assess your situation and make adjustments. Maybe you aimed too high. Keep plugging along until you feel like you're making progress.
4. **Consider credit counseling.** Just about everyone can benefit from talking about their money goals. If your debt feels out of control, look for free and nonprofit sources of financial counseling or coaching to help get you the support you need.

Extra Credit: Set Your Own Credit Guidelines

As you have seen, using credit is a valuable tool but you need to keep five key points in mind:

1. **There is a cost**. You will pay more in the end if you have to buy on credit. Borrow wisely.
2. **Don't use credit to spend frivolously**. If you can't repay with a reasonable time frame, you shouldn't borrow money to finance the purchase.
3. **Read the fine print**. Always know what you are being charged and when.
4. **Pay as much as you can as early as you can**. This helps keep your credit report in good standing and reduces compound interest and fees.
5. **Strive to achieve and maintain good credit**. If you want the best terms and rates, keep your credit report in good standing.

Consider everything you have learned about using credit wisely and these five key points. Write out a few personal guidelines you will follow when considering whether or not to use credit. Include any self-imposed rules and habits you can apply as you take on credit. For example, you might set intentions to "Charge no more than $200 on credit cards each month" and "pay credit card bill in full to avoid paying interest."

CREDIT AND DEBT RESOURCES

Are you in a credit and debt crisis? Or maybe you're just looking to go deeper into this topic? There are many free and low-cost resources available to help you. Here are a few:

2-1-1

Just as you would call 9-1-1 in an emergency, you can call 2-1-1 (www.211.org) from anywhere in North America using your phone or computer to speak to a specialist in your community who can help you find a variety of free services including:

- Disaster and emergency help
- Housing and food assistance
- Employment and education opportunities
- Help starting a business
- Help for special groups such as veterans and victims of domestic abuse

National Foundation for Credit Counseling

Get free or low-cost counseling to help you get out of a financial crisis or improve your money management. Visit www.nfcc.org or call 1-800-388-2227 to connect with these and other types of financial guidance:

- Debt counseling
- Bankruptcy counseling
- Homeownership counseling
- Reverse mortgage counseling
- Student loan debt counseling

Get Your Free Credit Report

Get your free credit reports from Equifax, Experian and TransUnion at www.AnnualCreditReport.com.

Consumer Financial Protection Bureau

File a complaint about a financial product or service at www.ConsumerFinance.gov and dig deeper into how credit cards work at www.ConsumerFinance.gov/credit-cards.

Federal Trade Commission

The FTC has many helpful consumer pages, including information on identity theft, disputing credit card charges and correcting errors on your credit report.

Identity Theft Resource Center

Learn how to protect yourself and what to do when your identity is stolen at www.IDTheftCenter.org.

Bankruptcy Counseling and Advice

The federal courts administer bankruptcy and will require that you seek credit counseling through one of the U. S. Courts approved organizations. Although you can file on your own, you probably will want a lawyer to help you file for bankruptcy. Your lawyer can help guide you to the type of bankruptcy to file and guide you through the long-term impacts.

After you file for bankruptcy, you also must complete debtor education through a U. S. Courts-approved provider.

CONGRATULATIONS!

You have completed the Credit and Debt Basics course. Check out SAM's other free courses to continue your personal finance journey:

Disclaimers

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