Module 12
GETTING AND MANAGING CREDIT

Let's Discuss...

- $ **Credit Worthiness – the "3 Cs"**
- $ **Credit Rating**
- $ **Advantages and disadvantages of credit**
- $ **Signs you may be in debt trouble**
- $ **What to do if you have a debt problem**

Your Credit Worthiness

If you want or need to borrow money, you will have to make sure the possible lender is confident that you are able to pay back the loan. Credit is the ability to acquire goods or services prior to payment with the faith that the payment will be made in the future. In most cases, there is a charge for borrowing, and these come in the form of fees and/or interest.

Think About It

When might someone need a loan? When might a person want a loan? What's the difference? Be aware that it may be harder to get a loan when you need it than when you don't.

Anyone thinking of lending you money will be interested in your "credit worthiness." Your credit worthiness is simply a lender's check on your ability to take on, carry, and pay back debt. To check your credit worthiness, a lender will consider the "3 Cs" – your capital, character, and capacity. These aren't the only things that will be of interest to the lender. Your "credit rating" will also be very important. More on that shortly. But let's look at the 3Cs so that you know about some of the things that might affect your chances of getting a loan.

Skoden! Stoodis!

Try and arrange to have some credit available to you – even when you don't need it. Don't use it – just have it available in case you do need it. You may do this by the credit limit you have on a credit card or through a "line of credit" you set up with your financial institution. For students that need access to funds while attending an accredited Canadian university or college this line of credit features a low interest rate specific to you. You pay interest only on the amount you actually use while you are in school, and the year following your graduation or residency.

Capital

This refers to things you own. They have value and could possibly be sold if money was needed to pay back the loan. As you may know, things you own that have value are called “assets.” Your assets can include any “equity" you have in a house (that part of the house that you own – the value of the house minus the mortgage), stocks, bonds, cars, savings, and so on.

As a borrower, you would probably not have any intention of selling these assets or cashing them in to pay back the loan. However, if for some reason you were unable to make the payments or pay back the loan in full, then the lender wants some protection. The lender would like to know what assets you own that could be cashed in or sold (“liquidated”) to get the money needed.

Assets that you use to “secure” a loan – show you could find a way to pay back a loan if need be – are called “collateral.” The problem some people face is that they may not have much collateral to back a loan.

In that case, the lender may ask for someone to “co-sign” the loan. A co-signer is someone who will agree to pay back the loan if the borrower, for some reason, is not able to repay. Asking someone to co-sign a loan is asking them to take on a serious responsibility. And being a co-signer is taking on considerable responsibility. Any co-signer should be careful before co-signing a loan – a loan he or she may have to help repay.

So your “capital” is the assets that you have, to provide some possible “collateral” if needed. If you don’t have capital, the lender may ask for a co-signer – another person who will take on some responsibility for the loan. Now, how about your character?

How About You?

Do you have any “assets” at the moment? You may not use them to get a loan – but many young people sell things they own to get money, e.g. computer games, used sports equipment, used musical instruments, used bikes, etc. These are things of value – assets – since they can possibly be turned into money by selling them.

Character

When you apply for a loan, the loans officer will also be interested in your “character” – how responsible you seem to be and how reliable you are likely to be in repaying the loan.

Some of the questions that you have to answer on a loan application may surprise you. You may be asked how long you have worked at your current job, how long you have lived at your current address, and whether you have incurred any other debts, whether you are married, and if you have any dependents.

Why such questions? The lender (creditor) will be looking for signs of “stability,” “responsibility,” “reliability,” and so on. Being with an employer for quite a while, living at the same address for some time, being married, or having children or other dependents tend to be signs of stability and that you have taken on responsibility. This doesn’t mean that you can’t get a loan if you aren’t married with two kids and haven’t worked and lived at the same place for ten years. It also doesn’t mean that you will get a loan if you have. It does mean that if you have changed jobs frequently, are unemployed, or have moved from place to place, or have been married three times you may encounter some hesitation from loans officers when you apply for a loan. The lender will be looking to learn something about you – and the kind of person you are. You would probably want to know something about a person who asked you for a loan too.

We've looked at your capital (what you own) and your character (indications of the kind of person you are). Now how about whether you can afford the loan? That's your capacity.

Think About It

Of people you know well, who would you be willing to lend money to if asked – and if you had the money to lend? Are there others to whom you wouldn't lend money? If so, why not? What differences are you thinking about when you consider whether you would lend them money or not?

Learn About

Check out online what it would cost per month to carry different size loans at different interest rates. For example, see what the monthly cost is for a 5 year loan of $10,000 at 7% interest. Check out a variety of other loans for different amounts of money, for other lengths of time, and different rates.

Think About It

If someone asked you for a loan, what might you want to know about them before making your decision? Would you lend money to you at this point? Would you be a good "credit risk?" What changes are likely to happen in your life that may change your credit risk?

Capacity

The creditor will also want to know if you can afford the payments on the loan. Do you have enough income to pay the monthly cost? Do you have other expenses that may make it hard for you to make the monthly payments? Do you have other debts? What you own, what you owe, and what you earn will be of interest to the possible lender.

These, then, are "the 3 Cs" that help to show your credit worthiness – and whether you are a credit risk. However, your credit rating will probably be as, or more important, to the lender if you are looking for a loan.

Credit Rating

Many people don't know a credit rating system exists. But it does. Those who are in the business of lending money share information. They share information about people to whom they have loaned money. They share information about those who have been good in repaying their debts – and making payments on time. They also share information on those who have not been so good – or who regularly make payments late – or who have not paid their debts.

For example, suppose you purchased something from a store on a credit card. Then, for some reason you did not pay the charges on the card. If that happens, the credit card company will probably first try and get you to pay the charge. If you still don't pay, the credit card company may notify the "credit bureau." And that can go on your record and may affect your ability to borrow money.

There are a number of "credit rating agencies" that keep this information. For example, two large agencies in Canada are "Equifax" and "TransUnion Canada." They keep records on people who borrow money – who they borrow from, how much they have borrowed, how good they are at repaying their debts, and so on. They also have information on bills you may not have paid – and should have. Based on all the information they have, they will calculate a credit score. The credit bureaus will make the information they have available to other lenders. Therefore, before making a loan, lenders will usually check with the rating agencies and check out your credit score.

Credit scoring models generate credit scores based on the information pulled from your credit report. If you do not use credit accounts, you will not have a credit report, and thus, you will have no credit score. You are "credit invisible" or "unscored."

Now here is a very important point. You can go to these companies to check out your credit report – and you should. You may find things there you didn't know about – or you may find things that are wrong. A lender may have sent in notice that you didn't pay a debt – but you did, only late. But it may show on your credit rating that you never paid the debt – and that won't help your credit score.

Most creditors will work with a borrower to try and help the borrower repay the loan before providing any information to the credit bureau that would hurt a person's credit rating. After all, their goal is to get their loan back or have the bill paid. They may work out new terms with you to help you. That is why it is always important to contact the creditor if you are having problems repaying a debt or paying a bill that is overdue. You can often work out a payment plan. However, if a creditor does not hear from you, they may simply assume you aren't going to pay what is owed and send that information to the credit bureau.

Before information is sent to the credit bureau, people who are having trouble paying their debts or bills will often be contacted by a "collection agency." A collection agency will work for those to whom you owe money. Their job is to try and get you to pay.

It is best to get in touch with anyone to whom you owe money – and haven't paid – before they get a collection agency to get in touch with you. If you are contacted by a collection agency about a debt, take this as a warning and deal with the matter right away so that you don't end up with a negative report going to the credit agency.

Indigenous Financial Institutions (IFIs) are autonomous, Indigenous-controlled, community-based financial organizations. The IFI network plays a critical role in filling the financing gaps and unmet needs faced by Indigenous entrepreneurs. IFIs make loans that conventional financial institutions cannot, by identifying risks and then mitigating those risks by helping Indigenous entrepreneurs avoid them. IFIs have become experts in risk assessment, mitigation, and management for Indigenous entrepreneurs and communities.

Even if you don't have any intention of borrowing money, you never know when the need may arise. It is always wise to be able to borrow money just in case you have to some day. That means having a good credit rating.

How About You?

How can you establish credit?

1. Apply for a department store or gasoline credit card. The idea here is to start small and work your way up.
2. Buy something, make a big down payment, and make payments on the rest.
3. Apply for a small loan with your bank or credit union.
4. Apply for a secured credit card.

Skoden! Stoodis!

Go online to the two credit agencies to see if you have a credit rating. If so, you may want to check and see if the information is correct. If you don't have a credit rating now, check back now and then to keep an eye on it. You should always be in touch with your credit rating. It's important.

Skoden! Stoodis!

If you have trouble making loan payments, paying back a loan, or paying a bill that you owe, contact whomever it is you owe money to. Let them know you are having some difficulty. See if they can work with you to help. Try to do that before the matter is put in the hands of a collection agency – or recorded at the credit bureau.

The following are some tips for maintaining a good credit rating:

- Repay your debts and make payments on time.
- Don't borrow more than you can afford.
- Set a borrowing limit and stick to it. This sounds easier than it is. Most people don't know how to set a credit limit – that is, the maximum amount you can afford to borrow. Here is one suggestion. Set up a budget. (See the Module on budgeting.) As you do, see how much you could afford each month for debt payments. That amount should help set your debt limit. If you borrow money, don't borrow more than could be covered by the limit you have set.

  The cost of a loan will vary with how much you borrow, how long you will take to pay it back, and the interest rate. Therefore, the maximum amount of debt that you can comfortably afford to carry will change as these things change. Try to stay in your "comfort zone" and borrow only what you can afford.
- Don't sign any kind of loan agreement until you have read it thoroughly, understand it, and know what you are getting into. Sometimes you may feel a little awkward doing this. It may be a person you know. Or the person may make it seem like time is short and you should hurry – or that this is just standard stuff and you shouldn't worry about it. Or it may be that the document is quite lengthy and may take some time to read over. Don't let that stop you. Most people will understand that you want to read what you are signing. If they don't, it may be because they really don't want you to read it. Even if you feel awkward, take the time. It is a small price to pay to be comfortable with what you are signing.
- Never sign a blank form of any kind where information could be filled in or added after you sign
- Always try to pay your monthly bills on time (like phone, electricity, etc.)
- Contact your creditors if you are having trouble making payments on your debts.
- Deal with reputable creditors (they should have a good credit rating too).
- Be cautious about co-signing for a loan.

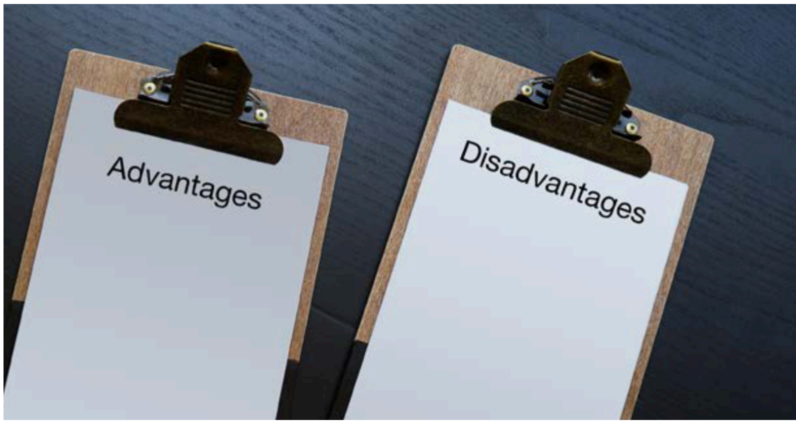
Skoden! Stoodis!

Don't just wait for your credit rating to be built up by others – try and build a good credit rating for yourself. If you can borrow some money without paying interest – like with some credit cards – and pay it back promptly and in full – consider doing this to build a good rating. Also, if you rent an apartment and pay electricity bills (on time), and phone bills, (on time), etc., this will show on your credit rating. So don't just let your credit rating happen. Try and do some things, as you can, to build a good credit rating.

As we noted, co-signing a loan is a serious responsibility. A parent may co-sign a loan for a child if the child is still relatively young and needs help with borrowing money. That is quite common until there has been time for the child to build up a credit rating. But always think carefully if you are asked to co-sign for a loan. It may affect your own credit rating if things go wrong. It's also a good idea to start to develop a good credit rating as early as possible. To do this, some young people decide to get a credit card from a retailer or credit card company, make purchases, and pay off the bills promptly and fully each month. In this way, a good credit rating can begin to be established even at a relatively young age. Many people borrow money by using a credit card or taking out loans to buy things. How you use a credit card or manage a loan can affect your credit rating. Let's take a look at some of the advantages and disadvantages of using credit through credit cards and loans.

The Advantages and Disadvantages of Credit

There are many advantages and disadvantages of credit. This a great discussion you should have with your family, trusted mentor, Elder, or leadership.



Advantages

- You can use something and enjoy it now (for example, a car, a house, a vacation, education, new clothes) and pay for it out of future income.
- You can buy things you could not buy from your current income. You can use some of your future income to pay for it.
- Credit enables you to handle emergencies and unexpected costs due to an illness, accident, losing a job, car repairs, and so on.
- Credit can enable you to pay more to buy goods of higher quality that you otherwise could not afford now. Buying better quality can mean it will last longer. That may make it a wise consumer choice.
- You can take advantage of sales and deals – if a really good one comes along. (Just make sure that the amount you save through the sale is more than it may cost you in interest.)
- Using a credit card provides you with a record of your expenses. Credit card issuers provide a monthly statement which lists all of the spending you did with the credit card.
- Credit can make it easier to deal with a number of debts you have if you are having difficulty repaying. By taking out a "consolidation loan" you can borrow one amount to pay all or most of your bills and then make a single payment each month rather than many.

Disadvantages

- Credit can encourage you to live beyond your means and get you into financial difficulty.
- Credit can mean that your future income will be tied up in paying past debts. You may not be able to buy things in the future that you wish you could.
- Using credit can increase your total cost for a product or service since the interest you will pay must be added to the price.
- Credit can lead to more impulse buying, which may lead to buying things you don't really need – and wish you hadn't.
- If you get and use a credit card for a particular store, you may just shop there and do less comparison shopping. You may lose out on cheaper prices or better deals elsewhere.
- Tapping into credit now will mean that you will have less available if unforeseen emergencies arise.

One way to keep a good credit rating is to avoid getting into debt trouble. When you "get in over your head" and have more debt than you can afford, you can start missing payments, paying late, or not repaying your debts. That can lead to problems with your credit rating. So avoiding debt trouble in the first place is the wise thing to do. But how do you know if you are heading toward debt trouble? Let's take a look at some of the signs that you may be headed in the wrong direction.

Signs That You May Be in Debt Trouble

You may be heading for debt trouble if you find you are:

- finding it difficult to save anything.
- continually short of money.
- using your savings to pay debt costs.
- near your credit limit on all or most of your credit cards and accounts.
- missing payments or due dates for your bills.
- always making only the minimum payments on your credit cards and accounts. Each month you will likely see a "minimum" monthly payment on your credit card statement. This is the minimum amount that the lender is willing to take as payment for that month. It is not the minimum you would be best to pay. The best thing is to pay off the full amount. If you can't, pay off as much as you can. If you just make the minimum monthly payment it can take a long time to pay back the money – and you end up paying a great deal of interest.
- unaware of how much you owe.
- worrying a lot about money – your debts are always on your mind – you are having trouble sleeping.
- borrowing money to pay off past debt costs.
- having to borrow money to meet your week-to-week or month-to-month living expenses.

How About You?

Do any of these signs apply to you? Even at a young age, are you possibly heading for some debt problems or are you well in control? What do you see as your likely "debt future?"

What To Do If You Have a Debt Problem

Do all that you can to avoid debt problems. Know how much debt you can afford and don't go over that limit. Set up a budget so you know how much debt you can afford. Don't borrow to that limit – leave yourself some room in case something comes up. Think about the trade-offs you are making when you borrow money – and borrow only when it is a good decision for you.

But in the end, some people will get into debt trouble. What can you do if that happens? Banks in Canada recognize the need to foster a more inclusive and sustainable future for Indigenous individuals, businesses and communities. For more than 25 years, Canada's major banks have provided tailored banking, borrowing and investment services for Indigenous businesses, governments and families through specialized Indigenous Banking Teams.

- Perhaps the most important advice for you if you are having debt troubles is to face up to your problems and start to do something about them. Don't try to handle it all alone. If you have close personal friends or family, seek their help and advice. They can also help you deal with what may be a bad situation. You will probably be surprised at how many people will understand and will try to help see you over a rough period.
- Contact your creditors. Don't simply start missing payments. Most of those who have loaned you money will try to help you get out of the hole you are in. After all, they have an interest in helping you – they hope to get their money back. Work out a new payment schedule with them. You will probably be surprised at how co-operative most creditors will be.
- Put all of your credit cards away to avoid getting into worse trouble. In fact, stop all further borrowing. No sense digging a deeper hole.
- Consider a consolidation loan for your debts. A consolidation loan is one loan you take out to pay back your other loans. In this way you can turn a number of payments for a number of different loans into a single payment for one loan. The monthly cost may be less than the total monthly cost of all other payments combined. If you are carrying debt on credit cards, the interest you will pay on a regular loan will usually be much lower than that on a credit card balance.

- Consider a second job, if you can, to see you over the hurdle and tough times.
- Cash in some investments or savings to lower your debt position. The costs you pay on your debt will usually be greater than the interest you earn on your investments. It may make sense to give up the investment to do away with the debt.
- Seek some professional advice and credit counselling if you can get it – or if someone will help you get it.
- Review your lifestyle and past decisions. What got you into trouble? What could you change to get out of trouble? What can you give up to get money to help you pay your debts?

When it comes to handling money, and making good money decisions, few things are more important than getting and keeping a good credit rating. Right from the outset, make that one of your priorities. Debt can help you – or debt can hurt you. Borrow wisely. And always stay within a limit you can afford.

Module Summary

Say What? Possible New Terms!

1. **Capital:** the assets you own – things of value – things that could be sold or cashed in, if needed, to help pay back a loan.
2. **Character:** things about you that indicate your degree of stability, responsibility, and reliability.
3. **Capacity:** your ability to make payments on a loan – usually determined by your income.
4. **Credit rating:** a score that indicates your history of managing and paying your bills and debts.
5. **Collateral:** something of value that you put up in support of a loan and that could be sold, cashed in, or given to the lender if a loan can't be repaid.
6. **Co-signer:** a person who signs a loan agreement who is willing to pay back the loan, or what is owing on a loan, if the borrower can't repay.
7. **Consolidation loan:** one loan taken out to pay off a number of debts to make one payment monthly rather than a number of payments to hopefully reduce the monthly cost.

Did it Stick? Can You Recall?

1. What are the "3Cs?" Why are they used?
2. What is your credit rating? What kinds of things can affect your credit rating?
3. How can you build a good credit rating?
4. What are some signs that you might be heading toward debt problems?
5. What are some things you can do if you have debt problems?
6. What are some of the advantages and disadvantages of using credit cards and loans?

Thinkabout… or Discuss

- How can a young person build a good credit rating?
- Is it too easy for young people to get credit these days?
- What leads some young people to get into debt difficulties at a young age?
- How might borrowing help a young person as he/she tries to build a successful future and achieve goals?

Tips & Suggestions

- Protect your credit rating. Pay bills – and pay them on time. Pay debts – and pay them on time.
- Know your credit limit – and stick to it. Know what you can afford – and leave some room if you can in case surprises come along.
- Know how borrowing can help and use it to your advantage. Know how borrowing can hurt, and avoid debt issues.

Tech Talk

If you can, use the Internet to:

- See if you have a credit rating – and, if so, check it out.
- Compare the cost of carrying different amounts of loans over different periods of time at different rates of interest.
- Search:
    - Building and keeping a good credit rating
    - How to pick the right credit card
    - Signs of debt trouble
    - Credit Canada – Debt Solutions
    - Financial Consumer Agency of Canada