

Understanding Credit

“Some debt—such as for a modest home, expenses for education, perhaps for a needed first car—may be necessary. But never should we enter into financial bondage through consumer debt without carefully weighing the costs.”

(Joseph B. Wirthlin, “Earthly Debts, Heavenly Debts,” Ensign, May 2004, 41)

OBJECTIVES

This lesson strives to teach family members the importance of credit in accomplishing financial goals, and to teach them to manage credit wisely to improve their credit scores.

WHY?

We use money to purchase things that we need here in mortality, but we are to prove that we can be wise stewards over our money. It is important for family members to learn that although credit card offers come in the mail almost daily, it is not free money. Credit cards can be very useful and necessary, but if not governed correctly, they can lead to serious heartache. Debt is enslaving and can control you. It is important to learn about credit so that the family can know how their decisions with credit cards can affect them for the rest of their lives.

LESSON

What Is Credit?

In personal finance, credit is the granting of a loan and the creation of debt. In other words, credit is the financial trust a lender has in the borrower. Creditworthiness is based on your demonstrated ability to pay back on time what you have borrowed.

Factors That Determine Credit Worthiness

- Annual income
- Time at current residence
- Time at current job
- Age
- Employment
- Number of bank accounts
- Number of credit cards
- Credit history

Anytime you borrow money that has to be paid back you are using credit. Borrowing can be in many forms (e.g., a credit card or other loans, such as a car loan or mortgage). Of course, to get something now and pay for it later, you’ll have to pay the lender a fee, called “interest.” Interest is a percentage of the amount you originally borrowed, called the “principal.” Because of interest it is more expensive to buy on credit than to buy with cash.

The higher the rate of interest, the more expensive it is to borrow, and the harder it is to pay back.

Why Use Credit?

Most young adults don't have enough money (cash) in savings to pay for the entire cost of a house, car, or other expensive items. Using credit can be an investment if it's for things that increase in value the longer you have them.

Elder Joseph B. Wirthlin of the Quorum of the Twelve Apostles said, "Some debt—such as for a modest home, expenses for education, perhaps for a needed first car—may be necessary. But never should we enter into financial bondage through consumer debt without carefully weighing the costs" ("Earthly Debts, Heavenly Debts," *Ensign*, May 2004, 41).

President Gordon B. Hinckley has said, "Debt can be a terrible thing. It is so easy to incur and so difficult to repay. Borrowed money is had only at a price, and that price can be burdensome" (*Ensign*, Mar. 1990, 4).

Credit Reports

- A credit report lists all the lines of credit you have, what the balances are, and whether you've made your payments on time.
- All of this information is combined to create a credit score that tells lenders how likely you are to repay a loan. The higher your score, the more lenders will trust you to make your payments on time.

Reasons to Have a Good Credit Score

- You can get lower interest rates on loans.
- Your credit score is referenced when you apply for a job, when you rent an apartment, when you buy a car, and when you buy a house
- Cell phone and utility companies may charge you a deposit before giving you service if your credit score is low.
- Your credit score influences how much you pay for car insurance.

Elder Joseph B. Wirthlin said, "Remember this: debt is a form of bondage. It is a financial termite. When we make purchases on credit, they give us only an illusion of prosperity. We think we own things, but the reality is, our things own us" ("Earthly Debts, Heavenly Debts," *Ensign*, May 2004, 40).

President Heber J. Grant said, "From my earliest recollections, from the days of Brigham Young until now, I have listened to men standing in the pulpit . . . urging the people not to run into debt; and I believe that the great majority of all our troubles today is caused through the failure to carry out that counsel" (In Conference Report, Oct. 1921, 3).

Our Prophet has said "I urge you to be modest in your expenditures; discipline yourselves in your purchases to avoid debt to the extent possible. Pay off debt as quickly as you can, and free yourselves from bondage" ("To the Boys and to the Men," *Ensign*,

Nov. 1998, 53–54).

Credit Cards

- Credit cards are a way to utilize credit. A credit card is basically a monthly loan, usually with a grace period to pay back the money borrowed. Each card has a limit, or maximum amount of money you can spend with that card. With most companies, you have until a certain date each month to repay your purchases before they start accruing interest.
- If not used in the right way, credit or consumer debt can cause problems. Credit card debt is particularly expensive.
- Interest rates on credit cards can become very high.
- Late payments result in fines and even higher interest rates.
- If you don't pay your balance in full, the amount you owe the credit card company will increase until you pay off your full balance.

Having a debt on your credit card is like agreeing to give someone a bigger and bigger portion of your paycheck each month.

President Monson said, “This is a day of borrowing, a day when multiple credit card offers arrive in our mailboxes each week. They generally offer a very low rate of interest which may apply for a short period of time; but what one usually doesn't realize is that after that period has expired, the rates increase dramatically. I share with you a statement made by President J. Reuben Clark Jr., who many years ago was a member of the First Presidency. Its truth is timeless. Said he:

‘It is a rule of our financial and economic life in all the world that interest is to be paid on borrowed money. . . .

“Interest never sleeps nor sickens nor dies; it never goes to the hospital; it works on Sundays and holidays; it never takes a vacation; it never visits nor travels; it takes no pleasure; it is never laid off work nor discharged from employment; it never works on reduced hours. . . . Once in debt, interest is your companion every minute of the day and night; you cannot shun it or slip away from it; you cannot dismiss it; it yields neither to entreaties, demands, or orders; and whenever you get in its way or cross its course or fail to meet its demands, it crushes you.” (Thomas S. Monson, “Constant Truths for Changing Times,” *Ensign*, May 2005, 19)

Tips for Building Your Credit with Your Credit Card

- 1) Get one credit card and pay off the balance every month. Pay your bills on time!
- 2) Stay away from store credit cards. Store cards don't help your credit rating much and can even hurt it if you have too many or forget to close an account you're not using.
- 3) Open new accounts only as you need them. Don't open a lot of new credit accounts at once. The more new accounts you have, the lower your credit score.
- 4) Find the best deal. When shopping for a credit card, look for one that has a low, fixed interest rate. Be wary of “introductory” or “teaser” rates that start off very low but jump after a few months.

- 5) Try to get a card that has no annual fees and that offers some kind of reward, like cash back, for using it (like Citibank cards).

Tips for Finding and Using Your Credit Card

- Shop around for a credit card with a low interest rate and no yearly fees.
- You can make payments on your credit card anytime, including before you receive a bill.
- Pay the monthly balance in full, period.

Credit Card Safety

- Sign the back of your card as soon as you receive it.
- Never let anyone borrow your credit card.
- If your credit card is lost or stolen, report it immediately. You are not responsible for any unauthorized purchases if you report the card missing before they are made.
- Go over your monthly bill carefully to make sure all charges are correct.
- If you need to contest a billing, call the company's customer service number.
- If you decide to discontinue using the credit card, simply cutting it up isn't enough. You must call the company and cancel your account as well.

STORY AND DISCUSSION

For the first few months that Steve had his credit card, it stayed in his wallet. But in the last three weeks of his freshman year in college, Steve went on a spending spree. “After a year of living on a few hundred dollars a month, I decided to go have some fun,” says Steve.

With his credit card he paid for weekend trips and new clothes. By the time he went home, he had racked up charges nearing his credit limit. As a result, he spent the summer before his mission working frantically to pay off the debt. “It wasn’t a positive learning experience,” says Steve. “At the time, I didn’t realize that a credit card doesn’t expand your income now; it shrinks your future income because of debt.”

Questions:

What could Steve have done differently?

What rules of credit did Steve not understand?

What could Steve's parents have done to help him understand credit better?

For Grade School Children:

Judy has the option of using cash or spending money with a credit card.

Questions:

What should Judy do?

Why should Judy do that?

Why is it important for Judy to be careful with her credit card?

ACTIVITY

Family Pie Chart (for younger children)

To help show the family the importance of not going into bad debt and to cut out unnecessary spending, this is a good activity. Present a color-coded pie chart that illustrates the percentage of income that is spent each month for the family's food, clothing, medical needs, transportation, music lessons, and other items. Explain that it shows proportions of the income are spent on the family's needs. This way, they can see expenses comparatively. This is a good way to get suggestions from the family on how they can cut expenses.

Card Guessing Game (for older children)

Find different things that can improve or decline your credit score. Write them on different index cards. Show them to members of your family and have them determine and guess whether or not they would increase or decrease your credit score.

ASSIGNMENTS

1. Keep a spending journal and record everything that you spend for a week. At the end of the week, we will look at spending patterns and see if we can encourage more saving.
2. Write in your journal three big things you want to use your money for in your life. Think about how you can save for those things and write your feelings about money.
3. Find a situation to teach two of your friends about credit. Ask them what they have been taught and then discuss some of the principles that we have learned from our prophets.

SUGGESTED SONGS

“Count Your Many Blessings” – Hymn #241
“Choose the Right” - Hymn #239

OTHER RESOURCES

- ”Taking Credit!,” Danielle Nye Poulter, *New Era*, Aug 2006, 10–13.
- “Fantastic Plastic?” Elyssa Renee Andrus, *New Era*, Apr 2001, 32–35.
- “The Dangers of Debt in Marriage,” Rulon T. Burton, *Ensign*, Sep 1984, 49.
- “Earthly Debts, Heavenly Debts,” Joseph B. Wirthlin, *Liahona*, May 2004, 40–43.
- “Guide to Family Finance,” Marvin J. Ashton, *Liahona*, Apr 2000, 42.
- “Where’s All Our Money Going?,” *Ensign*, Apr 1990, 49.
- “Constant Truths for Changing Times,” Thomas S. Monson, *Liahona*, May 2005, 19–22.
- “Earthly Debts, Heavenly Debts,” Joseph B. Wirthlin, *Liahona*, May 2004, 40–43.

AUTHORS

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