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# ARE YOU DROWNING IN DEBT?

Do not be a man who strikes hands in pledge
or puts up security for debts; if you lack the
means to pay, your very bed will be
snatched from under you.
—Proverbs 22:26-27

Tears ran down Jane's face as she and her husband sat across from me. She had lost her job the previous day, and their world was turned upside down. They had bought two investment houses with plans to rent them out for one year and then sell them for profit. Instead, the market took a downturn, and the properties were worth less than they paid for them. Not only that, the mortgage payments were more than the rent they were receiving. Every extra penny they got their hands on had to go toward the payments on the rentals and the mortgage on their own home. They had used the equity in their home to buy the investment properties. Without Jane's income, they had no idea how they could make it.

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Sarah called the office, frantic because she was behind on her bills. Collection agencies called her constantly. She could not sleep, and she was a nervous wreck. She wanted me to tell her what her options were.

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Jack and Mary were in a state of gloom when they contacted our office. Their bills totaled more than their income, and they didn't know what to do. They fought regularly about money, and their marriage was suffering.

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These are typical situations that credit counselors deal with.

Did God cause these problems? No. Then who is to blame? The first thing these folks and others must do is take *responsibility* for bad financial decisions they have made. The Bible warns us repeatedly to stay out of debt and to seek wise counsel. Psalms and Proverbs both contain many scriptures pertaining to money.

## HOW DID I GET HERE?

Many people don't realize the importance of establishing credit and the responsibility of maintaining it. They see credit as a kind of blank check and don't keep track of what they're spending. Believing they can pay tomorrow for what they're enjoying today, they run up their debts. Before they know it, money trouble is looming.

No one sets out to get deeply into debt; it creeps up slowly. Most people are sincere in their intention to pay that credit card balance in full. The problem is that all those little purchases have added up to a balance that the budget can't support. Making only the minimum payment feels so much better.

High school doesn't teach it, college doesn't teach it, and parents rarely teach it: the importance and responsibility of using credit wisely. Those who reach adulthood with no education on managing money and debt are extremely vulnerable to financial disaster.

Frequently clients who come for credit consulting say to us, "If I had only known the importance of handling money, I would have done things differently."

Those who are prone to financial disaster usually have at least one of the following three personality traits: (1) eternal optimism, (2) believing in dreams, or (3) believing that things will get better if they just wait it out.

A person who has one or all of these personality traits runs an increased risk of succumbing to "big-deal-itis." People like this tend to live for the future and never face the present; they grab what they can right now without any concern for tomorrow, because the big deal is just around the corner. They live in perpetual denial.

These are the persons who have more bills to pay than money with which to pay them—you know, the ones who use credit cards as they would a blank check. Are you one of them?

Proverbs 16:20 says, "Whoever gives heed to instruction prospers, and blessed is he who trusts in the LORD." It is difficult to trust in the Lord when we're slaves to our wants and must-haves to satisfy the need for material things.

With no vision, no plan, no discipline or direction—and no one to come to your rescue—disaster just sits and waits.

A person without vision can't see what may be ahead and doesn't learn how the credit system works or how to manage debt. Once in debt, this person is left to wonder, *How did I get here?*

Without a plan to retire the debt you've incurred, you're stressed out and have difficulty sleeping. You feel overwhelmed. Prayer is absolutely essential, but it's important that you make a realistic plan tailored to your situation. We'll present several different strategies to help you formulate your plan.

No plan will work, though, if you don't exercise discipline. It's through planning *and* discipline that you'll achieve freedom from debt—and inner peace. You'll sense the yoke of bondage lifting from your shoulders as you take these first important steps.

You must have a financial roadmap to keep you moving in the right direction. In the following chapters we'll help you map your course from where you are right now to the end of your money trouble.

We know how upsetting and discouraging it is to feel that all is lost. Being overextended and drowning in debt, with bill collectors hounding you, makes you feel as if no one else has ever been in such a mess. Don't give in to discouragement—there's light at the end of the tunnel.

As the economy struggles, desperation rises; companies are closing their doors. At this writing, the real estate market is in decline, and people find themselves owing more on their homes than their homes are worth. With the uncertainty caused by declining markets, the rising cost of utilities and groceries, and the discouraging news of layoffs and cutbacks, many are trying to cut back on spending. Some have resorted to using credit cards and equity lines

of credit to pay their bills. Renters are being pushed out of their homes because landlords can't afford the payments and the bank is foreclosing. Homeowners can't tap into their home equity because the banks have frozen lines of credit. Those with adjustable-rate mortgages face higher house payments.

With a downturn in the economy, many of us suddenly face a mountain of debt and no plan to conquer that mountain. Banks, department stores, and credit card companies love us when we pay on time; that love turns to aggressive collection tactics if we fall behind with payments.

Here's something to think about: If you hadn't borrowed and charged, would you be living without some of the luxuries you now enjoy? By "luxuries" we mean those things that can't really be classified as necessities: eating out, the to-die-for wardrobe, toys such as the big-screen television set and state-of-the-art computer, the latest and greatest gadgets for our children. Have these kinds of purchases led to excessive debt? Three little words open the door to the beginning of the end: *small monthly payment*.

Being knowledgeable about the use of credit and other financial matters empowers you to use self-control and avoid a financial crisis, whether it's here or is approaching.

## ANNIE'S STORY

When we first met with Annie, she and her husband, Ben, were struggling to pay their bills. They had excessive debt, and two of their credit cards were delinquent. We instructed them to contact their creditors and make payment arrangements.

Several months later, Annie phoned us again to tell us that their situation had gotten worse. They had acquired $25,000 in credit card debt, and all their credit cards had become delinquent. They didn't own a home, so an equity loan wasn't a consideration. They had no assets.

Annie explained that both she and Ben were employed and also had a side business. Instead of paying their credit card bills,

they were putting all extra money they had into the business. They were waiting for a "big deal" to come in so they could pay off their credit cards.

As soon as we heard about the "big-deal-itis," we knew they weren't living in the real world. This wasn't a new story to us. We had heard it over and over again from others who had gotten into side businesses or were self-employed and owned their businesses, to name just a few. As a matter of fact, we related to this because we had been down that road and quickly discovered that most big deals don't ever happen. As a matter of fact, if reality doesn't sink in really fast, people counting on a big deal to save them end up filing bankruptcy, which is exactly what Annie was considering.

Prayer works, but you also must get out of your comfort zone and take action. Your prayer should be for God to grant you knowledge and discipline to create a plan to help you overcome this financial crisis you face. Optimism is fine as long as you're also realistic in taking care of the immediate needs of your family and yourself.

Annie said that once the big deal came, they would pay off all their credit cards. But in the meantime she was having trouble dealing with the creditors who were calling and demanding payment.

We told Annie to not look at the big deal as their ticket to freedom but to look at it as icing on the cake. The proceeds of the big deal, if it materialized, should be added to what they are already doing financially and not be counted on as the only strategy for financial freedom. It was time for Annie and Ben to face reality and get their debt under control and their finances back on track.

We encouraged Annie to make a list of creditors and make payment arrangements with each of them. Since she and Ben were both employed, there were steady paychecks coming in to help them with their plan. It was also suggested that if they felt uncomfortable talking to each of the creditors themselves, they should contact a debt management company to assist them in working with their creditors.

If Annie and Ben's big deal does come in, they won't have to use every penny of it to catch up with bills. There will be enough to put away and save.

## QUIZ TIME

Before you go any further, circle what you consider to be the correct answer to the following questions. Remember: knowledge is power, and this is knowledge that will help you get where you want to go.

1. When a credit card application arrives in the mail, before making a decision to apply, you
   a. Check the annual fees and other charges.
   b. Review the interest rates and the way the interest is calculated.
   c. Read the fine print.
   d. All of the above.
2. When a lender is deciding whether or not to approve your loan, what is the most important information the lender is seeking?
   a. Payment history from your credit report and income
   b. Number of dependents in the household and marital status
   c. Whether you rent or own your home
   d. An unlisted telephone number
3. When deciding whether to approve your credit application for a home, automobile, or credit card, the lender is looking for
   a. Your FICO score.
   b. Your debt-to-income ratio.
   c. Length of employment.
   d. All of the above.
4. When determining the cost of your loan, the most important indicator is
   a. Minimum monthly payment.
   b. Interest rate.
   c. Loan amount.

   d. Number of monthly payments.
5. If you make a partial payment other than the amount due on your credit card statement, your credit report will reflect
   a. Delinquency.
   b. Payment is current.
   c. Unrated.
   d. None of the above.
6. If you have a credit card balance of $2,000, make the minimum payment each month, and never pay more than the minimum, how long will it take you to pay off this debt? (Your interest rate will be approximately 21 percent.)
   a. Two years
   b. Four years
   c. Eight years
   d. Sixteen or more years.
7. If you're self-employed, how many years will a creditor expect you to have been in business before granting credit?
   a. Two or more years
   b. Three or more years
   c. Four or more years
   d. Five or more years
8. Creditors see a red flag and your application is immediately denied if your debt-to-income ratio (excluding your mortgage or rent payments) is
   a. Two to seven percent of your take-home income.
   b. Eight to twelve percent of your take-home income.
   c. Twelve to nineteen percent of your take-home income.
   d. Twenty percent or higher of your take-home income.
9. When you get a credit card solicitation for a pre-approved card or application and don't want to apply for the card, you should
   a. Toss it into the trash.
   b. Shred or destroy the solicitation.
   c. Call the company and say that you decline the offer.

   d. None of the above.
10. The ideal number of open accounts on your credit report should be
    a. Zero or one.
    b. Two or three.
    c. Four or five.
    d. Six or more.

## REVIEW YOUR ANSWERS

1. **(d)** All of the above. When you receive a credit card application, read every word in the application and the disclosures. There may be fees charged such as an annual fee, over-the-limit fees, late fees, returned-check fees, and others. Also, know what the interest rate is and how interest is charged. There may be a grace period from the date of purchase (approximately twenty to twenty-five days) when no interest is charged. This grace period enables you to pay off the balance of new purchases without being assessed a finance charge. If there is no grace period, interest begins accruing at the time of purchase and is calculated daily.
2. **(a)** A lender will look at your credit report closely regarding your payment history. From the information taken from your credit report and your monthly income, the creditor will determine if you can likely make the payments on the credit you're applying for.
3. **(d)** The FICO score is a numeric tabulation of several factors listed on your credit report that include payment history, type of credit you currently carry, balances compared to credit limits, open accounts, and number of inquiries. FICO scoring is an important qualification when applying for credit. If you're overextended, your FICO score will be low. In addition to your FICO score, your debt-to-income is calculated to make sure you can handle the payments. If you've been employed for less than two years, you probably won't qualify for credit.

4. **(b)** Knowing how much interest you'll be paying is the most important factor in determining how much this loan or credit card is going to cost you. The higher the interest rate, the more you're paying in finance charges.
5. **(a)** If you're having trouble making your payment, a partial payment will be reported on your credit report as a delinquency. The difference in the payment made and the payment owed is rolled into the next month. This is called a "rolling late" and will not become current until the total payment is received. This is a negative mark on your credit report.
6. **(d)** If you make only the minimum payment on a credit card balance of $2,000, it will take sixteen years and eight months to pay it off. You'll also pay approximately $2,500 in interest.
7. **(a)** You must have been self-employed for two or more years to qualify for new credit. Financial statements such as tax returns, bank statements, and a year-to-date profit-and-loss statement may be required. A self-employed person is a higher risk for the lender, because the monthly income is not stable.
8. **(d)** Credit will be denied if your debt-to-income ratio is twenty percent or higher. Even fifteen percent and above would signal the lender that you may be headed for problems.
9. **(b)** If you get a credit card solicitation for a pre-approved card or application and don't want to apply for the card—shred it! Failing to do so leaves you open to identity theft.
10. **(b)** The ideal number of open accounts is two or three. You don't need more than that to show a payment pattern.

## SCORING

**9 to 10:** Good job! You have good credit knowledge.

**5 to 8:** Be careful. Examine all solicitations and know what the contracts state. That means reading the fine print. Do your homework when applying for credit, and make sure you aren't going to be overextended and have more debt than you can afford.

**0 to 4 correct:** Watch out! Learn all you can about credit and debt. You could easily make a wrong decision that will result in excessive debt and financial problems.

## TOUGH TIME TIPS

- Learn all you can about how the credit system works.
- Establish a plan to get out of debt.
- Be disciplined to avoid spending.

Knowledge is power in breaking free of debt and managing your finances.