Financial Capabilities: Understanding Credit and Debt

Sarah Spunt: Good afternoon, everyone. We are excited for you to be with us for the session on "Financial Capabilities: Understanding Credit and Debt." We'll be talking about credit and debt with families, and we know that that is very personal and overwhelming. In this session, we will build family workers' understanding of credit and debt, and explain how it's important for families' long-term economic mobility, and share tools and resources that are designed to help families develop a plan to increase their credit and decrease their debt.

Now we know as family advocates, we work with many different types of families and many diverse families. Some of the families that we work with do not have access to traditional credit-building opportunities or traditional banking opportunities. We understand that those barriers might come up while discussing credit and debt with families. We just want you to take into mind the barriers of the families that you serve and that you work with while we're having this discussion. If you have any questions on how to approach credit and debt while addressing barriers, please put those in the chat as we continue throughout this training.

A little bit of housekeeping. We want to be able to maximize your experience here today. I'm going to talk through a couple of the tools you have available to you. First is, if you look at the bottom of your screen, there are several ways to engage with us. We know in this virtual setting the engagement is a little difficult, so we want to make sure that this session feels interactive and that you're able to interact with us as much as possible. The Media Player – you can use this tool to watch the presenters and any videos during this session.

If you have a question for a presenter, you can use the tools in the Question or Comment section to ask us any questions that you may have or add in a comment, because we all know some of the people in this room are experts themselves and want to make sure that your comments and your feedback are welcome as well. There's also the Slides. You can use this tool to display the PowerPoint and presentation slide on your own screen.

We also have Related Resources and Links. This tool includes a list of resources available for you to download in helpful links. You can find your slide deck and session handouts here on the Engagement Hub, as well. We also have the Presenter Bios. If you want to learn a little bit more about myself or Lucy, we're going to introduce ourselves in a second, but you can also check out our bios and learn a little bit more about us. Then there's also the Certificate of Attendance. You can use this tool to access your certificate at the end of the session. You must meet the criteria to earn your certificate. All these engagement tools are in your console and resizable and movable. If there is a tool that you want to make bigger or one that you want to make smaller, feel free to click on the icons at the bottom of the screen to make them reappear or disappear and move up as you see fit.

As I said, we're going to introduce ourselves now. My name is Sarah Spunt, and I am with the National Center on Parent, Family, and Community Engagement. I am the executive director for LIFT-Chicago. We are one of the subject-matter experts on family economic mobility and

working with the National Center. I am excited to be here with you. I know I have presented at a few other trainings throughout the institute and a few others earlier this year. You might recognize my face from one of those webinars or trainings. Now, I'm going to pass it over to my colleague, Lucy.

Lucy Smart: Thanks, Sarah. Hi, everyone. I'm Lucy Smart. I'm also here with the National Center on Parent, Family, and Community Engagement. I'm the program manager for Family Economic Mobility with LIFT, representing the National Center from that aspect as well as Sarah.

Sarah: Thanks, everyone. I see in the comments section that some of you are hearing my voice, but my face is frozen. I do apologize for that. I hope that the video unfreezes a little bit for that, but if not, hopefully my voice will carry through, and you will still be able to get the content. Thank you for that – and just understanding some of the bumps in the road as we do these virtual trainings.

On to the learning objectives for today. We have four learning objectives for today's session. One, to understand the importance of credit and how it is crucial to overall economic mobility. The other is to acquire an increased level of comfort in discussing credit and debt with families. The next one is to demonstrate how debt impacts individual credit score, and share tools that families can use to develop a plan to pay down their debt and thus, increase their credit score. Finally, review resources that help families know their consumer rights.

A little bit into understanding and managing credit. Understanding and managing credit are crucial to achieving economic mobility. At the same time, both topics can be a little intimidating and overwhelming to discuss with families – both for us, it might be intimidating, for us as family advocates, and overwhelming in case we don't feel the most confident in that. That's why we wanted to bring this session to you. It also can be overwhelming or intimidating for families because finances are a sensitive topic, and it might be a little intimidating, or parents might even feel, and families might even feel, a little bit of shame while talking about their overall debt. It's important to acknowledge all of those emotions while approaching the credit and debt conversation.

As family advocates and trusted partners, we play a crucial role in supporting families to understand the role that credit and debt plays in their financial life, and develop plans together to achieve credit- and debt-related goals. The "Building Foundations for Economic Mobility" toolkit includes key resources and helpful tips to support your work with families and to start your work with families in the credit and debt. Today, we are going to share some concrete steps for you to take to do just that. Before we dive in, let's take a moment to consider the context of this discussion.

I am still getting a little bit of feedback that my screen might be frozen. If anyone can put in the chat, if they are, if I need to refresh my screen before I move on, I just want to make sure that the video and audio are coming in clear. OK. I have refreshed. Is that better? Yes. Great. OK. Awesome. Hopefully, that has solved the problem. Thank you for bearing with us through these technological difficulties right now.

As I was saying, we want to set the context that we play as family advocates and workers in supporting parents with their credit- and debt-related goals and also the current context for today. First, we continue to be in the middle of an ongoing pandemic, and there will be long last effects, especially for the families that we work with. Many families may have accumulated debt during this time and over the past years. It could have affected their credit score, as well. By better understanding the topics of credit and debt, we can more effectively help families navigate financial situations that were either here before the pandemic or maybe have gotten a little bit more severe during the pandemic.

As always, each family's experience is different, and some families have been able to make progress towards paying down their debt and building credit thanks to funds from COVID relief packages and other sources. Other families may have not been able to access both benefits and resources or had accumulated more debt during this time. It's important we understand the different contexts that families are coming from.

Second, we cannot stop acknowledging the role systematic racism has played in the world of finances. Credit and debt are a part of this world. Historically, people of color were not able to access opportunities to build credit or to avoid debt. Some of those barriers still exist today. We will continue to discuss this as we go through this session, but please do not hesitate to share your thoughts in the chat when you notice a topic in which systematic racism is playing a role.

Finally, finances are complicated and intimidating. The purpose of today's session and previous ones is to help you feel more familiar and confident in some of the financial topics and to provide you with resources that can help you support families achieve their economic stability and mobility. Additionally, developing community partners – local organizations focused on financial coaching, counseling, and literacy building – to help you do this can be crucial. Later in this session, we'll provide some tools to get started in finding this support. And remember, all these resources mentioned in this session and previous ones are available in the session's handout.

I have done a little bit of talking now. Now, I want to hear from you. We have a poll. Before we dive into this credit discussion, we want to see where you stand. Please answer this poll question for us: "What are your hesitations around discussing credit with families? (A) I struggle with my own credit, so I'm not sure – I'm not sure I can be helpful. (B) Families are hesitant or uncomfortable discussing credit. Or both – Or (C) A and B together." I'll give you all a few seconds to answer this poll question.

Thank you all for your participation. Just going to give it a few more seconds before we close it out. I see a lot of variety of answers, but yes. Discussing credit can be overwhelming, and both answers, A and B, are OK. It's especially overwhelming to discuss credit when we feel overwhelmed with the topic ourselves, or we feel the family's hesitation to share, or a combination of both.

It's important to remember you are not expected to be an expert at credit. This session is designed to help you become familiar with the topic and prepare you for discussions with

families. I just want to reiterate that it's OK if you do not feel like an expert in this topic. We want to make sure that we give you the tools and resources to feel more confident in the topic and ways to find answers around the topic as well as you discuss with families.

Now, we are going to go on to another discussion. You can use the chat box to help answer these questions. First one, "What is credit?" The second one, "How does it differ from debt?" The first question, "What is credit?" or what do you think when you hear "What is credit?" Or you just hear "credit," what do you think of?" Also, "How does credit differ from debt?"

I see some of the answers coming in now. "Credit is a history of your debt." That is a great answer. Yes. Part of your credit, or I should say your credit report, and things will go into there includes the history of your debt. A great answer. "Credit involves qualifying for a loan." Yes. Credit is part of the loan process. That is true. Also, "Credit is how much you make versus how much you owe." That's a very insightful answer. Yes. That also plays a part of your credit score, and we will continue to go into that. Some other things coming in from the chat. "I don't know much about credit. I believe it is based on banks' trust in your ability to pay for the future." That is a fantastic answer. Yes. It goes into your ability to secure – part of knowing your credit is knowing how to secure a loan.

I'm going to go on to – now that we have some more things coming into the chat, we will address some of those questions too coming in, but I'm going to go on to the next slide, just giving an overview on debt and credit. When working with families, you think of credit as your ability to borrow money and repay it later. Debt is the money that you have to repay once you've used credit. Going based off of one of the answers we saw in the chat, but "I believe it is based on banks' trust in your ability to pay for the loan," and that is true. Credit is your ability to borrow money.

Understanding your credit typically has two components of it: one is your credit report, and two is your credit score. A credit report shows the detailed accounts of a person's credit history, the loans that they have received or the loans that they are currently paying, overdue bills that they have owed or late payments, and credit cards that you have opened. It shows, like I said, the history of anytime you have applied for a loan through a bank or a credit card, that is part of your credit score, and your ability to take out the money is part of the credit. Credit scores are a summary of the person's credit history, essentially a numerical measure of confidence for the person's ability to pay back the loan on time. If we go back to the answer that was in the chat of the bank's trust in your ability to pay for the future, using your credit report and the credit score is how the bank determines the trust around that.

As we look into how people have access to credit and credit scores, we also need to name that the unequal access to credit that people have. Credit is invisible. You have no credit history without any credit reporting companies. While we are talking about credit scores and how it can be an asset, it's important to look at the lack of equity around credit scores.

While the purpose of today's credit score system is to eliminate bias, there is still a lack of equity around credit scores and access to credit. Before credit scores were available, borrowers

were deemed credit worthy by lenders, using factors such as income, referrals, or even home visits. It wasn't until 1974 that the Equal Credit Opportunity Act was passed and no longer allowed credit score systems to use information such as sex, race, marital status, national origin, or religion to determine whether or not someone was credit worthy or not.

Now, FICO considers payment history, amount owned, length of credit history – when was the first time you first accessed credit is how we determine the length of credit history – new credit, and credit mix in its model. But that data may be influenced by generational wealth that many Black and Latinx borrowers do not have access to. According to a report by the Consumer Financial Protection Bureau, the CSPB, Black and Hispanic people are those living in low to middle – low income neighborhoods had higher credit invisibility rates. When we talked about being credit invisible and access – if you are credit invisible, you don't have access to credit. If there's higher rates of credit invisibility in Black and Hispanic communities of low-income neighborhoods, we need to address the unequal access to credit and take that into consideration while working with families.

Now, we are going to go into another discussion question. "Why might having a good credit history or a strong credit score be helpful?" I'm going to wait a few seconds as some things come into the chat box.

Yes. "Having a good credit history or credit score is foundation of economic mobility, like getting or keeping a job, better terms on a car or student loan, or housing decision." You also have, yes, some of the things like more access. The better your credit score, the more access to loans you have. A good credit history can make it easier for families to do a lot more, such as getting an apartment, insurance coverage, lower deposits on utilities or cell phone bills, and much, much more. We can also help families draw direct connections between their long-term family goals and the importance of credit. For example, if a family's long-term goal is to purchase a car or own a home one day, understanding that their credit score and their credit report helps them have access to better terms for their loan, or may qualify them for a reduced rate in terms of how long – what their interest is, and the duration of the loan as well.

A first step in supporting families with these types of goals is to help them get the full picture of the credit history. That starts with pulling a credit report. As a little recap, credit as an asset can be done – can be looked at in three ways. One, to get and keep a job. While credit does not appear in most background checks for employment, some industries do check credit scores. Studies have shown up to 30% of employees' background checks include credit history. As you're working with families on their employment goals, it might be worthwhile also checking their credit history, especially if they're entering an industry that holds credit scores as part of their background check. One industry that might do this are some financial institutions. If they're looking to get a job at a local bank or an insurance agency, you might want to talk to the family about their credit score to see if it's something that might be taken into consideration while looking for employment.

As we discussed in the chat, better terms on loans, on receiving lower interest, for example, and getting better terms on the loan is how credit is used as an asset and also securing housing.

Oftentimes during background checks for housing while renting, credit scores are taken into consideration. Like I said, as you're looking to – or a family is looking to purchase a home one day, credit will be taken into consideration as they are securing the loan.

Now, we're going to go into a little bit more about taking control of credit, and families can take control of their financial security by viewing their credit report. As we discussed, credit reports are a summary of a person's credit history. This information is used to calculate the credit score. To empower families to take control of their financial security, they need to understand what is the importance of – they need to understand what is in their reports and how they can correct the errors if they see any in their report.

You can help families start this by having them review their credit report. One way that you can review their credit report is by looking at different tools and resources that helps you access their credit reports. And I would – sorry, I'm just double checking to see if the slides are working. Please pause with us. I'm not seeing … There we go! I just want to make sure. I'm about ready to share some resources with you. You may be familiar with the Consumer Financial Protection Bureau's kit called "Your Money, Your Goals." This resource is a helpful tool to help you work with families on looking for their credit scores. It also has a wide range of topics around all financial goals. It has specifically a module on how to access credit reports. You or a family that you work with should never pay for a credit report. That is a – something that I want to repeat one more time. You should never pay for a credit report.

There are three credit reporting bureaus, and you have the legal right to one free credit report from each bureau per year. Supporting families in accessing their free credit report on annualcreditreport.com. A little tip I like to use is if a family is actively working on looking at their credit score or report, sometimes it's helpful to pull one free credit report from one of the financial bureaus and then four to five months later, pull it from another financial bureau. Then when they want to pull it for a third time, they can do that and creating a cycle so they can see how things are being taken off their report while still not having to pay for a report. Because like I said, you have access to a free report through annualcreditreport.com for free up to once a year, and you can pull it from each credit bureau at different times.

It's a good habit to check your credit report regularly to avoid issues related to identity theft or false reporting by lenders. For most families, checking their credit report once a year is a good idea, and I encourage it if you do it on a schedule of checking it if they are actively trying to make sure they are seeing the progress that they are disputing something on their credit report. Families who have a history or false claims on their credit report, or who are working to clean up their history and want to check their credit report more frequently, you can support them in developing a schedule to pull one report from different bureaus every four months.

A question that came into the chat is, "How do families ensure they are doing a soft credit check rather than a hard credit check?" That is a very good question, and I'm going to give a pretty high-level answer right now. Then we'll circle back with some more resources later on in the chat to make sure that there are – there's a tool and resources around that, as well.

Most of the time when you are applying for a loan through a lender, that is when you are going to be – people are going to be pulling your credit score for a hard credit check. That means, a hard credit check means that it will show that someone has accessed your credit report or your credit score. For example, if I was to go into a car dealership, and I wanted to finance the car ,and they pulled my credit report, that would get dinged as a hard pull. And you want to limit for the number of hard pulls that you have in a year. The good news is hard pulls don't drop your credit scores by that amount, but if done too consistently or too often, the couple of points that a hard pull does drop your score can add up over time. That's the importance of talking about that, as well. When you are looking to ensure that someone is pulling your credit, first, I would ask the lender if they are going to be doing a hard pull or a soft pull.

The second is if you are accessing your report online and it's not through annualcreditreport.com in one of your free reports that you get a year, I would follow the rule that the chances are they might be doing a hard pull. That is why we wanted to double down on making sure that you never pay for a credit report, or a family never pays for a credit report to ensure that they are getting soft pulls and not hard pulls.

The last thing I will add with that one is if any of the people listening are participating in this webinar or the families that you work with use online banking apps and have access to things like through Capital One, their CreditWise – I know each banking app has their own way to check your credit score – those are all soft pulls for checking your credit score. Anything that is done through those apps, those are often a soft credit score because they are collecting data that way. Those are also – can be inaccurate sometimes, too.

Sometimes they over-estimate credit score. Sometimes they underestimate credit scores. The best way to get the most accurate information is through the free credit report through annualcreditreport.com, where you can access that for free up to three times a year. But like I said, we'll follow up in the chat with a more detailed answer for the sake of time. I hope that was helpful.

Thank you for that, with the information. I'm glad that was helpful. I want to make sure that I cover everything we were supposed to on this slide. We talked about helping families get into a schedule of checking every four months if it is something that they're working on. Also, families who cannot get reports online, for example, if they don't have a Social Security Number, they can request one via mail. Once you access the credit report, "Your Money, Your Goals" has great tools for reviewing it and checking for errors. You can find links for both of these in the resource handout.

Now we're going to go into, what do you do if you spot an error on a credit report? "Your Money, Your Goals" definitely has great resources for that. You can support families in resolving their issues on their credit report. Correcting inaccuracies on a credit report will most likely boost someone's credit score. You want to use the tool, "Disputing Errors on Your Credit Report," in the "Your Money, Your Goals" toolkit and work together with the families to file the discrepancy.

This tool includes a step-by-step guide on what you should look for in a credit report, as well as "dispute templates" that you or the families that you use can report – that you can see on the report and report the errors, as well. This is a good way to check to make sure that credit cards have not been opened in your name – so if someone – it's a good way to screen and protect against identity theft is to look at credit reports and make sure that nothing has been – no line of credit, whether a credit report or a different loan, has been taken out in your name.

Why is all of this important in terms of credit scores? That is, for credit reports, it's in understanding your credit score. What's important about credit scores? This may be what most people think of when they think of their credit. A credit score is a three-digit number that is based on your credit history. Scores range from 300 to 850. Unlike credit reports, you can check your credit score at any time. Credit scores can be accessed through a number of states' platforms, including Credit Karma or Credit Sesame or through your bank or credit union.

A general rule, good scores 690 and up, and excellent scores, 720 and up, give you better chances to help you save money when it comes to loans. While companies, such as FICO or Your Vantage Score, measures credit scores a little differently, most companies take the same factors into consideration. The first one is your payment history. Your payment history tracks whether you are paying your bills on time or as agreed to. This is the biggest factor in your FICO score. Paying bills late, not paying bills at all, or having bills go into collections will cause your score to drop.

The older the information is, the less likely it is to impact your credit score. Amount owed includes whatever you are paying down on your loan in the balances as agreed. It also includes your credit utilization rate. Your credit utilization rate is how much of your available credit that you are using. By that means, if you have two credit cards that give you a limit of $5,000 total, so $2,500 dollars each, and you have $3,000 worth of on your credit cards, that is how your utilization rate is calculated. It is how much is on your credit card versus how much credit that you have. If you use more than 20 to 30% of your credit limit, your score may drop. The lower your credit utilization is, the better it is from the perspective of scoring.

The other thing to take into consideration when you're looking at your FICO score is the length of credit history. That is the next factor that impacts your score. Your score increases the longer you have credit history. New credit tracks your inquiries. This is what we were talking about when people are opening up new cards, like new credit cards or a new inquiry. If you have too many inquiries, the model interprets this to mean that you have a high demand for credit, which may be an indicator of risk and also may drop your score.

You want to make sure that when you are looking at loans or shopping for a loan, the model gives you a shorter window of time, generally 14 to 45 days, when multiple inquiries made for some type of credit without causing your score to drop. An example of that is, like I used earlier, if you are looking for financing for an auto loan, if people are looking at your credit score and pulling information within a certain amount of time, the algorithm will show that you're probably looking for a specific loan, and therefore, your score will not drop, or it will only drop a couple of points.

The last thing that is taken into your FICO score is the types of credit that is to be considered. Your FICO score increases if you have credit cards, revolving credit, or loan installment, such as a mortgage payment, or a car payment. Generally, it is considered positive to have a mortgage, an auto loan, and some credit cards, but not too many.

It's also important that if you do have a mortgage, an auto loan, and credit cards that you are paying all of your bills on time, especially with your credit cards – that it's not just paying the minimal amount but that you're paying the statement balance on time. Because if you are only paying the minimal amount – that you are – you could still be accumulating debt, which Lucy will go into, but it also will impact your utilization rate and on time payments.

I also see a few questions in the chat. If we haven't been able to answer those verbally, I will go back and answer them by writing them out to you. But do see specifically, "Do you need a Social Security Number to apply for credit?" It really depends on the type of credit and loan that you're applying for and the lender. But just a reminder, if a family that you are working with does not have a Social Security Number, they can apply for their credit report by mail. You can, even if you don't have a Social Security Number, you can still have a credit history. That means you can access some type of credit. But that's a very specific question that we can follow back up. Also looking at how undocumented families build credit, we can give you some resources on that.

A few things to look into consideration for undocumented families are some of the community partners in your area that focus on financial capabilities and financial literacy. If you have any community partners in your community that serve undocumented families, I would highly encourage you to reach out to them because they might have some programs in place specifically for undocumented families and how to build credit that way. Thank you for all the great questions.

A few more slides for me, and then I'm going to hand it over to Lucy. I'm going to go into building credit. Once you work with a family to develop an understanding of their credit history and score and the role it plays in long-term financial goals, how you can help families improve their credit score. We're going to watch this short video of three methods for building a good credit score. Let's play that video.

[Video begins]

[Music playing]

Speaker: This is Kendra. Kendra wants to buy a new car. She has some credit from previous accounts, but she doesn't have enough credit history to get a loan. Seeking a solution, Kendra turns to consumerfinance.gov and discovers she has options to help build her credit. Among her options, Kendra could apply for a secured credit card, a credit builder loan, or open a retail store card. While each option comes with different responsibilities and requirements, all three require Kendra to make on-time monthly payments as a way to steadily build her credit.

If Kendra chooses to apply for a secured credit card, she would pay the bank a security deposit, like you would when renting an apartment. The security deposit for a secured card typically ranges between $50 and $300. The bank would then give Kendra a credit card with a credit line matching the amount of her deposit. She has to leave that deposit in the bank while she has the secured credit card. If Kendra makes consistent, on-time payments on this credit card, her credit record will improve over time, and she could eventually graduate to a regular credit card and will be refunded her deposit. While various cards have slightly different terms, this is how most secured cards work.

Kendra could also choose to improve her credit through a credit builder loan. Kendra would take out a small loan from a bank or credit union, with the proceeds kept in a locked account, and make payments to it, typically $50 to $100 per month. At the end of the term, which is usually about 12 months, the financial institution would give Kendra her money back. Each on-time payment is reported to one or more of the credit reporting companies and would help Kendra build both credit and savings. Another option for Kendra to start to build her credit is to open a retail store credit card. Many gas stations, department stores, and other retail chains offer credit cards. These cards are usually easier to obtain and typically have a lower credit limit than other credit cards. Kendra would still need to pay her bill on time every month in order to build her credit score.

Kendra chooses to apply for a credit builder loan. After the 12 months, the bank pays Kendra back the $1,200 that she paid for the loan. With Kendra's new credit score and savings, she has the ability to buy the car she wanted and will save money when paying off the car loan.

Building credit takes time, but it's worth the effort. As Kendra continues to make on-time payments on her car loan and other bills, her credit continues to improve. It's important to consider all your options when trying to improve your credit score. A credit builder loan might have been the right choice for Kendra, but a secured credit card or a retail store card could be the right choice for you, depending on your situation. If you want to build your credit, like Kendra, or explore more information on improving and maintaining a good credit score, visit consumerfinance.gov/credit.

[Video ends]

Sarah: Now that we have talked about ways to build credit and looking at that video, I am going to pass it over to my colleague Lucy to dive a little bit into debt and how to help families tackle debt. Take it away, Lucy.

Lucy: Thanks, Sarah. Before we transition right over to debt, I just wanted to give one more reminder that there are resources to build off this video and all the information, especially in "Your Money, Your Goals." There's a great tool called "Getting and Keeping a Good Credit History," and that's linked in your resource list for you to check out after the session.

Like Sarah said, let's shift our focus over to debt. There are a lot of ways to define debt. We're going to walk through a few of them. Simplest terms, debt is just money that you owe another

person or a business. When you owe someone money, you have a liability, and you're expected to pay that money back. While borrowing money might give you access to something today, you may have monthly payments for months or years to come, and that obligation is going to factor into your monthly budget, like we talked about earlier today. Debt is the result of using credit. Like Sarah mentioned, credit is not a liability because you could have credit cards on which you don't owe any money because you paid off the balance, or you pay regularly. But when you use that credit, you create a liability or a debt.

Then finally, I want to name that having debt is not always considered a bad thing. Some debt might be necessary in pursuing your future goals, like student loans for education, a mortgage when you're purchasing a home, or even an open credit card to maintain a strong credit score.

I also want to pause before we go on to acknowledge the structural forces and racism that have led to inequity in most financial areas. People of color have historically not had equal access to credit building and this reality continues today. Further, communities of color are targeted by predatory financial providers and institutions that offer high interest rate loans and high-cost products, which can result in higher debt, worse credit history, and less financial opportunity. Just like Sarah said, let's keep that in mind as we keep going through this conversation and through discussions with family.

The big question, "How do we know when we are in too much debt?" One pretty easy and valid way to do this or to determine this is based on identifying how much stress your debt is causing you. If you're worried about your debt, you may have too much. A more objective way to measure debt is the debt-income-ratio. This compares the amount of money you pay out each month for debt payments to your income before taxes and other deductions. Let's watch a short video to break that down.

[Video begins]

Speaker: If you're looking into buying a house, consumerfinance.gov can help you navigate the home-buying process and understand any new financial terms you encounter along the way, like debt-to-income ratio, or DTI.

Why does a debt-to-income ratio matter? Your DTI is all of your monthly debt obligations divided by your gross monthly income, which is the amount of money you earn before taxes and before any deductions are taken out. This percentage is one way lenders measure your ability to manage payments you make on money you've borrowed. It may affect how much a lender will loan to you, the interest it will charge, and what you feel comfortable spending on monthly mortgage payments as part of an overall budget.

Different loan products have different DTI limits and lending criteria, and the same is true for different lenders, so it's important to look at all of your mortgage options and talk to multiple lenders to choose the loan that's right for you. ConsumerFinance.gov is your go-to resource for clear answers to hundreds of financial questions. To learn more about buying a house and choosing a mortgage, check out consumerfinance.gov/buyingahouse.

[Video ends]

Lucy: All right. After working with a family to determine their debt-to-income ratio, whether it's in preparation for buying a house or another financial goal, how can they reduce their debt, if necessary? You can support families by providing information on common strategies for managing debt. There are two primary methods for reducing debt that we'll go over: the high-interest rate method or "avalanche," and the "start off small" or "snowball" method. As a family support worker, you can provide information on both techniques to families, and each family will need to determine which strategy works best for them. Let's go into a little detail on both methods.

First, we have the high-interest rate or "avalanche" method. With this method, you focus on unsecured debt with the highest rate interest and eliminate it as quickly as possible. People usually do this by adding an extra payment on top of their monthly payments. Once that high-interest debt is paid off, you can start to contribute that extra monthly payment to the next most expensive debt.

For you guys in the audience, what might be some pros of this method or some cons that you can think of? Absolutely. I'm seeing some great answers in the chat. And yes, a big pro is that you're getting rid of that most costly debt first. In the long run, that's going to save you money. You're paying off the debt with the highest interest rate and saving yourself some money. Yes, I'm seeing in the chat as well, a con is that you might not feel like you're making progress very quickly, especially if that high-interest debt is large. That's where we come into the second method.

With the "start off small" or "snowball" method, you focus on the smallest debt first and get rid of it as soon as possible. Similar to the first method, you would do this by adding an extra payment on top of your monthly payment, and once it's paid off, contribute that extra monthly payment to the next smallest debt. Again, I'll ask, what are some of the pros you can imagine with this debt payoff method and some of the cons as well?

Absolutely. Thanks for those answers. On the positive side, you might start to see progress quickly, especially if you have a lot of small debts, and you're paying them off, starting with the smallest first. For a lot of people, this creates momentum and motivation that another method might not bring. But yes, on a more negative side, you might pay more in total because you're not necessarily eliminating your most costly debt first.

You can see from both of these methods, there are pros and cons to both, and it really will depend on a family's preference and how they want to get started paying off their debt. The Debt Action Plan Tool from "Your Money, Your Goals" lays out both of these methods in detail and can help you help families get started taking steps towards reducing their debts.

All right. As we've mentioned, both credit and managing debt can be complicated. You can support families in understanding confusing situations and also in finding professional help

when it's necessary. We're going to go over a few of these confusing situations and show you some tools that you can lean on when they do come up.

First would be avoiding debt traps. A debt trap is a situation in which people get a loan and have to repeatedly take new loans to make a payment on the first one. These include things like payday lending and pawn shops. It can become difficult to escape this cycle of borrowing and still be able to pay for critical needs.

Then we have debt collectors. When companies decide they no longer want to try to collect overdue debts, they may assign or sell these debts to third-party debt collectors. There are laws about how debt collectors can act, what they can say, and how they can treat you. "Your Money, Your Goals" has a tool that you can use with families when debt collectors call to help with these situations.

Finally, debt settlement programs. There are companies that offer debt settlement plans that say they can renegotiate, settle, or change the terms of your debt, and these programs charge fees for their services. This method of debt management typically leads to high fees and damaged credit and should be avoided. Safe and trusted information can be found at the Federal Trade Commission website, which is linked in the resource list. Also, when necessary, you can help a family find a professional credit counselor via the consumerfinance.gov website.

All right, I've said it before and I'm going to keep saying it, but credit and debt are complicated. We want you to remember that there are resources available to support your work with families. It's important to note that some of these situations are best addressed by professional credit and debt counselors as well. The Consumer Financial Protection Bureau offers helpful information to support families in deciding if a credit or debt counselors is right for them and how to carefully choose one. Programs can then partner with or refer families to local nonprofits that provide counseling services and financial coaching in your area. Staff and families can identify free local credit counseling opportunities via the websites of the Financial Counseling Association of America and the National Foundation for Credit Counseling, which are both linked in the resource list in your hub.

Then additionally, programs can consider bringing on financial coaches to support families using both CARES and Recovery Act funds. I also want to give one more reminder about the "Your Money, Your Goals" toolkit that's available for free online for you to use with families or share with families for them to use on their own. Everything is available as a fillable PDF as well as for printing. This is a great tool to dig into with families when you're working on these topics. Of course, the "Economic Mobility Toolkit for Head Start and Early Head Start" focuses on exactly these topics in Key Topic Three: Building Credit and Managing Debt, which is another great resource for connecting these topics to your work with families.

OK. We've covered a lot of information today. I want to make sure we pull out a few of the key takeaways. First, managing credit and debt are crucial to achieving economic mobility. As trusted family partners, we can help families understand these topics and create action plans to manage them.

Credit is key to many long-term goals, but credit is also tied to a history of systemic racism in financial practices. Acknowledging this in our work with families is important and something that we should continue to do as we dive into the work, one on one with families. Finally, again, credit and debt are complicated topics. Remember, there are resources to support your work with families, and there are places to turn to when a family member needs help from a financial professional. Again, as Sarah said, you aren't expected to be a credit or a debt expert, but having some of this baseline information can help you point families in the right direction for where they need to go.

All right, and I know we're starting to wrap up our presentation. I wanted to address a few questions in the chat down here. We had one question asking, "Are there any legal routes a family can take if they feel they have been taken advantage of financially?" It's a great question. Absolutely. I think that's one of the great opportunities where it would be good to connect a family with a credit or a debt professional. Find them a credit or debt counselor, typically these are nonprofit organizations that can support the family in identifying how to resolve the situation.

Some examples I can think of would be if something has been put incorrectly on their credit report, if an identity has been stolen, or if there are other predatory financial practices taking advantage of them. These are all situations in which a professional and safe credit or debt counselor can assist. Again, those resources can be located at the two websites we mentioned previously and that are linked in your resource list.

All right. Just like before, to complete this session and download your certificate of attendance, make sure to follow these steps. Go to the engagement tools at the bottom of your console and click on the blue Certificate of Attendance icon. A pop-up message is going to appear on your screen, and if you've met the full credit criteria, a certificate icon will appear in the tool window where you can download your certificate. Click that icon, and you can open the certificate as a PDF in a new browser. Save it to your computer or print it out. Also, if you attended this session with several of your colleagues and all of you met the full-credit criteria, the group leader can add other viewers by opening the Group Viewer form.

Finally, don't forget to download the resources in the Resource and Helpful Links section. I know we went over a lot of them today. All of that's available in your console. Then the resources are also available on the Engagement Hub. Finally, your feedback is important to us. At the end of the institute, at the end of today, we have an event survey link posted to the Engagement Hub. Please remember to complete that at the end of today's sessions.

Of course, we know how eager everyone is to resume full in-person services for children and families. We're excited to share that the Biden Administration has prioritized teachers, early educators, and child care staff to receive the COVID-19 vaccination. You can learn more about the vaccine in the Engagement Hub. We have some information available to help you become confident in making the right decision for yourself. Now, join us in the Engagement Hub for a self-care break and get ready for your next session. Thanks for joining us.

Sarah: Thank you, everyone.