

CANADIANS, CREDIT CARDS, AND DEBT

Introduction

Focus

In a troubled economy, Canadians are facing a credit crunch, where less money is available to borrow at a time when many of us are already in considerable debt. In this *News in Review* story we examine Canadian personal debt—what we owe, why we owe so much, and the ways in which we can get out of debt. We pay special attention to credit cards. We admire their usefulness but point out the many ways they can make us owe more than we can really afford.

This is a story about something important to all of us: money.

In some ways it is more about the idea of money than about money itself. Few people really handle cash much anymore. Most daily transactions involving money are now made with debit cards and credit cards. And in the case of credit cards, many of those transactions are made without money on hand to back them up.

There was a time when people saved up for major purchases. For example, this writer can remember his parents setting aside an amount from their weekly paycheques for several months in order to purchase the family's first television. He can also remember an instrument called the Christmas Club. One could establish a special bank account with that name and set aside an amount of money every week that would be returned in early December, with interest, to be used for Christmas gifts and expenses.

Credit

These practices, common less than a half-century ago, seem very quaint today. Today, VISA and MasterCard reign supreme. We see it, we want it, and we buy it. "No money, no problem."

For those who use credit wisely, there really is no problem—only real convenience. It's a pleasure not to have to carry much cash, to be able to pay for one's purchases with one monthly cheque (or, better still, electronic transfer), and to benefit from the rewards provided by many cards (air miles or cash bonuses).

Debt, Good and Bad

The dark side of credit, however, is debt. For most people, some debt is unavoidable, such as a home mortgage or a car loan. Many of you will, at some

point, take out a student loan to further your education. We borrow money and pay interest on these items because it would, quite frankly, take much too long to save up to pay for them outright. Fortunately, we can usually negotiate with our financial system's lenders for reasonable rates of interest and carry these debts with minimal difficulty.

A problem with debt arises when we decide we have to have more than we can afford. An entire industry—advertising—is dedicated to making us want all kinds of things. It has succeeded admirably, and we have become a nation of spenders. Most of what we buy we buy on credit. A lot of what we buy on credit is also bought on impulse. And much advertising is directed at young people.

There are currently twice as many VISA and MasterCard cards in circulation in Canada—64 million—as there are Canadians. About another 10 million specialty cards—department store, Canadian Tire, gas cards—are also in use. Some major Canadian banks now make more money from credit cards than they do from other kinds of loans.

Credit card companies and the banks that provide them charge fees to retailers who accept the cards; but the bulk of their money comes from loans at extremely high rates of interest. As those who overuse their cards discover very quickly, paying back a loan with an interest rate of 19.5 per cent is not a pleasant experience.

Canadians and Debt

A credit card can be a great asset if you pay off the balance every month. But it can be a real problem if you fail to do so, especially if your balance continues to rise. The banks are happy when this

happens; in fact, until recently, they would usually automatically increase your credit limit as your balance reached its maximum. They even reduced the minimum monthly payment required so that you could carry more interest-bearing debt from month to month.

Canadians obliged. There is now more than \$50-billion of credit card debt sitting and bearing interest. And, since over 60 per cent of Canadians pay off their cards every month, less than 40 per cent of VISA and MasterCard holders are responsible for that \$50-billion.

Some of these Canadians will be able to budget their way out of debt. Others will require outside help (and there is plenty of good help available) to work their way out of a crisis. Some will never succeed without declaring personal bankruptcy. The available options will be discussed later in this guide.

Staying completely out of debt may be impossible for most of us. Using credit wisely, however, is something that we all can and should learn to do. Young people in particular need to be wary of too much debt.

For Discussion

1. Whom should we blame when we get into serious debt difficulties?

Is it strictly our fault, or are there others to share the blame—advertisers, lenders, even governments?

2. How do you and your friends handle money? Do you ever get into debt? How much? For what reasons?

CANADIANS, CREDIT CARDS, AND DEBT

Video Review

Quote

“Youth is in danger until it learns to look upon debts as furies.”

— Edward George Bulwer-Lytton (www.quotationpark.com)

Part I

Answer the questions in the spaces provided.

1. According to Roger Sauvé, what is the total amount of Canadian consumer debt? _____
2. What is the average debt load per Canadian household? _____
3. By what percentage has average household income risen since 1990? _____
4. By what percentage has average household spending risen since 1990? _____
5. In 1990, savings were what percentage of disposable income? _____
In 2008? _____
6. By what percentage has household debt per household risen since 1990? _____
7. What percentage of Credit Canada’s (www.creditcanada.com) clients are under 30 years old? _____
8. According to Duff Conacher, what responsibility do governments have to ensure people use credit cards wisely? Do you agree or disagree? Why?

9. How many Canadian consumers declared personal bankruptcy in 2008? _____
10. According to Statistics Canada (www.statcan.gc.ca), how much debt does the average Canadian household have for every dollar of disposable income?

11. How much of your existing debt will a credit counsellor expect you to pay back if he or she puts you on a debt management program? _____
12. How long did it take Tina Boudreau and Neil Bigelow to pay off their debts under a debt management program? _____

Part II

During the video, participants make several suggestions for staying out of debt and for getting out of debt. During a second viewing of the video, make a list of those suggestions under the headings in the spaces provided. Compare your list with those made by your classmates. Are there any suggestions that you would add to either list? Circle those that you believe are most important

Staying out of Debt	Getting out of Debt

CANADIANS, CREDIT CARDS, AND DEBT

Credit and Canadians

Did you know . . .

The per-capita debt of Canadians has risen 5.2 times over the last 25 years, from \$5 470 in 1980 to \$28 390 in 2005. For Americans, it jumped 7.5 times, from CAD\$6 510 to \$48 700 (Statistics Canada, January 2007).

Further Research

For additional information on student loans and student debt, see the CBC Web site at www.cbc.ca/news/background/higher-education/studentdebt.html and www.cbc.ca/news/background/personalfinance/studentdebt2.html.

With \$1.3-trillion in outstanding Canadian consumer debt (including mortgages) it seems safe to say that Canadians are enthusiastic users of available credit. Whether or not they are wise users of credit is another question altogether.

In itself, debt is not an evil thing. Few Canadians would be able to afford a home if they were not carrying a mortgage. And major purchases like automobiles are usually financed by loans from banks or finance companies. The sheer financial size of these investments means that few people would have the cash on hand to pay for them in full at the time of purchase. So they borrow the money and agree to pay it back over a certain period, with a reasonable amount of interest. Home buyers and loan seekers also usually shop around to find the lowest rates of interest on their loans and mortgages.

And then there are credit cards. Even in times of fiscal uncertainty, banks and credit card companies make it very easy for individuals to get a major credit card. For many young people it is their first introduction to credit. Credit card companies sign up first-year students at university and college initiation weeks. Companies mail out thousands of invitations to recent graduates to register for cards.

As will be seen in the section of this guide titled “Credit Cards,” not all cards are alike. But they do share one very important characteristic: they make it extremely easy to spend money one doesn’t have and to get into debt. They can be very convenient. Credit cards can now be used to purchase almost anything—from groceries to televisions, prescription drugs to beer and liquor. Best of all, one doesn’t even have to

present the card to make a purchase. Just give a number and expiration date to a company with an online store, and that book or vacuum or camera is on its way to your home.

It’s no small wonder that Canadians have 74 million of these cards. It probably should also be no surprise that we have managed to pile up about \$50-billion in consumer debt charged to them. What is surprising is the number of people who carry a balance from month to month, unruffled by an interest rate in the range of 20 per cent.

Student Debt

Canadians who plan to attend college or university have a special debt challenge: the student loan. Over the past several years, government funding of post-secondary education has decreased relative to costs. More students have found it necessary to take out larger loans.

In 2004, Statistics Canada determined that 45 per cent of graduating students with bachelor’s degrees leave school owing money to student loan programs. The average amount was just under \$20 000.

Most students see this as a necessary and positive investment in their futures—and it probably is a textbook example of a “good” debt. But it does mean that their careers start with a large amount of money that has to be paid off. Other purchases and expenses, such as a new car or larger apartment, will have to be delayed.

The Lending Umpires

How individuals handle their various debts and sources of credit helps determine the relative ease with which they can obtain more credit in the future.

Further Research

For information on credit reports, including instructions on how to obtain one's own credit report, see the Financial Consumer Agency of Canada Web site at www.fcac-acfc.gc.ca/eng/publications/CreditReportScore/CreditReportScoreTOC-eng.asp. Other excellent information on credit reports is available from the CBC at www.cbc.ca/news/background/identity-theft/credit-rating.html, www.cbc.ca/consumers/market/tips/creditrating.html, and www.cbc.ca/consumers/market/files/money/creditscore.html.

As credit tightens up in the current economic slowdown, borrowing money will be more of a challenge for many Canadians. Who is allowed personal credit—and how much he or she is allowed—is largely in the hands of three Canadian companies: Equifax, TransUnion, and Northern Credit bureaus. These companies maintain files on the credit history of millions of Canadians.

These files contain information that can only be revealed to others if the subject of the report gives his or her permission. If you sign a loan or credit card application, you are almost certainly giving the financial institution permission to make an inquiry. Landlords, public utilities, and potential employers may also request permission to obtain a credit report.

Reports contain both personal (name, date of birth) and financial (loans, mortgages, bank accounts) information.

They include information on payment history, bounced cheques, and collection agency referrals. If the subject of the report has declared bankruptcy during the previous seven years, this will also appear in the report.

Credit-reporting agencies also assign a credit score to each individual. The score is the agency's evaluation of your financial health at the point in time when the request for a report is made. The better the score, the less risk there is to the institution considering lending money.

A good credit report is critical to anyone wishing to borrow money for any worthwhile purpose. An individual may obtain a free copy of his or her credit report by writing to each of the three agencies. Many financial authorities recommend that Canadians check their reports for accuracy at least once a year and immediately request any necessary changes or corrections.

To Consider

1. Offer an example of "good" debt and an example of "bad" debt.
2. What are some of the powers of credit-reporting agencies?

CANADIANS, CREDIT CARDS, AND DEBT

Credit Cards

Did you know...

The highest legal rate of interest in Canada is 60 per cent per annum.

As reported by the CBC (www.cbc.ca/news/interactives/map-credit-card-bill/), there are 64 million VISA and MasterCard cards currently in use in Canada—two cards for every Canadian. Millions of other cards from a variety of retail operations, such as gasoline companies and department stores, are also in use. In 2007, Canadians charged \$275-billion to VISA and MasterCard alone. The average purchase on these cards was \$111.09.

The Good

Credit cards—especially VISA and MasterCard—are very convenient. Over 650 000 locations in Canada alone accept them; indeed, it's almost shocking to be in an establishment where credit cards are not accepted.

Credit cards make carrying cash almost unnecessary. A shopping trip no longer requires a visit to a bank. Amazing bargains can be snapped up on the spot. Credit cards have also opened up the Web to serious commercial activity.

Many cards provide their users with significant bonuses. These range from a one or two per cent cash refund on purchases to travel rewards. Some provide perks like free purchase or travel insurance. For about 60 per cent of Canadians, credit cards cost them nothing in interest fees. They pay the full balance on the card every month.

The Bad

The cards can, however, have their drawbacks. For many Canadians they lead to impulse buying. They may not have the money in hand for that new big-screen TV, but they have their credit cards. At the end of month the money still isn't on hand, but the debt certainly

is—and it's accumulating interest.

They've joined the nearly 40 per cent of Canadian cardholders carrying about \$50-billion in debt on their cards.

Many of them are carrying that debt at high rates of interest. The majority of VISA and MasterCard products carry interest rates on overdue balances in the range of 18-19.5 per cent. Department store cards are even higher, usually 24-28 per cent. The average bank loan, on the other hand, would likely be no more than one-third that rate.

VISA and MasterCard will also advance cash to their cardholders. These advances are loans that begin charging interest the moment the cash is advanced—at the card's regular rate.

Needless to say, the banks sponsoring the various cards make a great deal of money from them. In fact, according to the CBC (www.cbc.ca/news/interactives/map-credit-card-bill/), the Canadian Imperial Bank of Commerce (CIBC) “now takes in more annual revenue from its credit card operations than from mortgages and personal lending.”

One way in which credit card companies encourage consumers to carry a monthly balance is by requiring that only small monthly payments be made—three per cent or less of the outstanding balance. In 2004, Tom McFeat (www.cbc.ca/news/background/personalfinance/creditcards.html) analyzed the real cost of carrying a significant balance on the average credit card. He wrote:

“Let's assume you owe \$10 000 on a credit card that carries an 18-per-cent interest rate. Let's also assume you want to take them up on their minimum monthly payment terms of three per cent of the outstanding balance (or \$10, whichever is greater). Enter the

variables and you'll see that simply paying the minimum will mean that it will take you 272 months to pay off the debt (that's almost 23 YEARS). You'll also pay almost \$9 800 in interest, almost as much as you charged. And this assumes you charge nothing more on that card during that 23-year period."

Most credit counsellors in Canada identify credit cards as the number-one cause of consumer debt difficulty.

Choosing a Credit Card

For most Canadians, the advantages of carrying a major credit card will outweigh the disadvantages. Knowledgeable Canadians will ignore the standard offers that flood the mails and make a choice of card after comparing the features available. Some cards have few bells and whistles but offer a low rate of interest (good for those who carry a monthly balance). Others carry a higher rate of interest

but provide air miles or dividend points (good for those who pay off their balance every month). Some cards charge an annual fee but offer even more bonuses to their users.

To help Canadians understand how credit cards work, the Financial Consumer Agency of Canada maintains a guide to credit cards at their Web site (www.fcac-acfc.gc.ca/eng/consumers/CreditLoanDebt/CreditChargeCards/CreditChargeCards-eng.asp).

The site also provides an interactive tool that consumers may use to choose the credit card that best suits their needs (www.fcac-acfc.gc.ca/eng/consumers/ITools/CreditCards/default.asp).

Students can especially benefit from consulting the table on student credit cards. This can be found by going to www.fcac-acfc.gc.ca/eng/publications/CreditCardsYou/CreditCardComparisonTables-eng.asp and clicking on "Student Credit Cards." The range of costs and options is extensive.

Activity: Choose a Card

1. As a student, what would you consider the most important features of a credit card: annual fees, interest rates, credit limits, payment requirements? Be prepared to defend your choices.
2. Using the comparison table at www.fcac-acfc.gc.ca/eng/publications/CreditCardsYou/CreditCardComparisonTables-eng.asp, choose the card you feel would best suit your needs. Be prepared to justify your choice to the class, and compare it with those of your classmates.

CANADIANS, CREDIT CARDS, AND DEBT

Getting Out of Debt

Quote

Dickens said it best: "Annual income twenty pounds, annual expenditure nineteen six, result happiness. Annual income twenty pounds, annual expenditure twenty pound ought and six, result misery" (*David Copperfield*). What do you think is the meaning of this quotation?

Owing money is one thing; being in serious debt is something altogether different.

Most Canadians live with ongoing debt: a mortgage on the family home, an automobile leased or purchased with regular payments, a bank loan for a major home improvement—and, in addition, regular monthly expenses for utilities, food, entertainment, and more. As long as the debt is manageable, and one's income can meet the payments and reduce the principal, all is well.

But when debt takes on a life of its own a real problem has developed. More and more money goes into interest payments. Amounts owing rise, rather than decrease. You live literally from pay cheque to pay cheque, and some months you barely make it.

Eventually, you don't make it. Payments are missed, and collection agencies start to call. You know how you got into this mess, but how do you get out of it?

The first thing you need to realize is that you are not alone. There are a variety of services—many of them free—to help Canadians manage and get out of debt. Relief can be as close as the nearest computer connected to the Internet.

Moneyproblems.ca

A valuable resource for anyone worried about personal debt in Canada is Moneyproblems.ca. It offers a free e-book titled *Solve Your Money Problems: A Canadian Guide*, which presents a series of suggestions to help you deal with debt. These range from budgeting, through debt counselling, to the ultimate step, declaring personal bankruptcy.

As Moneyproblems.ca points out, for many people, developing and sticking to

a budget is often enough to solve their problems, especially if this is combined with a debt-consolidation loan. A debt-consolidation loan combines debts from a variety of sources—several credit cards, for example—as one single debt, usually at a much lower rate of interest. As a result, the outstanding amount can be paid off at a much quicker rate. Banks are often pleased to provide these loans—especially if they are the provider of one of the credit cards you're having trouble paying off.

Credit Counselling

Not-for-profit credit counselling is readily available across Canada for those having difficulty meeting their bill payments. First contact with credit counselling services is often via the Web. Two of these counselling services—Toronto-based Credit Canada (www.creditcanada.com) and Credit Counselling Services of Atlantic Canada (www.solveyourdebts.com/en/index_en.php) were represented in the video presentation. Other provinces with similar societies include British Columbia (www.nomoredebts.org), Alberta (www.moneymentors.ca), Saskatchewan (www.justice.gov.sk.ca/provincialmediationboard), Prince Edward Island (www.familyservice.pe.ca/credit.htm), and Newfoundland and Labrador (www.creditanddebtsolutions.ca). Many individual communities also have their own credit counselling services.

Credit counselling services can do far more than offer advice. They can develop budgets, negotiate with creditors, arrange repayment plans, and set up a trust account to handle all monthly payments for the debtor.

Credit counsellors often develop a debt-management plan, making a deal

with the debtor's creditors to arrange the payback of all his or her debts over a set period of time. Often they will negotiate a reduced rate of interest (or the elimination of interest altogether) to help accelerate paying off the debt. The debtor gives a set amount of money to the credit counsellor each month; the counsellor, in turn, dispenses this to the various creditors. Credit counselling and debt-management plans have helped thousands of Canadians avoid personal bankruptcy.

Consumer Proposals

A last-ditch effort for avoiding personal bankruptcy is the consumer proposal. Only those who are legally insolvent (have more debts than assets) can file a

consumer proposal. The document is an offer to creditors to pay back a certain percentage of what the debtor owes. To work, it must be accepted by 50 per cent plus one of the creditors.

Unlike a debt-management plan, the consumer proposal is a legal document of some complexity, and the rules for filing are very detailed (interested students can read more at www.moneyproblems.ca/solve-your-money-problems.pdf, pages 21-31). Although not a bankruptcy declaration, the proposal must be prepared and filed by a trustee in bankruptcy acting as proposal administrator.

If none of the above steps work for a given debtor, then he or she will need to file for personal bankruptcy.

Inquiry

1. What sources of support are available to Canadians plagued by too much debt?
2. Do you know anyone carrying too much debt? What advice might you offer them?

CANADIANS, CREDIT CARDS, AND DEBT

Declaring Bankruptcy

Further Research

Bankruptcy Canada, one of the best sources of bankruptcy advice for Canadians, is available on the Web at www.bankruptcy-canada.ca.

Definition

The *Official Receiver* is an officer of the Insolvency Service and Bankruptcy Court who supervises bankruptcy procedures.

For most people, declaring bankruptcy is a devastating experience. Bankruptcy has an odour of failure to it. Popular opinion sees all bankrupts as failures. The term *bankrupt* is often used to describe someone or something deficient in some way (“The government has demonstrated that it is morally bankrupt.”).

Bankruptcy is, in fact, a legal determination that one is insolvent—that is, unable to pay his or her debts. You cannot declare bankruptcy unless you are insolvent, and this requires satisfying three criteria (www.cbc.ca/consumer/story/2008/09/05/f-bankruptcy.html):

1. You are not already bankrupt.
2. You owe at least \$1 000 and are unable to meet payments as they come due.
3. You would be unable to pay your debts even if you sold all your assets.

Filing for Bankruptcy

Should you choose to file for bankruptcy, the process will not be free. You will have to hire a trustee in bankruptcy. He or she will prepare the necessary documents. Among the documents filed by the trustee with the Official Receiver will be those giving the trustee the power to sell off all your assets in order to settle your debts.

Dealing with Debts

Once the forms are filed you are officially declared bankrupt. While bankrupt, you will no longer have to make payments to your creditors; the trustee is selling your assets to do just that. The only exception would arise should you suddenly come into money—win the lottery, receive a major tax refund, inherit from a wealthy relative,

or suddenly start to pull in higher income from your job or business.

But there are debts from which bankruptcy cannot protect you. These include:

- Alimony and child support payments
- Student loans if you are still in school or have been out of school for less than seven years
- Debts arising from fraud
- Court awards for damages
- Court fines

As Tom McFeat of the CBC points out (www.cbc.ca/news/background/personalfinance/credithelp.html), filing for bankruptcy brings some particular responsibilities. “During the time someone is an undischarged bankrupt (which is a minimum of nine months), they must abide by a long list of requirements governing their financial affairs. For one thing, they must inform anyone they do business with that they are bankrupt. They must also attend at least two counselling sessions. They must turn over all their credit cards to the bankruptcy trustee. They must disclose all of their assets. Failure to do any of those things is a crime.”

Bankruptcy Exemptions

Bankruptcy exemptions are personal assets that may not be seized for sale by the bankruptcy trustee. These include limited amounts of things like food, heating fuels, clothing, furniture, and the tools of one’s trade. In some circumstances it might include a car or a house. (For more information on bankruptcy exemptions, see www.bankruptcy-canada.ca/what-i-keep-or-lose-in-bankruptcy-in-canada/what-can-i-keep.htm.)

