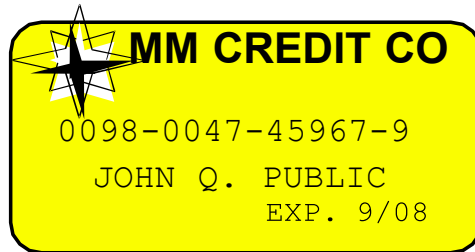


## ***UNDERSTANDING CREDIT AND CHARGE CARDS***

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Credit and charge cards are different from checking accounts. Checking accounts use only your money (i.e., you must have enough money in your account to cover any incoming checks), while credit and charge cards are a form of a loan from the credit company to you. While this type of loan seems to make shopping more convenient, keep in mind that it also bears certain risks (like overspending.) In addition, many credit institutions have a yearly membership fee. Some credit and charge card accounts also include an additional “service charge” or interest fee for certain kinds of transactions. It is important to understand how and when these additional fees are included.



In order to get a credit or charge card from a bank, service, or store, you must fill out an application form. Approval will be based upon a number of considerations, including your present income, length of employment, the balance and activity in your checking or savings account, and your credit history (Have you ever had credit/charge cards before? Did you pay your bills on time? Have you bounced checks?). Approval is not automatic. If you have just begun full-time employment or do not have a credit history, your application might not be approved. You can always re-apply, however, at a later date.

A credit card allows you to borrow only up to a certain amount, called your “credit limit.” When you purchase something with a credit card, the credit card company is actually paying for you. At the end of the month, the credit card sends you a statement telling you how much money you owe them. If you have a charge card from a particular store, similar loaning and billing procedures are followed.

This is an example of a credit card statement:

 <b>MM CREDIT CO</b> P.O. Box 008 Boston, MA 02116		<i>Return top portion with your check or money order.</i>	
Your Name Street Address City, State Zip		Amount Enclosed:	
Account Number 382-792-730-6	Exp. Date 9/08	Credit Line \$500	Available Credit \$377.67
Total Account Balance:	<b>\$122.33</b>	Total Minimum Payment:	<b>\$40.00</b>
<b>DETAILED TRANSACTION SUMMARY FOR PERIOD OF 5/01/95 to 5/31/95</b>			
<b>Date</b>	<b>Amount</b>	<b>Merchant ID#</b>	<b>Bank</b>
05/11/05	\$46.12	LA Boutique	458875344
05/21/05	\$76.21	Al Cleaners	842196002
<b>Monthly Percentage Rate 1.5%</b>			

The total balance is the amount of money you owe the credit card company for charging things during a specific period. The total minimum payment is the part of the total balance that **must** be paid by the payment date. The available credit lets you know how much more you can borrow before reaching your credit line. “Credit line” means the same thing as “credit limit,” and you can’t charge more than your limit. If you do, the credit card company may cancel your card. Transaction date, amount, and merchant ID# show when and where you used your card, and how much you charged.

You have two ways to pay off your credit card charges:

1. You can pay the total balance (\$122.33) all at once and be finished with it.
2. You can pay anywhere between the total minimum payment (\$40.00) and the total balance (\$122.33), and pay the rest over several months.

**Option 1** is good, but you may not have that much money available. You may only be able to pay a little bit at a time, which is your second option. When you use **Option 2**, however, the credit card company charges interest. They charge you for the privilege of putting off payment until later. In the end, you’re paying for your loan ( the things you charged) *and* the interest on the loan, which means that your total payment will exceed the amount of the original loan.

Which option should you use? **Option 1** means you end up paying back only the money you borrowed. **Option 2** means paying only a small amount of money at any given time but paying back extra money on interest.

Try to pay off your loans from the credit card company as soon as possible. If you wait, you can end up paying a lot of excess interest.



### ACTIVITY

Go to a department store and a bank to research additional information about credit and charge cards.

As stated in the beginning of this section, although there are advantages to credit and charge cards, they also bear risks.

**C**onsider the following:

Susan has been working full-time as a nurse's aide for the past twelve months. She is on a fairly tight budget and, after paying for rent, utilities, food, and transportation, Susan has approximately \$100 a month for miscellaneous expenses. A few months ago, Susan was approved for a credit card with a \$500 credit line. As soon as she got the card, Susan went shopping and charged \$200 for clothes. Two days later, Susan bought a new TV for \$280. When Susan got her statement in the mail three and a half weeks later, she was a little surprised. She had not anticipated that she had to pay for all these items and interest as well. Actually, it almost felt as if the items she charged were free, since charging did not have an influence on her cash flow.

How do you think Susan will pay the money back?

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How long do you think it will take her to pay off her credit card balance?

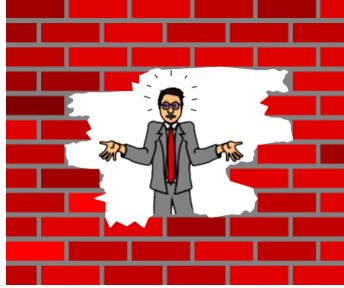
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Do you think Susan would have bought the items if she had not had a charge card?

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Many people get themselves into dangerous “credit holes,” meaning they buy much more than they can afford because it seems so simple to use the credit card now and pay later. Most of these people can never pay off the debt they owe, and the high interest rate on credit cards makes things worse. Some people spend years paying off debts that they have created through careless charging.

While credit and charge cards can be helpful in establishing a good credit history, necessary to apply for larger bank loans or to finance a car for example, they can negatively impact your ability to get credit if they are misused. You should be aware of the long range effects of bad credit.

**C**onsider the following:

Susan struggled for quite some time to pay off the charges for her purchases. She was late with her payments several times and actually missed one or two. Now, three years later, Susan (who has gotten a promotion and a raise at work) is shopping for a used car. After looking around she finds a car she likes and can afford, with reasonable monthly payments. She then applies at the car dealership for financing. The salesperson checks Susan’s credit history through one of the computerized credit rating companies and informs her that her loan has been disapproved.

What do you think has happened?

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After evaluating all the information, do you feel that credit and charge cards are a good option for you now or in the future? Explain your choice.

## Independent Living Skills – Understanding Credit



If you think that credit cards are a good option for you, remember to be very cautious when using them and never charge more than you can afford!