



Understanding Credit Cards



AFSA EDUCATION
FOUNDATION
Brightening Your Financial Horizon

INTRODUCTION

This brochure can help you understand how credit cards work, become familiar with common terms offered with a credit card, and avoid the dangers of using credit unwisely. A credit card allows you to pay for goods and services by borrowing against a line of credit provided by the issuer. Credit card rates and features vary, just like rates and terms for other types of loans.

DO I NEED A CREDIT CARD?

When deciding whether to apply for a credit card, consider the advantages and responsibilities. A credit card:

- 1. REQUIRES DISCIPLINE.** Responsible credit card use means not charging more than you can handle. Don't let the thrill of buying obligate you to more than you can afford.
- 2. MAKES IT POSSIBLE TO HANDLE UNEXPECTED EXPENSES.** The ability to make charges to a credit card can be helpful if an emergency arises that requires extra money.
- 3. OFFERS CONVENIENCE.** You can make purchases and obtain services now and pay for them later. You also don't have to carry around a lot of cash.
- 4. MAY OFFER REWARDS OR BENEFITS.** With some credit cards, you may earn cash, miles on airlines, or other rewards based on how many dollars you spend using the card. You may also be eligible for certain types of insurance or extended warranties.
- 5. ALLOWS MANAGEABLE PAYMENTS FOR MAJOR PURCHASES.** You can pay in small amounts each month rather than in one large sum of money. *Keep in mind, however, that you will pay interest each month on what you still owe.*



CAN I AFFORD THIS CREDIT CARD?

Before applying for a credit card, use the "Monthly Spending Plan" shown below to see if you have enough income to cover your living expenses. If a credit card company sends you a solicitation, you need to decide if it's in your best interest to accept it. The only time to take on a new monthly credit payment is when you're spending less each month than you take home. The additional debt should not cut into the amount you've committed to saving.

MONTHLY SPENDING PLAN

(1) Monthly Take Home Pay	\$ _____
(2) Saving	- \$ _____
<u>MONTHLY EXPENSES:</u>	
Mortgage/Rent	- \$ _____
Utilities	- \$ _____
Groceries/Lunches/Dinners Out	- \$ _____
Transportation	- \$ _____
Insurance (Home, Renters', Car, Life)	- \$ _____
Clothing	- \$ _____
Personal	- \$ _____
Entertainment	- \$ _____
Gifts/Contributions	- \$ _____
Family	- \$ _____
Education	- \$ _____
Car Payment(s)	- \$ _____
Loan Payment(s)	- \$ _____
Current Credit Card Payment(s)	- \$ _____
Other	- \$ _____
REMAINING MONEY	= \$ _____

WHAT TYPE OF CREDIT CARD IS RIGHT FOR ME?

■ **FOR THE CREDIT CARD USER WHO CARRIES A BALANCE FROM MONTH TO MONTH**, getting a low Annual Percentage Rate (APR) is usually the most important factor. Another important consideration is how the finance charge is calculated. (Please see the “How Will My Credit Card Issuer Calculate the Finance Charge” section on page 4.)

■ **FOR THE CREDIT CARD USER WHO PAYS OFF THE BALANCE IN FULL EACH MONTH**, the APR isn't the most important feature. For this user, attention needs to be given to the allotted grace period — the period between the time the purchase is made and the time the finance charge is added to the balance. It's also important to note any other fees charged by the issuer, such as annual fee, transaction fees, late charges, or over-limit charges. For many non-revolvers, the line of credit is also a factor, especially if the card is used for business or vacation travel.

■ **FOR THE CREDIT CARD USER WHO WANTS TO EARN REBATES, AIRLINE MILES OR OTHER REWARDS FROM A FREQUENT USER PROGRAM**. Pay attention to the annual fee and APR as they can be higher than those for a traditional card. Read the “restrictions” fine print on using your rebate or reward. Most of these cards are affinity credit cards that are made available to members of a particular union, professional group, interest group or university.

WHAT HAPPENS WHEN I APPLY FOR A CREDIT CARD?

You will need to complete a credit application that may include: your name, social security number; date of birth; current and previous addresses and length of stay; current and previous employers and length of employment; occupation; sources of income; total gross monthly income; and financial information on existing credit accounts.

Information about you and your credit experiences, such as your bill-paying history, the number and type of accounts you have, late payments, collection actions, outstanding debt, and the age of your accounts, is collected from your credit report. Your credit history helps predict how creditworthy you are — how likely it is that you will repay and make the payments when due.

A credit score is a number that sums up what your past and current credit usage predicts about your future credit performance. Credit scoring helps card issuers apply one set of rules to everybody and create a production model to compute the likelihood of repayment, the appropriate interest rate to charge, etc. One reason these scoring models are so widely used is because they can differentiate between the credit patterns of individuals. Different credit card issuers may value some characteristics, such as length of time spent at a job, to be more important than other issuers.

The best rates are offered to consumers with good credit histories (similar to auto insurance, where better rates are offered to those with good driving records). It is important to maintain the best credit report possible. Each person should check his or her credit report at least once a year and make sure it is accurate. Always get your credit report in order before shopping for a loan.

TEN TIPS FOR MANAGING YOUR CREDIT CARDS

1. Do not charge more than you can afford to repay.
2. Pay your bill on time to avoid fees and a possible increase in your cards' interest rates.
3. Be aware that paying only the minimum each month may mean it takes you a long time to pay off your balance.
4. Maintain the best credit record possible so you will be offered the best rates.
5. Decide in advance how you will use the credit card — whether it's for emergencies only or for routine purchases.
6. Understand the terms, conditions and costs for a credit card before you select one for your use.
7. Know where your credit card is at all times; don't leave it lying around.
8. Make a central record of your credit cards. For each card, include the account number, name on the card, the expiration date and the phone number to call if it is lost or stolen. Keep this record in a safe place, other than your wallet.
9. Keep track of your credit card purchase receipts so you can check them against your monthly statement.
10. Destroy receipts and statements once you no longer need them.

WHAT CREDIT CARD TERMS SHOULD I KNOW BEFORE I SIGN?

Take the time to review your credit card application and understand all of the terms, conditions and costs involved with the use of a credit card. Call the card issuer and ask questions about any items you don't understand.

[ANNUAL FEE] A membership fee for use of the card that's paid once a year. Some credit cards have no annual fees. Many people with good credit histories will be offered a credit card with no annual fee. However, "reward cards" may have annual fees, regardless of an individual's credit history.

[ANNUAL PERCENTAGE RATE (APR)] A measure of the cost of credit expressed as a yearly rate. Your APR might change, depending on your payment history or other factors. Always check your rate on your monthly bill.

[ARBITRATION] A process to resolve disputes. One or more arbitrators hear evidence from the involved parties and then issue an "award" that decides who gets what. Some credit card companies require arbitration if there is a dispute between the card holder and the card issuer.

[BALANCE] The outstanding dollar amount owed on the card.

[CASH ADVANCE] Cash borrowed against a line of credit provided by a credit card company for the amount of cash obtained. Cash advances have a higher interest rate than regular charges on a credit card and carry no grace period.

[FINANCE CHARGE] The total dollar amount you pay to use credit. If you pay the total amount you owe before it is due, you won't have to pay a finance charge.

[GRACE PERIOD] A free period between the time a charge is made and the time the finance charge is added to the balance. For credit cards, the typical grace period is 20-25 days.

[LINE OF CREDIT] The total amount of credit available to you on the credit card.

[TRANSACTION FEES AND OTHER CHARGES] You may be charged a fee if you use your credit card for a cash advance, pay late, or exceed your credit limit. Some of these fees can be significant, so it is important to read the fine print in your credit card agreement.

HOW CAN I SHOP FOR A CREDIT CARD TO SUIT MY PURPOSES?

Use the worksheet below to review and compare the financing terms offered by more than one credit card issuer

	Credit Card #1	Credit Card #2
Annual Fee	\$ _____	\$ _____
Annual Percentage Rate (APR)	% _____	% _____
Arbitration Clause (Yes No)	_____	_____
Finance Charge		
Average Daily Balance (Y/N)	_____ %	_____ %
Previous Balance Method (Y/N)	_____ %	_____ %
Adjusted Balance Method (Y/N)	_____ %	_____ %
Two-cycle Balances (Y/N)	_____ %	_____ %
Grace Period	_____ days	_____ days
Transaction Fees		
Cash Advance	\$ _____	\$ _____
Late Payment	\$ _____	\$ _____
Overlimit	\$ _____	\$ _____

HOW WILL MY CREDIT CARD ISSUER CALCULATE THE FINANCE CHARGE?

Issuers generally use one of the following methods:

- **AVERAGE DAILY BALANCE - *The most common method.*** Calculated by averaging the amount of debt you had in your account each day covered by the billing statement.
- **PREVIOUS BALANCE METHOD** - Calculated on the outstanding balance at the end of the previous billing period.
- **ADJUSTED BALANCE METHOD** - Calculated by subtracting the payment(s) made by you from the outstanding balance at the end of the previous billing period.
- **TWO-CYCLE BALANCE** - Calculated by making use of your last two months' account activity.

HOW CAN I PROTECT MYSELF AGAINST CREDIT CARD FRAUD?

Credit card information can be used fraudulently by others to charge purchases to a person's account, particularly those made by phone, mail or on the Internet. The following safeguards will help protect your credit cards from unauthorized use.

- Sign your credit card in ink as soon as you receive it and keep it in a safe place. Destroy expired cards.
- Notify your card issuer if you have applied for a card and haven't received it in a reasonable amount of time, such as 30 days.
- Be sure that your card is returned after you use it. Don't leave a cash register until you have returned your card to its proper place.
- When paying by credit card in a restaurant, check the amounts and total for accuracy before signing the bill.
- Keep receipts so you can check the charges on your monthly statement. If you don't need the receipts for your records, shred them, especially if your credit card number is on them.
- If you receive a credit card application in the mail, and you don't intend to apply for the card, destroy the application.
- Avoid writing your credit card number on return cards or mailers that can be pulled open easily.
- Do not give your credit card number to a telephone solicitor unless you placed the call and you know the company is legitimate.
- If you get an unsolicited e-mail from a bank or card company requesting account or other personal information, don't give out the information. Call the company first (using the phone number on your statement).
- Keep a record of all your credit cards, including the account number, name used on the card, the expiration date, and the phone number to call if a card is lost or stolen. Keep this information in a safe place — not in your wallet.
- Notify the card issuer immediately if a credit card is lost or stolen. Once you notify the issuer, you are not responsible for unauthorized charges on the card. Under federal law, you may be responsible for up to \$50 of unauthorized charges made before you report the loss or theft. However, most major payment systems have a zero dollar fraud liability.

WHAT IF I AM A VICTIM OF IDENTITY THEFT?

When someone uses your name, your Social Security number, your credit card number, or some other piece of your personal information for his or her own purposes — it's identity theft. You may not know your identity has been stolen until you notice that something's wrong: you may get bills for a credit card account you never opened, your credit report may include debts you never had, a billing cycle may pass without your receiving a statement, or you may see charges on your bills that you didn't authorize, or don't recognize.

IF SOMEONE HAS STOLEN YOUR IDENTITY, THE FEDERAL TRADE COMMISSION RECOMMENDS THAT YOU TAKE THREE ACTIONS IMMEDIATELY:

1. Contact the fraud departments of any one of the **THREE MAJOR CREDIT BUREAUS** to place a fraud alert on your credit file. The fraud alert requests creditors to contact you before opening any new accounts or making any changes to your existing accounts. As soon as the credit bureau confirms your fraud alert, the other two credit bureaus will be automatically notified to place fraud alerts. Once the alert is placed, you may order a free copy of your credit report from all three major credit bureaus.
2. Close the accounts that you know or believe have been tampered with or opened fraudulently.
3. **FILE A POLICE REPORT.** Get a copy of the report to submit to your creditors and others who may require proof of the crime.
4. **FILE YOUR COMPLAINT WITH THE FTC.** The FTC maintains a database of identity theft cases used by law enforcement agencies for investigations. Filing a complaint also helps the FTC learn more about identity theft and the problems victims are having so that they can better assist you.

WHAT IF I HAVE TROUBLE PAYING MY CREDIT CARD BILLS?

Creditors realize that circumstances such as unemployment or illness can make it very difficult to meet bill payments. If this happens to you, contact your creditor, explain your situation and work out a repayment schedule.

If your situation requires outside help, contact a nonprofit budget and credit counseling agency, often called a consumer credit counseling service. These agencies can work directly with consumers and their creditors to help resolve debt problems.

WHAT FEDERAL LAWS SHOULD I KNOW?

[TRUTH IN LENDING ACT] Requires creditors to give you written disclosures of important terms of the credit agreement such as APR, finance charges, monthly payment amounts, payment due dates, total amount being financed, length of the credit agreement and the consequences of not making a monthly payment.

[FAIR CREDIT BILLING ACT] Specifies the obligations of a credit card issuer upon receiving notice of a potential unauthorized use, and limits the liability of the consumer when the proper reporting steps are taken.

[FEDERAL TRADE COMMISSION'S CREDIT PRACTICES RULE]

- Requires creditors to provide a written notice to potential co-signers about their liability if the other person fails to pay;
- Prohibits late charges in some situations; and
- Prohibits creditors from using certain contract provisions that the government finds to be unfair to consumers.

WHAT IF I DON'T WANT TO RECEIVE CREDIT CARD OFFERS IN THE MAIL?



Credit card companies often send “prescreened” or “preapproved” offers of credit to consumers. These offers are based upon information in the consumer’s credit reports. You can choose to stop receiving these offers by calling toll-free 1-888-567-8688.

[EQUAL CREDIT OPPORTUNITY ACT] Prohibits the denial of credit because of gender, race, marital status, religion, national origin, age, or receiving public assistance.

[FAIR CREDIT REPORTING ACT] Gives you the right to learn what information is being distributed about you by credit bureaus. As of September 2005, the three major credit bureaus—Equifax, Experian and TransUnion— must provide all consumers, upon request, a free copy of their credit report once every twelve months. You can order your free annual credit report online at www.annualcreditreport.com, by calling 877-322-8228, or by completing the Annual Credit Report Request Form and mailing to: Annual Credit Report Request Service, P.O. Box 105281, Atlanta, GA 30348-5281.

[FAIR DEBT COLLECTION PRACTICES ACT] Prohibits third party debt collectors from using unfair or deceptive practices to collect overdue bills that your creditor has forwarded for collection.

IMPORTANT CONTACTS:

Federal Trade Commission

Washington, D.C. 20580
Phone: (877) FTC-HELP (382-4357)
Web site: www.ftc.gov

Federal Reserve System

Washington, D.C. 20551
Phone: (202) 452-3693
Web site: www.federalreserve.gov

National Association of State Attorneys General

Washington, D.C. 20002
Phone: (202) 326-6000
Web site: www.naag.org

CREDIT BUREAUS

Equifax Credit Information Services, Inc

Atlanta, GA 30374
Phone: (800) 685-1111
Web site: www.equifax.com

Experian

Costa Mesa, CA 92626
Phone: (888) 397 3742
Web site: www.experian.com

TransUnion

Chester, PA 19022
Phone: (800) 916-8800
Web site: www.transunion.com



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AMERICAN FINANCIAL SERVICES ASSOCIATION EDUCATION FOUNDATION

919 Eighteenth Street, NW • Suite 300 • Washington, DC 20006-5517
Tel: (202) 466-8611 • Fax: (202) 223-0321 • Web site: www.afsaef.org