



Spending Tomorrow's Money Today

In today's society, more and more people are using credit on a daily basis. Many of them do not appreciate the effect it may have on their financial future. The average family today has six credit cards. For those families who do not pay off their balance in full every month, the average amount of debt they carry on their credit cards totals \$8500. At one time, if you wanted a new television, you would have to settle for your outdated model until you could afford to buy a new one. Today, with the ease of both obtaining and using credit, most people would go to the appliance store and buy the television on credit using either a credit card or an installment loan.

Credit can be part of a sound financial management plan if used responsibly.

There are good reasons for using credit, such as financing a home, home improvements, and education. Credit can also be useful in the case of financial emergencies if you have not built up a sufficient emergency cash reserve. There are also situations when you should avoid using credit; for example, buying luxuries that you cannot afford or buying products that will not outlast the credit payments.

Debit cards offer some of the same advantages as using credit without some of the disadvantages. Like credit cards, debit cards are safer and more convenient than cash. However, unlike making purchases with credit cards, there are no interest charges when using

debit cards and fewer fees. In addition, using a debit card reduces your ability to overspend since you cannot spend more money than you have available in your checking account.

There are, however, a few important things to keep in mind when using debit cards. One, you don't have the flexibility to pay for items over time because the money you withdraw comes out of your checking account immediately. Two, you don't have the same right to withhold payment for defective

merchandise as you do with credit cards. Three, debit cards are not protected under the same law that applies to lost or stolen credit cards, so your potential for financial loss is much greater with debit cards. Finally, debit cards may make it easier to overdraw your checking account if you are not careful to record all transactions in your checking account register. Penalties and fees for overdrawing your account can really add up.

Here are some tips for using credit to your advantage:

- ◆ Limit the number of credit cards you have. This will limit your potential for debt and allow you to keep track of how much you owe and to whom.
- ◆ Plan ahead when using credit. Determine what expenses you already have by developing a spending plan. Make sure that your income will be able to cover all your basic living expenses in addition to your debt payments.
- ◆ Always pay your bills when due. Pay more than the minimum amount due so that you can reduce finance charges.
- ◆ Make sure credit payments do not outlive the items purchased.
- ◆ Use credit infrequently. Instead, pay with cash, checks and debit cards.

Understanding the Contract

When you sign or co-sign an application for credit you are agreeing to all of its terms. If you are approved, the application becomes a contract and you are *legally* bound to the terms. It is important to understand the terms used in a contract before you sign on the dotted line.

By law, a creditor must disclose all the terms of the agreement in writing on the application. This is called the Truth in Lending Disclosure. The type of credit applied for will determine the terms that must be disclosed. Two types of credit are available to consumers: closed-end and open-end. Closed-end credit includes installment loans and mortgages. Credit cards and home equity lines of credit are examples of open-end credit.

Closed-end credit is a loan which requires the same payment each month for a specified amount of time, at a specified interest rate. This type of credit is often used to purchase cars, furniture and appliances and for personal loans. The following disclosures must be made in writing prior to the loan closing:

- ◆ **NAME** of the company financing the loan.
- ◆ The **AMOUNT FINANCED** and a list of **WHAT IS and IS NOT INCLUDED** in the amount financed (purchase price, down payment, taxes).
- ◆ The **FINANCE CHARGE** which includes interest and other fees, expressed in a dollar amount.
- ◆ The **ANNUAL PERCENTAGE RATE (APR)**. This is the cost of the credit expressed as a yearly rate.
- ◆ The **PAYMENT SCHEDULE** which includes



the number of payments, the amount of each, and when they are due.

- ◆ The **TOTAL AMOUNT** of the payments.
- ◆ The **PREPAYMENT PENALTY**, if applicable. This is a charge for paying the loan in full before the end of the loan period.
- ◆ The **LATE PAYMENT CHARGE** if the payments are not made on time. The consequences of not making payments on time is also explained.
- ◆ The **SECURITY INTEREST**, if any. For example, with a car loan, the car becomes the security for the loan. If payments are not made as agreed, the creditor can take the car.
- ◆ **INSURANCE CHARGES**, if any. For example, credit life insurance will pay the loan in full if the borrower dies. This coverage is optional, at the borrower's choice, and is an expensive way to buy life insurance.

Open-end credit allows consumers to incur new debt before paying off old debt. The borrower receives a line of credit and agrees to repay at least a partial amount each month. Most credit cards are this form of credit. The disclosures are different than those required for closed-end credit. Look for the following terms in an application for open-end credit:

- ◆ **ANNUAL FEE**: An amount charged to you once a year for the opportunity to use the credit. Not all open-end accounts have annual fees.
- ◆ **ANNUAL PERCENTAGE RATE**: The annual percentage rate (APR) is the annual interest rate you will be charged on any unpaid balance. Some creditors offer set or fixed rates, while others may have a variable rate (a rate that may change from month to month). If there is a variable rate,

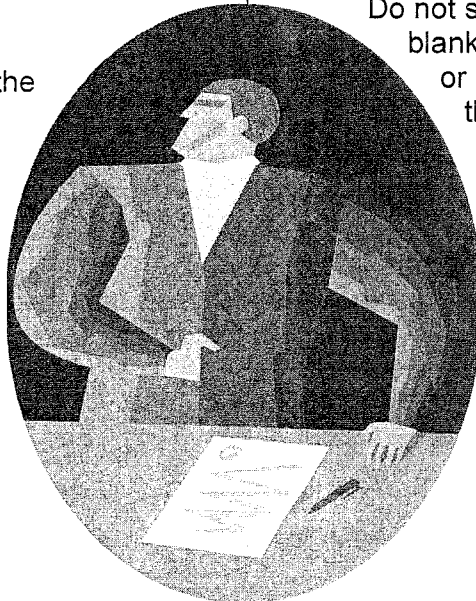
the disclosure statement will tell you how the rate is determined, how often it may change, and by how much.

- ◆ **MINIMUM PAYMENT:** The minimum amount which must be paid by the payment due date; usually between 1.5-4% of the unpaid balance.
- ◆ **LATE AND OVER LIMIT FEES:** The amount that you will be charged if you are late with a payment or go over the credit limit.
- ◆ **GRACE PERIOD:** The number of days you have to pay off your bill before interest is charged. Typically grace periods are 20-25 days in length. The grace period only exists if you do not have a previous balance. Not all open-end credit has a grace period.

- ◆ **CASH ADVANCE:** The cash advance feature allows you to make cash withdrawals against your line of credit. Withdrawals can be made through an ATM, at a bank or by cashing special checks. Interest rates on cash advances are usually higher than those on purchases. Moreover, there is no grace period on cash advances.

Before you sign or co-sign...

1. Read the contract carefully and completely.
2. If you do not understand the contract or if a particular item is unclear, have someone who is knowledgeable read and explain each item to you. Do not sign the application or contract unless you understand everything to which you are agreeing.



3. Make sure that all spaces are filled in. Do not sign the contract if there are blank spaces. Fill in blank spaces or draw a line through them if they are not applicable.
4. Make a copy of the final contract after you sign it. Keep this copy for your records.

The Credit Report

Every month, when you make a payment on time, are late with a payment, or miss a payment, this information is recorded on your **Credit Report**. There are three main credit reporting agencies, also called credit bureaus, in the United States: Trans Union, Equifax, and Experian (formerly TRW). Each credit bureau operates independently, thus, the format of their credit reports may differ somewhat. They all include the following types of information in their reports:

IDENTIFYING INFORMATION: The first section lists your name (including any aliases), your social security number, your address, and your most recent employers. (If you have had more than one address or employer within the last five 5 years, more than one may be listed on your report).

PUBLIC RECORD INFORMATION: This section shows any items that have gone through the court system. These include tax liens, bankruptcies, foreclosures, or court ordered child support.

ACCOUNT INFORMATION: This is the section most people think about when they hear the words "Credit Report". Listed here are the creditors with whom you have accounts, the type of accounts (i.e. revolving, installment, mortgage), how much you currently owe on each account, your monthly payments, your credit limit with each creditor, and your repayment history with each. The repayment history includes whether your payments were on time or late, and if late, how late.

INQUIRIES: This section lists the names of creditors who have viewed your credit report. Your credit report can only be reviewed if there is a "permissible purpose." Anyone reviewing

your credit report must have your permission and do so only if there is legitimate cause. It is your right as a consumer to review your credit report. In fact, it is suggested that you look at your credit report at least once a year, and definitely before a major purchase, such as a house.

Creditors do not have to report to all three agencies. In many cases, they may only be affiliated with a single agency. For this reason, it is suggested that you review credit reports from all three agencies. This will allow you to be aware of all of the credit information that has been compiled about you, and therefore to know the information on which the creditor will be basing his/her decision.

You can order your free annual credit report:

- online at www.annualcreditreport.com
- by calling 1-877-322-8228
- by completing the Annual Credit Report Request Form and mailing it to: Annual Credit Report Request Service, P.O. Box 105281, Atlanta, GA 30348-5281

When you order, you will need to provide your name, address, Social Security number, and date of birth. To verify your identity, you may need to provide some information that only you would know, such as the amount of your monthly mortgage payment.

If you have been denied credit based on information in your credit report, you may receive within 60 days of the denial a free copy of the credit report that was used.

Contact information for each of the three major credit bureaus is below.

Equifax
P.O. Box 740241
Atlanta, GA 30374-0241
(800-685-1111)
Web site: www.equifax.com

Experian
P.O. Box 2104
Allen, TX 75013-0949
(888-397-3742)
Web site: www.experian.com

Trans Union Corp.
760 W. Sproul Road
Springfield, PA 19064-0390
(800-888-4213)
Web site: www.tuc.com

Commonly Asked Questions About Credit Reports and Credit Scores

How can my credit report be used?

Credit reports are used for more than just extending credit. They may be viewed by landlords for apartment rentals; by employers before hiring potential employees, before promoting a current employee, or for issuing security clearances; and by insurance companies prior to selling an insurance policy. To view your credit report, an individual must have a legitimate business need in connection with a transaction initiated by you to review an account. For example, a potential employer must have written permission before looking at your credit report. If you do not give permission, the employer cannot hold this fact against you when determining if you should be offered the job.

How long does information stay on a credit report?

Most information will stay on your credit report for seven years. Inquiries made by creditors when you apply for credit stay on your credit report for two years, and bankruptcy can stay on a credit report for up to ten years. Recent inquiries used for credit solicitation or account review may also appear, although only the report sent to the consumer contains these inquiries. When information is deleted from a credit report, it does not mean the debt is no longer owed. The creditor can still continue to collect the debt unless it was discharged through bankruptcy.

What should I do if there is a mistake on my credit report?

If after reviewing your credit report you believe that there is incorrect information listed, you can dispute it through the credit reporting agency. A dispute form, enclosed with the credit report, can be completed and sent to the credit

reporting agency. The agency then has 30 days to research the dispute. If they find there is a mistake, the incorrect information is taken off your report and a copy of the new report is sent to you and anyone else who received the report within the last 6 months. If the credit bureau's records prove to be correct, the information will stay on your credit report. If you still believe it is inaccurate, you can dispute the information with the original creditor. If the credit reporting agency cannot verify if the item is true or false, it will be deleted from your record until it is verified.

It is your right to put a statement, up to 100 words, at the end of your credit report explaining the situation that may have caused you to become delinquent.

How do I *FIX* my credit report to improve my credit score?

The information in your credit report is used to create your credit score. Lenders use your score to determine whether or not to grant you credit, and if so, how much and at what interest rate. Thus, a good credit score is important in order to obtain credit and to qualify for the best possible terms.

If you are not happy with your credit score or think it may be affecting your ability to obtain credit, there are some steps you can take to improve it. First, be sure your credit report is accurate. Your score will only be as good as the information in your report. Next, pay all of your bills on time and stay current on all of your active accounts. A credit history with a pattern of late payments can negatively impact your score. Keep in mind that while past repayment patterns can remain on your credit report for up to seven years, your credit score is more heavily weighted on your recent repayment history. Finally, avoid any companies who claim they can improve your credit score. There is nothing these companies can do for you that you cannot do on your own – for free!

The Center for Personal Financial Education is an educational resource and research center whose mission is to advance the adoption of sound personal financial practices by developing and delivering personal financial education programs and conducting related research. The Center, established in 1996, is a joint venture between the University of Rhode Island and the Consumer Credit Counseling Service of Southern New England.

Development of the Getting Fiscally Fit program was made possible by a grant from the CDNE Foundation.