

CHAPTER 7

Section 2-
Getting
Started with
Credit

CREDIT

- The ability to borrow money and pay it back later.
- The purpose is to allow buyers to purchase items and pay for them in the future
 - Creditor—The person or business that lends money
 - Debtor—The person who borrows money
- A savings or checking account is a good way to start with credit and keep it in good standing
- Credit card applications require (to determine creditworthy)...
 - Name
 - Address
 - Social Security number
 - Place of employment, income, length of employment

SERVICE CREDIT

- The ability to receive services and pay for them later
- Examples...
 - Electricity
 - Water
 - Sewer
 - Doctors
 - Dentists
- Some companies require a deposit to begin using service
- Deposit is usually refunded after a good payment record is established

REVOLVING CREDIT

- An account on which the account holder can charge repeatedly up to a maximum limit
 - Payments are made monthly on this account or paid in full based on a statement date
 - Account can have an ongoing balance, but requires a minimum monthly payment
 - Interest is charged on outstanding balances
- Most commonly recognized revolving credit account is a credit card
 - Credit Card-a plastic card linked to a credit account that can be used to make purchases.
 - Examples: Credit Cards (Visa, MasterCard, Discover)

STORE ACCOUNTS-AS CREDIT

- A credit account that allows you to charge items or services only at that store or with that merchant
- Classified as Installment Credit or Revolving Credit
- Cards issued by department stores, gas companies or other retail merchants
- Usually have high interest rates
- Require monthly payments
- Examples: Kohls, JcPenny, Macy's, Scheels, Menards

STORE ACCOUNTS-AS INSTALLMENT CREDIT

- Credit used to finance a single high-priced item through a series of equal payments over a set period of time
- Usually have high interest rates
- How it works...
 - Require monthly payments
 - Used to finance a single large purchase
 - Example: Appliances/Furniture
- You are not issued a card, you sign a document that is like a contract

CHARGE CARDS

- A form of credit card where the balance must be paid in full each month.
- Balance must be paid in full each month
- No interest charges
- No service fee
- Large annual fee
- Examples: American Express, Diner's Club

CONSUMER LOANS

- A direct loan of cash with a fixed interest rate for a set period of time.
- Single-payment loan-set amount borrowed with fixed interest rate, with entire amount due on a certain date (farmer's loans)
- Secured loan has collateral
 - Collateral-is security for the loan-something that can be taken if loan isn't paid
 - Examples: Mortgage Loan-House is collateral
 - If loan is not repaid, lender can take possession of collateral and sell it to get the money owed
 - If poor credit or no collateral, a cosigner may be required
 - Cosigner-a person that signs a loan agreement with the borrower and agrees to repay the loan if the borrower doesn't
 - Cosigner must have good credit

LINES OF CREDIT

- A preapproved loan amount that a debtor can borrow against, pay back, or borrow again as needed
 - Available through banks or credit cards
 - Maximum amount set
 - No interest is charged on the unused portion of the line of credit
 - Small businesses use this type of credit to make equipment purchases or complete a new project

BENEFITS OF CREDIT

■ Convenience and Rewards

- Consumers set up automatic billing to pay bills
- Paying one credit card bill each month more convenient than lots of little bills
- Reward features offer points or cash back for using the card
- Points can be used to purchase merchandise

■ Increase Spending Power

- Allows for a higher standard of living
- Don't have to wait to buy things (save the money)
- Allows purchase of expensive items that might not otherwise be able to be purchased (home or car)

BENEFITS OF CREDIT

- **Records**
 - Monthly statement provides you with a record of your spending
 - Benefits for resolving disputes with merchants about purchases
- **Benefits or protections from risks from using a credit card**
 - No charges for fraudulent use of the card
 - Withhold payment for disputed items
 - If store refuses to refund the price of a returned item (90 days) the credit card company will refund the money—up to \$500
 - Goods that are damaged or stolen within 90 days of purchase the credit card company will replace or refund eligible items
 - 24 hour emergency replacement for lost cards

CREDIT SCORE

- Score that shows your credit worthiness-ability to repay money borrowed
- Known as your FICO-is compiled on a point system
- Calculated on 5 categories
 - Payment history (35 percent)
 - Amounts owed (30 percent)
 - Length of credit history (15 percent)
 - New credit accounts opened (10 percent)
 - Types of credit used (10 percent)
- Credit Score available through 3 credit bureaus
 - TransUnion
 - Equifax
 - Experian

CREDIT SCORE (CONTINUED)

■ Score Ranges

- 700-850 is excellent
- 600's-very good score, minimum range needed to get a mortgage loan
- 500s-average
- Below 500-means lack of credit or poor credit

CREDIT REPORT

- **Credit Report**-a statement of your credit history issued by a credit bureau
 - A complete record of your borrowing and repayment performance
 - It provides a basis of your creditworthiness and helps creditors determine your ability to pay new debt.
 - Based on your credit report, you can be granted or denied new credit.
 - Everyone who uses credit has a credit report
 - Information is stored by your social security number
 - Provides evidence of your financial responsibility

CREDIT REPORT (CONTINUED)

- Entitled to 1 free credit report yearly from each credit bureau
 - Website: Annualcreditreport.com
 - If denied for credit you have 30 days to request a report
- Authorized users of your credit report include:
 - Employers, banks, insurance companies, landlords, investigators

CREDIT BUREAU

- A business that gathers, stores, and sells credit information to business members
- Three credit bureaus
 - TransUnion
 - Equifax
 - Experian
- Credit bureaus compile information monthly from businesses that report information

WAYS TO IMPROVE CREDIT SCORE

- Pay debts promptly
- Reduce outstanding credit (amounts owed) compared to total credit available
- Don't apply for more than one credit card at a time
- Keep a good mix of credit types (credit cards, credit accounts, installment loans, mortgages)
- Too much revolving credit can hurt you

WHY REVIEW YOUR CREDIT REPORT

- Check credit report on regular basis to make sure that it contains correct information
 - Incorrect information can cause you to be rejected for a loan
 - Incorrect information can increase your interest rate
 - Removing incorrect information can improve your credit score
- Helps to prevent identity theft
- Allows you to make sure that all credit accounts that are reported on your report are actually your accounts
- Allows you to check for fraudulent activity