Credit Basics

Reviewing:

• Types of credit available
• Finance charges- what they are and how they're applied
• Consumer's Rights

Types of Credit Available

There are a wide variety of credit options available to consumers. The following information reviews those options.

Installment Loans: are issued by lenders on the basis of credit worthiness with a fixed repayment schedule.

Installment loans are typically calculated with a simple interest rate and a fixed payment amount each month. A certain amount is paid towards principle and a certain amount toward finance charges each month. An installment loan may or may not have collateral attached. If collateral is held on the account and payments are not made as scheduled, the lender may reclaim the property held as collateral. If no collateral is held on the account and payments are not made the lender will have less recourse if payments are not made as scheduled; however legal action may be pursued in all cases if deemed necessary. Fees are typically applied if payments are not made as scheduled, but installments loans generally have a grace period.

Credit Cards: are issued by a variety of lenders. This can include your bank where you keep your savings, or a lender that solely deals with credit cards.

- Credit cards allow consumers to make transactions based solely on credit.
- The purchases made are added to the balance each month, along with any finance charges for that billing period.
- Credit cards typically have a credit limit placed on them. This is usually determined by the consumer's credit rating.
- Annual Percentage Rate (APR) on a credit card is computed as compound interest, because of that, the amount of the monthly finance charges will fluctuate from month to month.
- The monthly payment on these accounts will be variable, depending upon the balance. Each month a different amount goes towards principle and interest.
- Late payments on these types of account are generally penalized with a late fee that could be as much as $39.00 if the payment is even a day late.

Merchant Charge Cards are typically offered for exclusive use in the merchant's business. These accounts are typically treated the same as a credit card account in regards to credit limit, APR structures and payment requirements.

Lines of Credit: may be extended by a number of financial institutions.

- A line of credit is simply an account held with a bank, maintaining a consistent credit limit that can be borrowed from as needed.
- A line of credit will have an APR applied to the balance each month. The percentage rate would be fixed, however the amount of finance charges on the account would vary depending on the balance.
- For example, a consumer may have a line of credit for home repair with a limit of $5,000.00 where they borrow periodically for repairs and then repay on a monthly payment schedule. The payment schedule will fluctuate each month, as will the amount of the finance charges.

Mortgages: are issued to assist consumers in purchasing a home. Unless you are an independently wealthy person, you will need a mortgage for the purchase price of a home. There are several types of mortgages available that a consumer may choose from.

Finance Charges

Annual Percentage Rate (APR) is the rate of interest a consumer is charged over the time period of one year. This is then broken down into monthly amounts and added onto the existing balance of an account. There are three main methods of calculating monthly finance charges

Average Daily Balance
This method, which is the most commonly used, works as follows: The company tracks your balance each day, adding any charges and any subtracting payments as they occur. At the end of the billing cycle, they compute the average of these daily totals and then multiply this number by the monthly interest rate to calculate your finance charge.

Adjusted Balance
This system, which consumer experts say favors the cardholder, takes the balance from your previous statement, adds new charges, subtracts the payment you made and then multiplies this number by the monthly interest rate.

Previous Balance
This method generally favors the card issuer, according to consumer experts. The credit grantor multiplies your previous statement's balance by the monthly interest rate to find the new finance charge. This means you're still being charged interest on your balance even after you've made payments towards it. It's important when applying for credit that you look at how the lender calculates their finance charges. Some methods are better for consumers; some are better for the creditors. Also included in the monthly finance charges are any fees that are charged by credit grantors on the credit that they have extended. These fees vary from creditor to creditor but the main fee structure is for the most part, uniform. Among these fees include the following, but are not limited to;

Late fees, which are charged whenever a payment is not received by it's due date and could range from $10.00 to as much as $35.00 per month.

- **Over limit fees**, which are charged whenever the balance on the account exceeds the initial credit limit. These are typically $29.00 to $35.00 per month.

- **Past due fees**, which are charged whenever there is an amount that was not paid from the previous months billing cycle. These also typically range at $10.000 to $29.00 per month.
- **Transaction fees**, for any time a transaction is made with the account, these could range from $1.50 to $5.00, just for using the card.
- **Cash advance fees** will apply if cash is taken in place of a purchase and typically will carry a higher APR on that portion of the balance.
- **Monthly Maintenance Fees** applied for having the account opened with that institution.
- **Annual Fees** are applied once per year and my also be labeled as a **Membership Fee**. This is simply an annual cost to maintain that account.

When applying for credit, consumers should be aware of the fees listed above that are usually included in the service agreement.

A Consumer's Rights

With all of the different financial options available and the different aspects of each one, it's important for consumers to know their rights. For every aspect of the credit industry, their laws in place to protect consumers.

Before accepting any form of credit a consumer should know and understand how the finance charges that will be applied. Due to the *Truth In Lending Act*, each credit grantor is required to provide, in advance the annual percentage rate on the account and their method of calculating the finance charges. This allows for consumers to make educated decisions on which credit offers to accept. The information will be provided ahead of time, before any of the charges are applied. A consumer needs to review all of a creditors terms and conditions, prior to accepting the credit.

Also available to insure that consumers are treated fairly are several other acts that have been put in place to ensure equal treatment of credit applicants. The following is a listing of the these and a brief explanation of how they apply.

Fair Debt Collections Practices Act

The Fair Debt Collections Practices Act (FDCPA) was written as an amendment to the Consumer Credit Protection Act, to prohibit abusive practices by debt collectors.

One of the reasons for the amendment was stated as; "abundant evidence of the use of abusive, deceptive, and unfair debt collection practices by many debt collectors." The FDCPA covers such areas as misrepresentation, the acquisition of a consumer's personal information, communication in reference to a debt and harassment and abuse. The FDCPA is what determines when a collector can call you, and also how to stop collection calls. It's important for consumers to understand their rights in regard to collection accounts. The FDCPA governs what a collection agency can and cannot do.

Fair Credit Reporting Act

The Fair Credit Reporting Act (FCRA) essentially governs the manner in which Credit Reporting Agencies maintain and dispense information. The FCRA sets guidelines on the type of information that can be maintained, the extent of the information that is kept and the methods that the information they maintain is distributed to both consumers and to creditors. This Act also governs the accuracy requirements of the Credit Reporting Agencies to ensure that only factual information is maintained.

Equal Credit Opportunity Act
The Equal Credit Opportunity Act (ECOA) states that, "It shall be unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction" This includes race, religion, income, national origin, sex or marital status. The primary purpose of the ECOA is to insure that every consumer is given a fair chance when applying for credit. It lists all of the circumstances that would and would not be considered discrimination.

Each of the above Acts is to insure fair treatment for consumers when seeking credit. It also insures that lenders have all of the correct information that they need to make a fair and impartial decision.

For the full text of the above acts or for more information on this or any other topic, visit us on the web at www.delraycc.com.

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