THE COST OF CREDIT

Salesclerks often ask, "Will that be cash or charge?" What they want to know is whether you are going to pay with cash or with a credit card. Think before you answer. It is a very important decision.

You probably know all about paying with cash. But what about credit? Credit is simply a promise to pay for in the future what you buy or borrow today. Credit can be good or bad, depending on how you use it.

Unless you are eighteen and legally able to sign a contract, you can not take out a loan or open your own charge account. Most stores, however, allow shoppers under eighteen to use their parents' charge accounts if the parents have signed a release in advance.

Saying, "Charge it, please!", is easy, and buying many things at once is fun. But if you use credit too often or without thinking, you may end up in a "credit crunch" when it comes time to pay. In other words, you may find that you have more bills to pay then cash to pay them with. This happens often to buyers who make impulse purchases, or purchases made on the spur of the moment without planning. If you are that kind of shopper, credit is not for you.

If you plan carefully before you shop, though, credit can be a way to buy a new item that is more than you can afford at the moment. This lets you use the item before you pay for it. You can also take advantage of sales and bargains you might otherwise have to pass up. That is a credit " plus" that you can really enjoy.

Using credit almost always costs more than paying cash. Unless you pay the full price of your purchase within a short period. You must pay interest. The interest on the money you owe is called a finance charge. This charge is the fee you pay for the privilege and convenience of buying on credit. It is normally a percentage of the purchase price. The size of the percentage varies from bank to bank, store to store, and credit plan is credit plan. For this reason, it is important to study credit plans to find one that meets your needs.

As a rule, the longer you take to pay, the higher the finance charge will be. If you stretch your payments over many months, however, each payment can be small. You end up paying more over all because of the high finance charge, but that might be a trade off you are willing to make.

Thanks to the **"truth in lending law"** a store or bank must tell you three things about any credit plan:

a. the cost of the finance charge in dollars and cents,
b. the percentage of interest you pay per month

c. the percentage of interest you pay, which is called the annual percentage rate.

When you buy something on a credit, you must add the finance charge to the price of the item to find out what the item is really costing you. Suppose you buy a stereo turntable. If the purchase price is $150, the finance charge 1 1/2 percent per month, and you take 12 months to pay, you would figure the total cost of the stereo as follows:

1. List the purchase price: $150.
2. Find the annual percentage rate (1 1/2 percent x 12 months): 18 percent.
3. Find the total finance charge: (18 % x $150): $27.
4. Add this charge to the purchase price to find the total cost of the stereo: $177.

TYPES OF CREDIT

Many different types of credit are available from a variety of sources. The type of credit you should seek depends upon what you intend to use it for and your spending plan.

<u>CHARGE ACCOUNTS</u>
Many local stores offer charge accounts to their customers. The accounts are offered free as a service. Stores that give their customers credit, however, may charge higher prices for their goods than those that do not.

When charging at a small store, such as a butcher shop or a dry cleaner, you will be billed once a month. When you receive the bill, it is expected that you will pay the entire amount. Large department stores and chains will allow you to pay a portion of the bill monthly. They will then add a finance charge to the remaining balance.

<u>CREDIT CARDS</u>
Credit Cards are another way of charging your purchases. These are generally issued by banks and may be used in a wide variety of shops, theaters, restaurants, and hotels. You usually have to pay an annual fee for the card, and you must pay interest on the unpaid balance every month. Fees and interest rate vary from bank to bank, so it is worth shopping around before you apply for a card.

<u>THE INSTALLMENT PLAN</u>
When you want to purchase something major, like a car or furniture, consider an installment loan. This kind of loan is available through the retailer. It lets you pay for the item over a period of months or even years.

On the installment plan, you must first pay a lump sum, called a down payment. Then you make monthly payments, which include interest, until the total purchase price, plus interest, is paid.

Every time you want to purchase a new item on the installment plan, you have to re-apply for credit.

A WORD OF CAUTION
When paying for an item on the installment plan, the item is not really yours until you have completed all of the payments. If you miss payments, the store has the right to take the item back. You could lose the item as well as the money you have already paid for it.

THE LAYAWAY PLAN
Layaway plans are like installment plans except that you leave the item you have purchased in the store until all the payments are made. You first make a down payment, and then the store puts aside the item for you. You pay off the remainder of the price with regular fixed payments. Stores do not charge interest on a layaway plan. After your last payment, the item is yours and you take it home. If you miss a payment, the item goes back on the sales floor. Some stores charge fees for this service; others do not.

BANK LOANS
If you ever need money for college tuition or perhaps to open up a small business, you can apply to a bank for a loan. The banker will do an in-depth credit check to see if you are a good credit risk. If you qualify, you will be asked to sign an agreement describing how much you will pay each month and for how many years. Then the money is yours.

The most common reason that people borrow money from banks is to by a house. Loans for this purpose are called mortgages. They are like installment credit in that you must make a down payment, and if you miss payments, the bank may sell your house.

A word to the wise: interest rates on bank loans vary greatly. So shop around for the best plan. Be sure to check the interest rate and the annual percentage rate you will pay.

DO YOU QUALIFY FOR CREDIT?

Your credit rating is simply a record of your past performance in paying what you owe. Your credit rating will be checked when you apply for a charge account or credit card, buy something on an installment plan, or try to borrow money from a bank. The store or bank contacts an office called a credit bureau. A credit bureau is a business that keeps a detailed record of how people pay their bills. It can report how you have paid your bills starting from the very first time you bought something on credit. If you keep a good credit rating, your new charge accounts or loans will be readily approved. A good credit rating is one of your most valuable possessions!

When you apply for credit, you will be asked to fill out an application. This form has questions designed to find out if you are a good credit risk. The following are a few questions you will usually find on a credit application:

Do you have a job? If so, what is it? How long have you had it?
What is your salary?
Where do you live? How long have you lived there?
How much do you already owe?

Your answers will help to decide if the company will give you the credit or loan. In the case of credit cards, they will be used to determine your CREDIT LIMIT. That is the most you will be allowed to charge to, or the maximum you can owe the company at any time.

It is **not** legal for the store etc. to ask you any questions regarding your religion, race, age past 18, or marital status. The Equal Credit Opportunity Act prohibits businesses to take this type of information into consideration as they make decisions on your credit worthiness.

Reference: TEEN GUIDE, McGraw Hill 1990