

Credit Cards

Teens are interested in credit cards, and why not? Advertising makes buying look easy when paying by plastic. But there can be high costs associated with using credit cards. Every teen needs to be aware that they represent an important “target market” for credit card issuers. Understanding how credit cards work before heading off to college will help students avoid credit pitfalls.

This study guide uses a Consumer Action publication, “Credit Cards...What You Need to Know.” It contains the essential information everyone needs to know about credit cards. Additional teaching material is also available for leaders from Consumer Action. The remainder of the text in this guide is from the Consumer Action publication.

Introduction

Credit is a valuable and necessary financial tool. It can help you establish a credit history, make purchases conveniently, and take advantage of the benefits and services offered by credit issuers. Not managing your credit wisely can lead to:

- increased annual percentage rates (APRs),
- unnecessary fees,
- a decline in your credit score, and
- denials of future credit.

All of these negative consequences can be avoided. The information below will help you:

- understand the different types of cards available,
- sort through offers to choose the card that is right for you,
- understand credit card terms and conditions,
- avoid fees and penalty rates, and
- know where to go for more information and assistance.

Types of Cards

Credit Cards

- Revolving credit line
- Pre-set credit limit
- Pay charges in full, pay the minimum due, or make a partial payment

Charge cards

- All charges due in full every month
- No interest charged
- No pre-set spending or credit limits

Secured credit cards

- Guaranteed by money deposited in an account
- Credit limit equals the amount of the deposit

Sub-prime credit cards

- Low credit line, large up-front fees, high interest rates
- Marketed to people with lower credit scores

Prepaid or stored value cards

- “Loaded” with funds using cash, debit, or credit card
- Value reduced as card is used
- Can be “reloaded” to add more money

- No interest charged
- Initial fees to buy and load the card, subsequent fees to reload

Card Offers

There are two types of card offers – pre-approved and invitations to apply. These offers come in the mail, by telephone, online, and in-person at some retail stores.

Pre-approved offers are made based on your credit history. Federal law requires that these contain a firm offer of credit. The only exception is if you have experienced a serious decline in creditworthiness since the offer was made.

Invitations to apply simply ask you to apply for a card. They do not require a firm offer of credit.

To compare basic terms on card offers, look for a box listing interest rates, the grace period and annual fee, among other information. This box, required by law, is often headed with the words “disclosures” or “summary of terms.”

Before responding to any offer, you should know that:

- Not all terms are included in the initial offer. Important information can be found only in the “cardholder agreement” that will be sent with your new card.
- You may not qualify for some offers you receive. Once you apply, you may be offered less favorable credit terms.
- Card offers often state: “You have been approved for a credit line of up to \$100,000.” The key words are “up to.” When you apply, you won’t know how much credit you will receive. The company can, and often will, give you a lower credit limit.

- “No annual fee” offers may require you to make a minimum number of purchases using the card or you will be charged an “inactivity fee,” similar to an annual fee.
- A “fixed introductory rate” is fixed, but only for the introductory period, such as six months. The rate will change after that time and may even become a “variable rate.”
- Fixed interest rates can change at any time after a 15-day change-in-terms notice. Fixed rates can also change if you pay late or do anything else to expose yourself to a penalty rate increase – for example, making a late payment or bouncing a check.
- Many offers include the opportunity to transfer a balance from another card without paying a fee. Ask if you can wait until you get the card to transfer a balance. If the balance you want to transfer is higher than the credit limit on your new card, the company will only transfer a portion of your balance, leaving you with a balance on the old card.
- Sometimes, cards have low introductory rates that are good for balance transfers or purchases or both. In this case, your payments are typically allocated first to the balances with lower APRs. Higher interest balances are paid down only after balances with lower APRs. Sometimes, the low balance transfer rate comes with a requirement that you must make a minimum number of new purchases each month.

If you have any questions about a credit card offer, check the company’s website for more information, or call the company’s toll-free number before you apply.

Card Terms and Conditions

When you receive your new card, you will also receive a “cardholder agreement,” a legal contract between you and the card issuer. By using your new card, you agree to honor the terms and conditions in the agreement.

Terms and conditions in the cardholder agreement can change at any time. Changes are usually sent to you by mail. When you use your card after receiving the notice of changes, this means you have accepted the changes, even if you didn’t read the notice. Read everything your card issuer sends.

Save your cardholder agreement in a file that is easily accessible so you can refer to it when you have questions.

Terms to know include:

- **Annual percentage rate (APR):** A card’s interest charge, expressed as a yearly rate.
- **Variable rates:** Interest rates that change according to a set formula, such as Prime Rate + 3 percent. If your card has a variable rate, the APR changes when interest rates change.
- **Fixed interest rates:** The set APR on your card, which can change only when you receive a 15 day notice.
- **Default or penalty rate:** A higher interest rate charged if you pay late, bounce a check, or your credit gets worse. Also charged by some card issuers if you pay late on credit cards or loans with other banks.
- **Cash advance APR:** The interest rate you pay when you use your card to get cash. Most cards charge a higher interest rate for cash advances than for purchases.
- **Daily periodic rate:** Your APR divided by 365 days.

- **Arbitration:** A form of dispute resolution that is often binding with no right to appeal. Arbitration provisions may prevent you from suing the company in court or participating in class action lawsuits. However, some companies allow you to take your case to small claims court if the amount you are disputing is within the small claims limit.
- **Balance transfers:** The ability to transfer the balance from one card to another. If applicable, interest on balance transfers begins to accrue immediately.
- **Convenience checks:** Checks linked to your credit card account. They can be used to transfer a balance from another card or to make purchases or payments.
- **Double-cycle billing:** The calculation of your interest considering your average daily balance over a two month period, which may result in additional finance charges.
- **Grace period:** Period in which finance charges do not accrue if you are not carrying a balance.
- **Minimum monthly payment:** The lowest amount that you are required to pay the credit card company each month.
- **Payment due date:** The last day a payment can be accepted without penalty. Your payment may be required to arrive by a deadline on the due date, such as 1 p.m.
- **Prime Rate:** The “index” most commonly used to determine variable interest rates. It can be found in the business section of your newspaper or online.

Avoiding Credit Card Fees

You can avoid fees by carefully managing your account. Here are common fees and tips on how to avoid them:

- Annual or monthly fee: Common on charge cards, rewards and airline miles credit cards and on secured and sub-prime cards. Sometimes applied if you don't use your card at least a few times during the year.

TIP: Consider the overall value when comparing fee and no-fee cards. If you are thinking about getting a rewards or airlines miles card, make sure the card's benefits are worth the cost of an annual fee.

- Application processing fee: Charged on many sub-prime cards and some secured cards when an account is opened.

TIP: Secured credit cards are generally much better deals than sub-prime credit cards, and you can find secured credit cards that don't charge application fees.

- Account reopening fee: Charged if your account is closed or cancelled by the issuer and you ask to have it reopened.

TIP: Pay your bills on time to avoid card cancellation and an account reopening fee.

- Balance transfer fee: Charged for transferring a balance from one card to another; this fee is commonly assessed as a percentage of the balance transferred.

TIP: When you apply for a new card, ask about balance transfer fees. Most companies don't charge these fees to new cardholders for the first month or two.

- Bounced check or returned item fee: Charged if your check bounces.

TIP: Make sure you have sufficient funds in your bank account to cover your check.

- Cash advance fee: Charged as a percentage of the cash advance, with minimum charges common.

TIP: Cash advances are an expensive way to get cash. Not only do you pay a fee, but interest on cash advance balances begins to

accrue immediately. Instead, use your ATM or debit card to withdraw cash from your checking or savings account at ATMs.

- Foreign currency conversion fee: Charged when you make purchases overseas and the charges have to be converted to U.S. dollars.

TIP: If you plan to use a card while traveling outside of the U.S., shop around to find a card with a currency conversion method that is favorable to you.

- Late fee: Charged if your payment is late, sometimes even if it is received on the due date after a certain hour.

TIP: Always pay your bill on time. If you send your payment by mail, allow at least seven days for the payment to reach your issuer. Consider other payment methods, such as online bill pay, pay-by-phone, or automatic payments. Ask if your issuer offers e-mail reminders.

- Pay-by-phone or computer fees: Charged by some companies to pay your bill by phone or computer.

TIP: Avoid last minute, fee-based payment methods. Look for online bill pay, pay-by-phone, or automatic payments that do not carry a fee.

- Over-the-credit-limit fee: Charged if you go over your credit limit.

TIP: Know your credit limit. Call your card issuer in advance if you need an increase. Ask your issuer if it has free e-mail services that alert you when you are approaching your credit limit.

- Statement copy fee: Charged for extra copies of monthly statements.

TIP: File statements for the past three years in a secure location. If you sign up for online access to your accounts, you can download your statements and keep them in your computer.

- **Stop payment fee:** Charged when you stop payment on a credit card convenience check.

TIP: Be cautious about using convenience checks. If you write one and it is lost, you may not be able to avoid this fee.

- **Wire transfer fee:** Charged when you use your card to transfer money or when you buy money orders, lottery tickets, or casino gaming chips.

TIP : Pay for these services with a personal check or cash.

Links from Article

- www.bankrate.com
- www.cardweb.com
- www.cardratings.com
- www.ftc.gov
- www.federalreserve.gov/consumers.htm
- www.americanexpress.com

For More Information

Bank Rate (www.bankrate.com)

Bank Rate provides free credit card tips and rate information.

Consumer Action (CA)

(www.consumer-action.org)

CA's site features free credit card surveys with interest rates, fees, and other terms for dozens of credit cards, as well as free brochures and guides on choosing and using credit cards (provided in Chinese, English, Korean, Spanish and Vietnamese). CA also

provides consumer advice and suggests appropriate complaint-handling agencies. Leave a message, and a counselor will call you back. Chinese, English, and Spanish spoken. 415-777-9635 and 213-624-8327, TTY: 415-777-9456; e-mail: hotline@consumer-action.org.

Card Web (www.cardweb.com)

Card Web lists credit cards and offers e-mail newsletters for consumers, answers to frequently asked questions, and online credit card calculators.

Card Ratings (www.cardratings.com)

Card Ratings lists and reviews credit cards and offers tips and credit card calculators.

Federal Trade Commission (FTC)

(www.ftc.gov; 877-382-4357)

The FTC offers a wide range of free publications on credit and consumer rights. It also accepts complaints from consumers for use in investigating violations but does not resolve individual complaints.

Federal Reserve Board

(www.federalreserve.gov/consumers.htm)

The Federal Reserve provides a free brochure on choosing a credit card and a guide to credit protection laws.

American Express

(www.americanexpress.com)

Tips on money management, fraud protection, travel, and shopping online and more. From the home page, click on "About American Express" and then on "Consumer Resources," then "Ask American Express."

*Consumer Action created this publication in partnership with American Express.

This publication is available as a PDF download at

http://www.consumer-action.org/downloads/english/2005_CC_terms_en.pdf. It may be ordered in bulk quantities free of charge from Consumer Action. An order form will be posted to the Consumer Decision Making website.

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