

This booklet is one of a series of consumer guides published by [] to help you get more for your money.

Read it to learn how to avoid paying more than you need to when you borrow or buy on credit and to learn some important rights you have when you use credit. These rights have been created by both state and federal laws.

Because credit is widespread and readily available, using credit wisely is more important than ever before.

1. Types of Credit

All credit is either "**closed-end**" or "**open-end**".

With **closed-end credit**, you borrow a fixed amount for a certain period of time and must repay in regular installments (usually monthly). The finance charge (interest) you pay is added to the fixed amount you borrowed, and repaid over the life of the loan.

Credit cards are the most common examples of **open-end credit** which are sometimes called revolving charge accounts. The finance charge (interest) you pay under an open-end credit plan is figured differently than for a loan. Here, the amount of interest you pay depends on the size of the unpaid balance each month. The larger the amount you leave unpaid each month, the greater the finance charges you must pay.

This first section explains the most common ways you can borrow or buy on credit, the law that regulates each way, and the maximum rates you can be charged. NOTE: Not all lenders, credit card companies and merchants charge the same. So shop around to compare interest rates and the terms of the credit.

Small Loan Act (AKA Consumer Loan Act): This law regulates the terms and interest rates of loans you can get from a bank, consumer finance company (small loan company), a savings and loan association, or a credit union.

HERE'S HOW THE APR AND THE TIME YOU TAKE TO REPAY A LOAN AFFECT THE FINANCE CHARGES...

Suppose you need to borrow \$10,000 for a new car. The amount might be obtained through various sources at different rates. By using the chart below, compare the **Total Finance Charge** for 3 ... 4 ... 5 years at these 3 interest rates.

Amount Financed	APR	3 years		4 years		5 years	
		Monthly Payment	Total Finance Charge	Monthly Payment	Total Finance Charge	Monthly Payment	Total Finance Charge
\$10,000	16%	\$351.58	\$2656.88	\$283.41	\$3603.68	\$243.19	\$4591.40
\$10,000	12%	332.14	1957.04	263.34	2640.32	222.45	3347.00
\$10,000	9%	318.00	1448.00	248.85	1944.80	207.58	2454.80

You can see that the APR makes a considerable difference in how much a loan costs.

You also can see that the longer you take to pay off a loan, the more you will pay in **Total Finance Charges** - even for loans with the same APR.

HERE'S ANOTHER EXAMPLE

Suppose you need to borrow \$40,000 for a mobile home. If you borrow this amount at an **Annual Percentage Rate (APR)** of 14%, over 15 years, your **Total Finance Charges** will be \$55,886. If you were to find a lender who would make the loan at 13% APR, the **Total Finance Charge** would be \$51,098...

...a savings of \$4,788!

If you can't pay. If you "default" on a loan (that is, fail to make your payments), you must be given written notice that you have defaulted and you must be given time to "correct" it, in other words, to catch up on your payments or "cure".

If you're not able to catch up. The amount of money a lender can take from you if you have defaulted and don't correct it is limited to the amount of money you still owe, late charges and interest on that amount.

If you have defaulted, a common way for the lender to get the money you owe is to repossess the collateral and sell it to recover the money you weren't able to pay. If the money from the sale is not enough to pay off what you owe, you might be liable to pay the lender the difference. This is called a deficiency and can be enforced by a lawsuit against you.

If there is a default sale, you are entitled to a detailed accounting of all proceeds from the sale. This will help you make sure all the proceeds went toward paying-off your debt, and that any other costs that are part of the sale (attorney's fees, cost of repossession) are reasonable.

Under certain circumstances - when the loan was for personal, household or family purposes - the lender may be prevented from taking any extra money (deficiency) from you.

Co-signing. Federal law provides that, prior to signing, co-signers must be given notice of specific obligations they undertake by their act of signing. It generally is not a good idea to co-sign on a loan because when a lender requires a co-signer it means the lender has some doubts about the borrower's ability to repay.

The title "Small Loan Act" may be misleading. Any loan that meets the conditions outlined below may be called a "small" loan regardless of size. Some "small" loans are for many thousands of dollars.

For credit to fall under this act, there may be restrictions on the collateral that can be accepted. Collateral is an item, or items, put up to guarantee that you will repay the loan. If you don't, you can lose the collateral. Most often, the item you purchase with the credit becomes the collateral. Another item frequently used as collateral is a car if it's paid for. Under this law, certain things may **not** be pledged as collateral under both state and federal law. These include certain personal effects and "generic" security such as "household goods".

Loans taken out under this law are usually repaid in equal monthly payments; "balloon" payments, where the last payment is larger than the others, are generally disfavored for this kind of loan. There are limits to additional loan fees which may be charged for a small loan, and you may not be charged a penalty for paying off the loan early.

Even though interest is repaid over the life of the loan, a much greater portion of the interest is earned by the lender early in the loan. Therefore, if you pay off a one year loan after just six months, you would **not** be entitled to half of your interest back. ["Here explain refunding"]

NOTE: The maximum rates for credit mentioned in this guide are listed as the Annual Percentage Rate (APR). Federal law requires lenders, merchants who offer credit cards or arrange credit for their customers, and credit card companies to state the interest you're charged as the APR. This figure is the one you should ask for and use when you compare the interest rate for different types of credit.

Under the Small Loan Act, the maximum interest rates are as follows: []

A loan under the Small Loan Act might be "overdraft checking", which gives you a pre-arranged borrowing limit and allows you to write yourself a loan when you overdraw this special type of checking account.

Retail Credit Sales Act: Let's say, for example, you buy a refrigerator at an appliance store and the dealer "sets up" the financing for you, allowing you to pay for the refrigerator over several months.

In almost all cases, the dealer will sell the contract or "paper" you've signed agreeing to make payments for the refrigerator. Most frequently it will be sold to a bank or finance company and the result will be **like** a loan. But when a merchant sets up or arranges credit, this is a "time sale", **not** a loan.

For a time sale, the collateral for the merchant is almost always the item purchased. Your payments usually are - but need not be - equal in size and due monthly. And you may be charged a penalty if you pay off the balance in full early. Because of these potential added costs, be sure to read the agreement carefully **before** you sign it to make sure you know the date you must have the balance paid off and the total amount to be repaid.

A time sale arranged by dealers under the Retail Credit Sales Act often can be convenient but can cost you more than some of the other credit sources explained in the second section of this guide. On the other hand, some merchants offer free credit for a certain period of time such as "ninety days same as cash" arrangements. With this plan, you have 90 days to pay for the purchase in full with no finance charges. But if the entire balance is not paid within the 90 days, finance charges must be paid - often at a relatively high rate.

NOTE: That 90 days is FIRM; on the 91st day it's just another contract.

be prepared to say "no". Then, if a lender requires insurance - and he may - be prepared to offer him other coverage or to go elsewhere for credit.

Do the shopping yourself. There is real convenience in having a merchant arrange financing for you, and many merchants do offer this service. You may want to take advantage of this, especially when "free" or very low cost credit is offered. But remember that it is an "extra" and it can be very expensive. The least expensive approach is to have your financing all arranged before shopping. You should at least know what your costs would be elsewhere before you take advantage of "in-house" credit. Even if the merchant offers to arrange the credit at the same lender for you, it may cost you much more than if you had gone to the same lender yourself.

And never sign a contract or loan agreement if any spaces are blank.

4. Consumer Protection

Regardless of which type of credit you use, the state and federal laws offer certain consumer safeguards listed below.

Penalty provisions. []

Discrimination. When considering whether to grant credit, lenders may not discriminate against you on the basis of your age, race, sex, marital status or religion.

services, vary greatly among the different types of lenders. You do not help yourself if you do not check with at least one lender in each of the above categories. Your final decision might rest as much on convenience or goodwill as on rate, but you should at least take the time to check options.

3. How to Cut Credit Costs

No matter what type of credit you choose or which source of credit you select, the following tips can help you save money . . .

Know what to ask. Be certain that when you begin shopping for the best deal, you know what to ask. Otherwise, a poorly directed question will get confusing answers about rates, maturities, terms and principal. Be certain that you know the amount you want to borrow, how long you will need to repay, and the purpose of the loan. What you want to know is the cost of the loan and the APR. Put your question something like this: "If I were to get an \$18,000 loan for a new car from you and I needed 36 months to repay, what would the cost of the loan be in dollars? The monthly payment? What is the APR (Annual Percentage Rate)?"

Focus on the Annual Percentage Rate. This is the one figure lenders are required, by State and Federal law, to disclose. Payback time may vary and cause changes in the total dollar cost and monthly payment, but the APR always will help you compare lenders. And remember, the lower the APR, the lower the cost for a given loan.

Know what "Extras" you want (or don't want). Most lenders will offer to sell you credit insurance which will pay the debt if you die, become disabled, or lose your job and cannot pay-back the loan. Lenders have the right to be insured, but they may *not force* you to buy credit insurance *from them or anyone they designate*. If a lender requires insurance, the law allows you to offer existing life insurance or disability income insurance or you can consider shopping for new coverage elsewhere. Credit insurance - especially the type which is purchased from a lender -can be *very* expensive. If you don't want it,

Credit cards issued by department stores, such as those from Sears and Penney's, and gasoline companies fall under the Retail Credit Sales Act. The finance charge rates you pay on these credit cards are []

Here's a tip: Find out how the finance charges are calculated on your credit card bill. You can generally avoid finance charges altogether because most credit cards won't charge any interest if you pay your balance in full before the due date each month.

If you usually don't pay the balance in full each month, then you should know that some methods of calculating finance charges are more expensive than others. Under the most frequently used method, the "average daily balance", finance charges you pay are based on when you pay as well as how much of the balance you pay off. So if your credit card uses the average daily balance, the more of the balance you can pay and the sooner you pay it after you receive your bill, then the less you'll pay in finance charges.

Two other common ways of computing finance charges are the "adjusted balance" (least expensive for you) and the "previous balance" (most expensive).

Here's another tip: If you keep an unpaid credit card balance of around \$500, the interest you pay on that \$500 is likely to be 18% APR or higher. That's like having a loan at 18% APR or higher. Instead of paying off only your new credit card purchases each month or paying only the minimum amount due each month, consider borrowing enough money to pay off your entire credit card balance. If you shop around, you may be able to find a lender who will make a loan at a lower rate. Then you'll be paying off a loan with a lower interest rate than the continuous APR on your credit card bill.

Motor Vehicle Time Sales Act: This law is similar to the Retail Credit Sales Act, but the differences are very important. And if you aren't aware of them, then you could be paying a lot more than you have to when you buy a car.

If you have a motor vehicle dealer arrange financing for the purchase of a new or used car, truck, motorcycle or other motor vehicles including trailers and mobile homes, the sale falls under the Motor Vehicle Time Sales Act. Like purchases of other consumer goods under the Retail Credit Sales Act, the collateral is usually the car, balloon payments are legal but not common, and pre-payment penalties may apply.

It's especially important to note the APR when considering having a motor vehicle dealer arrange financing. You do not have to finance your motor vehicle through the dealer. Such financing may be convenient but very expensive as the dealer may make a profit off the financing as well as the sale. Compare costs and remember: You can choose to take out a loan. You may not always be able to get a lower rate of interest if you borrow the money instead of relying on dealer financing, but it pays to try with a purchase of that size.

2. Where to Get Credit

As explained above, the type of credit you select - loans, time sales or credit cards, may make a difference in what you'll pay for that credit. Just as important is where you get credit. It pays to compare costs and services. You can begin your search by considering the services offered by each of the following sources...

Banks offer a wide range of consumer credit including small loans with or without collateral, loans and other financing for major purchases such as automobiles, and home improvement loans. Most also offer bank credit cards which are widely accepted by stores, and which can be used for cash advances at many banks. Many banks also offer the convenience of "overdraft" checking.

Credit Unions offer consumer loans "for any worthwhile purpose" to members only. Credit unions are usually conveniently located at or near the borrower's place of employment. Credit unions also take deposits and pay interest and may offer credit cards or overdraft checking.

Consumer Finance Companies offer small loans and financing for all purposes to the general public. Such companies are conveniently located and most of them take telephone applications. Most finance companies do not offer credit cards or overdraft checking.

Insurance Companies commonly offer loans to holders of their whole life (not term) insurance policies. The loans are frequently limited to the cash value of the policy held by the borrower and must be applied for through the insurance agent or the company's home office.

Savings and Loan Associations have recently become much more like banks, and so, in addition to the traditional long-term home mortgage loans, often make loans frequently for home improvements, automobiles and educational purposes. Savings and loans take deposits and may offer credit cards and overdraft checking but generally don't actively seek to make relatively small loans.

Merchants are not lenders, as such, but commonly offer financing services. Most merchants will sell "on time", arrange financing for the buyer, or offer credit through the use of their store's credit card.

It is misleading to make generalizations about which of the above sources will offer you the best deal on credit. Not all lenders always charge the maximum rates. The key to avoiding having to pay more than you need to for credit is to take the time to check with more than one type of credit source.

Many borrowers talk with a number of banks, for example, and hearing that they charge about the same rates, think that the cost of borrowing is the same everywhere. **Wrong.** Rates, as well as