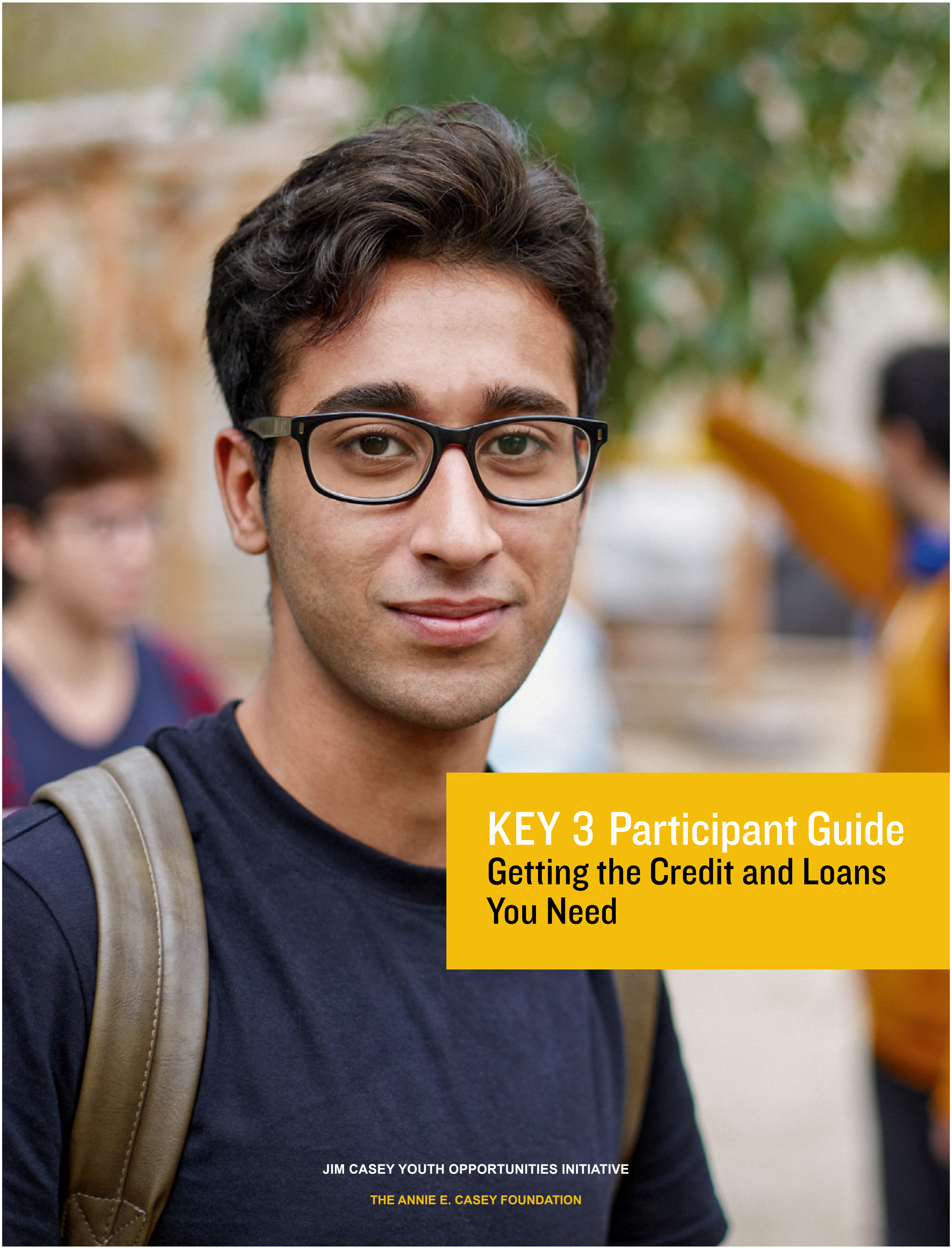


KEY 3 Participant Guide
Getting the Credit and Loans You Need

JIM CASEY YOUTH OPPORTUNITIES INITIATIVE

THE ANNIE E. CASEY FOUNDATION

KEY 3
Getting the Credit and Loans You Need

"Getting the Credit and Loans You Need" is the third key in *Keys to Your Financial Future*, a financial capability curriculum for young people. This key covers the details of borrowing money, including how credit decisions are made, the different kinds of credit available, how credit works, prioritizing debt payments, what it takes to pay off credit cards, comparison shopping for credit and loans and how some loans

What You'll Find in This Key

What You're Going to Know or Be Able to Do

By the end of this key, you'll know or be able to do the following:

- ☐ **EXPLAIN** the difference between installment and revolving credit and how they both work.
- ☐ **EXPLAIN** how interest works when you owe money — the relationship between amount borrowed, rate of interest and the time the money is borrowed.
- ☐ **DIFFERENTIATE** secured and unsecured credit and explain the reasons why it matters.
- ☐ **PRIORITIZE** debt payments.
- ☐ **DEFINE** basic terms associated with applying for and understanding credit.
- ☐ **READ** a credit card statement.
- ☐ **COMPARE** credit and loan offers.
- ☐ **KNOW** where to go in your community to get help with applying for and understanding credit and loan offers.
- ☐ **UNDERSTAND** the life cycle of debt and rights in debt collection.

KEY Concepts

CREDIT

Credit is the ability to borrow money. You commit or obligate future income to buy items on credit today.

WHEN TO USE CREDIT

When *should* you use credit? If you listen to some financial experts, they will say avoid the use of credit — stay out of debt! But sometimes this is not practical. The best times to use credit are when investing in assets that are likely to increase in value — your training or education, a home or even a well-planned business.

Generally, avoid the use of credit for short-term purchases *especially if they will create a long-term debt obligation*. This commonly happens when payday loans, rent-to-own arrangements or credit cards are used to buy things. For furniture, clothing, appliances and dinner with friends, use your income or create a small stash of savings to pay for these items.

CREDIT vs. DEBT

Credit is the ability to borrow money. It can be a productive asset. When you use credit, you have debt. Debt is when you owe someone or a business money. Debt is a liability.

BORROWING MONEY — CREDIT AND LOANS

Credit is the ability to borrow money. Credit allows you to do the following:

+ **Buy something now and pay for it later.**
+ **Avoid financial crises** — low-priced credit may help you deal with emergencies.
+ **Get a job** — education or training may help you get a good job, and student loans may help you get that education.
+ **Buy an automobile.**
+ **Start a business** — a loan for a key piece of equipment or inventory may lead to a successful business.
+ **Own a home** — most people use a mortgage (a loan for a home) to finance their own home.
+ **Get other assets.**
+ **Achieve your goals and realize your vision.**

When you buy something with credit you commit or obligate future income. Obligating future income means you are giving up income you haven't earned yet to buy something today.

Debt is the result of using credit. It's when you owe money to a person or a business. Debt is a **liability**.

Credit is a powerful tool. But as with all tools, knowing how to use them right is the key to success. A person with no training using a chain saw could create a bad situation. Likewise, a person with no training using credit can create a bad situation for themselves and potentially others. Understanding credit, how to get it and how to use it is a key financial capability skill.

WHO PROVIDES CREDIT?

People or businesses that provide credit are called **creditors** or **lenders**. They make money when they lend money.

What creditors or lenders can you list?

HOW ARE CREDIT DECISIONS MADE?

KEY ACTIVITY

What Would You Want to Know if You Were Giving Someone a Loan?

Just like you, people and businesses that lend money want to know about you — before they lend you the money. They want to know whether you **can** and **are likely** to pay them back. They look at four C's:

Capacity	Collateral
Do you have the financial ability to pay back the loan?	Do you have an asset (such as a car or a home) that can be pledged against the loan?
Capital	**Character**
Do you have other assets that can be used or sold to cover the loan?	Are you likely to pay back the loan as agreed?

Different lenders or creditors emphasize different C's in their decision making. For banks or credit unions issuing credit cards, character — your credit scores and credit reports — will be the most important criteria. For pawn shops or vehicle title lenders, collateral will be the most important criteria. For mortgage lenders, all four C's will be important. Where do lenders get this information?

Capacity	Collateral
From your credit application and verification of your income.	Collateral is most commonly the item you buy using the loan.
Capital	**Character**
From your credit application. This will not be examined for credit cards and most auto loans. This is most important in qualifying for a business loan or mortgage (a loan to buy a home).	Your credit history — your credit reports and scores.

THE DIFFERENT TYPES OF CREDIT

There are basically two different kinds of credit:

Installment loans — With an ***installment loan***, you are approved for a specific loan amount taken out for a specific period. The amount you owe each month is calculated when you take out the loan.

What are examples of installment loans?

Revolving credit — With ***revolving credit***, you are approved for a credit limit. You can borrow any amount up to the credit limit. What you pay back each month varies depending on how much you have borrowed during the month.

What are examples of revolving credit?

Credit can also be ***secured*** or ***unsecured***. A secured loan means there is another asset pledged against the loan. If you do not pay the loan as outlined in the terms, the lender can take back the pledged asset. This pledged asset is called collateral.

For a car loan, the car you are buying is the collateral. This means that if you do not pay the loan as agreed, the lender can take back the car. It's often called repossession or repo. With a secured credit card, a deposit held in a certificate of deposit in the issuing bank may be the collateral. This means that if you do not pay your credit card bill as agreed, the bank can take the money held in the certificate of deposit. The bank will probably close your credit card account, too. With a pawn shop loan, the item you have pawned is the collateral.

Unsecured means there is no asset pledged against the loan. Student loans, credit cards and other signature loans are examples of unsecured loans.

KEY Concept

SECURED LOANS OR CREDIT

When a loan or credit is secured, it means you have something of value to back it up. This is often called pledging an asset. Collateral is the name for the asset you pledge.

If you don't pay the loan as agreed in your loan agreement or credit contract, the lender may be able to take the collateral. With cars, the process of taking the collateral is called repossession. With a home purchased using a mortgage (home loan), the process is called foreclosure.

Often, the thing you wanted to get with credit in the first place becomes the pledged asset or collateral.

Loan for:	Collateral or Pledged Asset:
Auto	Your car
Home	Your house
Secured credit card	Deposit in bank (your money)

How Credit Works

When you use credit, you are borrowing money. The money you borrow is called **principal**.

Lenders and creditors lend money to make money. You must pay the lender or creditor a price to borrow the money. **The price you pay is *interest***. Interest is often quoted as the percentage of the loan that you pay each month you are borrowing the principal. Most lenders and creditors charge fees, too.

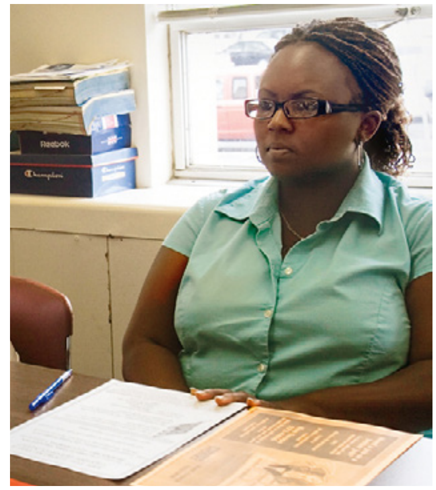
Because interest rates and fees vary from lender to lender, they must also calculate and explain the interest and fees as an ***annual percentage rate* (APR)**. The APR lets you compare credit offers. The APR does not include fees you may be charged if you are late with your payment — the APR only includes fees that apply to everyone taking out that loan.

Interest rates can be ***fixed*** or ***variable***. Fixed means the interest rate will stay the same. Variable means it may change. There are many reasons the rate can vary.

The ***terms of the loan include*** the interest rate, kind of interest rate (fixed or variable), the reason a variable rate may change, when and where payments are due and fees as well as other information about the loan. Sometimes these are called the terms and conditions of the loan.

The ***loan term*** also means how long the loan may last. The length of a loan may be two weeks, one year or 30 years, for example.

When You Owe Money



How much you pay for credit or a loan is based on the following:

- **The amount you borrow.**
- **The interest rate or APR.**
- **The term of the loan — how long you borrow the money.**

A change in any of these three factors will alter your monthly payment and the total interest you pay.

Here is an example. If you borrow **$6,000 for a car** and pay **4 percent interest** for three years, you will pay:

- $177.14 every month; and
- $274.62 in interest.

	Change the Interest Rate to 6 Percent	Change the Amount Borrowed to $8,000	Change the Term of the Loan to Five Years
Monthly payment	$182.53	$236.19	$110.50

KEY RIGHT Truth in Lending Act

The Truth in Lending Act (TILA) is a federal law to ensure you are treated fairly in the lending marketplace. TILA requires that borrowers receive written disclosures about important terms of credit BEFORE they are legally bound to pay the loan.

These important terms include:

- the APR;
- finance charge — cost of credit expressed as a dollar amount;
- amount financed — the dollar amount you are borrowing; and
- total of payments — the sum of all the payments that you will have made at the end of the loan.

TILA disclosures will also include other important terms such as the number of payments, the monthly payment, late fees and whether you can prepay your loan without a penalty.

In addition, TILA includes laws about how credit card issuers figure out the amount you owe and provides you with the right to dispute billing errors, among many other protections.

How You Repay: Installment Loan vs. Revolving Credit

How you pay back the loan depends on the kind of loan and the terms of the loan. Payments for installment loans are calculated over the entire length of the loan. You pay the same amount every month. With each payment, some of it covers interest and some of it goes to pay off the principal — the amount you borrowed. This is called ***amortization*** of the loan.

Student loan, car loan, small business loan and home loan (mortgage) payments are calculated like this.

Revolving credit loans are different. The amount you pay each month varies based on the money you have borrowed. Credit cards are the most common example. Banks use different methods to calculate payments.

KEY Concept

UNDERSTANDING VARIABLE INTEREST RATES

If a credit card or loan has a variable interest rate, the interest rate will change as market interest rates change. Commonly, variable rates are based on the prime rate. Prime rate is the interest rate banks charge for their best customers. The "best customers" are generally large corporations. It's the lowest rate at which money can be commercially borrowed.

Here is an example of a variable rate credit card: "We add 11 percent to prime rate for purchases and balance transfers." If the prime rate were 5 percent, the APR of this credit card would be 16 percent.

Variable rate credit cards and loans often start with an interest rate below those with fixed rates. This makes them attractive in the short term for most people. There is a risk, however, that the rates could increase.

Because the rates vary, the payments change. This makes budgeting for a variable rate loan or credit card payment more difficult.

KEY ACTIVITY

Installment Loan vs. Revolving Credit

Suraj and Darius both needed to borrow $1,000 to pay for books and fees. The cost of these items were over the amounts they received for college from Pell Grants and Education and Training Vouchers as well as scholarships. Darius decided to apply for a credit-building loan at a community bank to get the money. He borrowed $1,000 at 10 percent for 12 months. Suraj got a credit card. It had an introductory rate of 10 percent, with the rate increasing to 13.99 percent plus prime after 12 months.

Installment Loan — Darius's Loan

	Month 1	Month 2	Month 3	Month 4	Month 5	Month 6
Balance	$1,000.00	$920.42	$840.17	$759.26	$677.67	$595.40
Payment	$87.92	$87.92	$87.92	$87.92	$87.92	$87.92
Interest paid	$8.33	$7.67	$7.00	$6.33	$5.65	$4.96
Ending balance	$920.42	$840.17	$759.26	$677.67	$595.40	$512.45

	Month 7	Month 8	Month 9	Month 10	Month 11	Month 12	TOTALS
Balance	$512.45	$428.80	$344.46	$259.41	$173.66	$87.19	
Payment	$87.92	$87.92	$87.92	$87.92	$87.92	$87.19	$1,054.99
Interest paid	$4.27	$3.57	$2.87	$2.16	$1.45	$0.73	$54.99
Ending balance	$428.80	$344.46	$259.41	$173.66	$87.19	0	0

Revolving Credit Loan — Suraj's Loan

	Month 1	Month 2	Month 3	Month 4	Month 5	Month 6
Balance	$1,000.00	$958.33	$918.40	$880.14	$843.46	$808.32
Payment	$50.00	$47.92	$45.92	$44.01	$42.17	$40.42
Interest paid	$8.33	$7.99	$7.65	$7.33	$7.03	$6.74
Ending balance	$958.33	$918.40	$880.14	$843.46	$808.32	$774.64

	Month 7	Month 8	Month 9	Month 10	Month 11	Month 12	TOTALS
Balance	$774.64	$742.36	$711.43	$681.79	$653.38	$626.16	
Payment	$38.73	$37.12	$35.57	$34.09	$32.67	$31.31	$479.93
Interest paid	$6.46	$6.19	$5.93	$5.68	$5.44	$5.22	$79.99
Ending balance	$742.36	$711.43	$681.79	$653.38	$626.16	$600.07	$600.07

How much is Suraj's monthly payment vs. Darius's?

How much total interest does Darius pay vs. Suraj?

What are the balances left on Darius's and Suraj's loans?

Which loan seems like a better deal? Why?

Which kind of loan seems like it would be easier to manage in your budget? Why?

Which Debt to Pay First?

When you take on debt, you are required to pay it back. However, you may run short on money from time to time and not be able to make all your debt payments. How do you prioritize them? Consider consequences of not paying debts.

With most credit or loan payments, if you are late, you can expect:

+ a negative entry on your credit reports;
+ a possible drop in your credit scores;
+ the consequences that come with negative information on credit reports and drops in credit scores — harder to qualify for and/or may pay more for credit or services;
+ late fees; and
+ possibly higher interest rates.

If you have multiple late or missed payments, stop paying on loans or go into default, you risk:

+ collections;
+ lawsuits from a creditor;
+ garnishment (a portion of your paycheck or money from an account is taken to pay what you owe, which requires a court order);
+ loss of driver's license; and
+ reincarceration for nonpayment of some criminal justice debt.

When it comes to secured loans, you risk the loss of the item you used to secure the loan. In some cases, this is called **repossession**.

KEY RIGHT

Administrative Wage Garnishment

If you do not pay the federal or state government money you owe, you may experience administrative wage garnishment. With administrative wage garnishment, there is no court hearing. If you owe money on federal student loans or for child support, for example, your employer may get an order to withhold part of your paycheck. This is then sent to the federal or state agency you owe money to. This means less money in your paycheck.

You will receive written notice 30 days before administrative wage garnishment begins. You can enter into a repayment agreement with the agency to avoid the garnishment.

The maximum that can be withheld through administrative wage garnishment is 15 percent of your income after federal and state deductions have

TYPE OF LOAN	YOU RISK LOSING
Secured credit card	The money you placed in deposit to secure the credit card
Auto loan	Your car
Mortgage (loan for a home)	Your home
Pawnshop loan	The item you pawned
Vehicle title loan	The vehicle named in the title you used to secure the loan
Student loan	Your good credit history and part of your paycheck and possibly all your savings to garnishment

Sometimes, one late payment may trigger the loss of your item. Sometimes, it may take several late payments. This depends on the contract you sign when you get the credit or loan.

KEY ACTIVITY

Prioritizing Debt Payments

Ming's Story

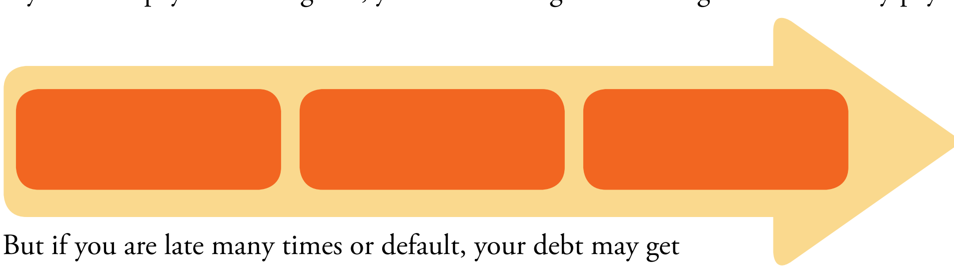
Ming uses her car to get to and from work and classes at the community college. She also helps transport her siblings to and from some of their afterschool activities. She has an automobile loan, two credit card debts and a medical debt she pays monthly. She missed work due to illness so she had a smaller paycheck. She also had some unexpected expenses and found she cannot afford all her debt payments.

How should Ming prioritize her debts?

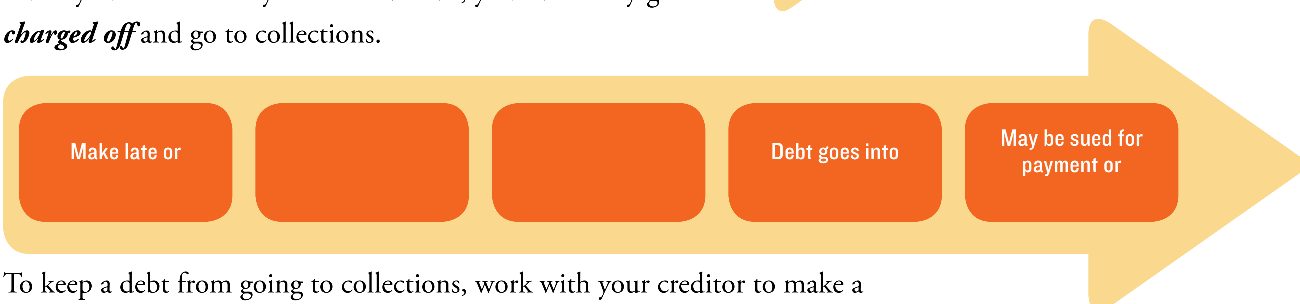
THE LIFE CYCLE OF DEBT

When you use credit or get a loan, you have debt. You may also have debt resulting from a bill you did not or could not pay — medical debt, debt to a cell phone provider, debt to a state agency (child support) or debt to a bank or credit union, for example.

If you make payments as agreed, you will be "in good standing" and eventually pay off the debt.



But if you are late many times or default, your debt may get ***charged off*** and go to collections.



To keep a debt from going to collections, work with your creditor to make a payment arrangement you can afford. Get the new agreement in writing.

KEY RIGHT

Fair Debt Collection Practices Act

The Fair Debt Collection Practices Act (FDCPA) says what third-party debt collectors can and cannot do. This law does not apply to businesses trying to collect their own debts.*

The law states that debt collectors may not harass, oppress or abuse you or any other people they contact. Examples of harassment include:

- making repeated phone calls that are intended to annoy, abuse or harass you or any person answering the phone;
- using obscene or profane language;
- threatening violence or harm;
- publishing lists of people who refuse to pay their debts (this does not include credit reports); and
- calling you without telling you who they are.

The law also says debt collectors cannot use false, deceptive or misleading practices, including:

- misrepresenting the debt, including the amount owed;
- saying that the person on the phone is an attorney (unless they are an attorney);
- threatening to have you arrested; and
- making threats to do things that cannot legally be done or that the debt collector has no intention of doing.

*Some states extend the FDCPA to original creditors collecting debts. Some do not or have different laws. Check your state attorney general's office or visit www.bbb.org/financial-building-blocks/collection-laws for more information.

KEY RESOURCE

GETTING HELP WITH COLLECTIONS, GARNISHMENT AND LAWSUITS

If your debt has been charged off and it is in collections or you have been notified of a lawsuit or garnishment, get help.

Pro bono attorney network contact:______________________________________

Legal aid contact:____

Nonprofit consumer credit counseling contact: ______________________________

PAYING OFF CREDIT CARDS

Credit cards are convenient. They give you access to money you do not have and let you buy things without having cash; provide you with a record of your spending; and can build your credit if you pay your bills on time and use less than 30 percent of your credit limit. Also, if your credit card is stolen and you report it, the most you could ever be liable for is $50.

But credit cards get people in trouble. People charge things on credit cards believing they will be able to pay them off when the bill comes. But then other priorities win out over paying off the credit card in full. So a ***minimum payment*** is sent in instead.

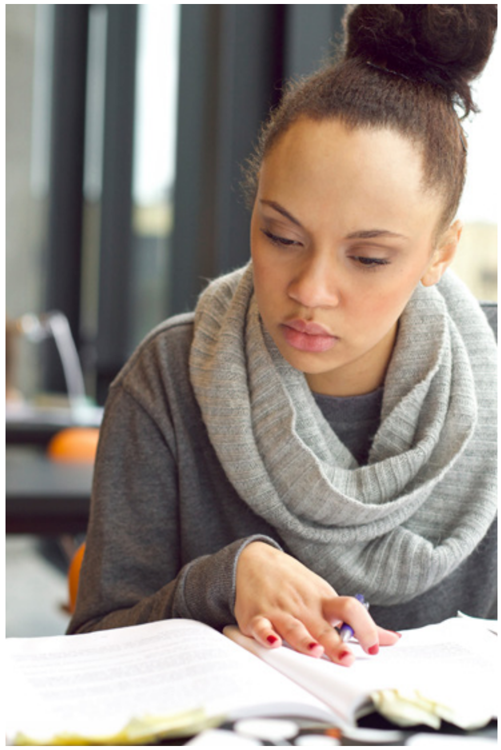
While paying the minimum payment on time keeps you in good standing, this is exactly what credit card issuers want you to do. This is how they make a lot of their money. A better approach, if you are carrying a credit card balance, is to pick a fixed amount above your minimum payment and pay that amount every month. You will:

+ pay off your credit card balance faster; and
+ pay a lot less interest.

KEY Concept

CREDIT CARD ISSUERS

Banks and credit unions are credit card issuers. Visa and Mastercard are the payment processing networks that make credit cards work. Discover and American Express are both credit card issuers and payment processing networks. When you apply for a credit card, it is the credit card issuer that approves or denies your application.



KEY RIGHT

Lost or Stolen Credit Cards

If your credit card or credit card number is lost or stolen and fraudulently used by someone else, the amount you must pay for these charges is limited.

Often, you won't owe anything once you report the card lost or stolen. The most you will owe is $50.

KEY ACTIVITY

Reading a Credit Card Statement

Credit card statements contain a lot of information. Use the questions on page 16 to read this credit card statement.

Summary of Account Activity	
Previous Balance	$535.07
Payments	-$450.00
Other Credits	$0.00
Purchases	+$517.12
Balance Transfers	+$785.00
Cash Advances	+$318.00
Past Due Amount	+$0.00
Fees Charged	**+$69.00**
Interest Charged	**+$11.36**
New Balance	$1,786.00
Credit limit	$2,000.00
Available credit	$214.00
Statement closing date	3/22/2012
Days in billing cycle	30

QUESTIONS?

Call Customer Service	1-XXX-XXX-XXXX
Lost or Stolen Credit Card	1-XXX-XXX-XXXX

Please send billing inquiries and correspondence to:
PO Box XXXX, Anytown, Anystate XXXXX

Payment Information	
New Balance	$1,786.00
Minimum Payment Due	$53.00
Payment Due Date	4/20/2012

Late Payment Warning: If we do not receive your minimum payment by the date listed above, you may have to pay a $35 late fee and your APRs may be increased up to the Penalty APR of 28.99%.

Minimum Payment Warning: If you make only the minimum payment each period, you will pay more interest and it will take you longer to pay off your balance. For example:

If you make no additional charges using this card and each month you pay...	You will pay off the balance shown on this statement in about...	And you will end up paying an estimated total of...
Only the minimum payment	8 years	$2,785
$62	3 years	$2,232 *(Savings = $553)*

If you would like information about credit counseling services, call 1-800-XXX-XXXX.

KEY ACTIVITY

Reading a Credit Card Statement (continued)

Notice of Changes to Your Interest Rate

You have triggered the Penalty APR of 28.99%. This change will impact your account as follows:

Transactions made on or after 4/9/12: As of 5/10/12, the Penalty APR will apply to these transactions. We may keep the APR at this level indefinitely.

Transactions made before 4/9/12: Current rates will continue to apply to these transactions. However, if you become more than 60 days late on your account, the Penalty APR will apply to those transactions as well.

Important Changes to Your Account Terms

The following is a summary of changes that are being made to your account terms. For more detailed information, please refer to the booklet enclosed with this statement.
These changes will impact your account as follows:

Transactions made on or after 4/9/12: As of 5/10/12, any changes to APRs described below will apply to these transactions.

Transactions made before 4/9/12: Current APRs will continue to apply to these transactions.

If you are already being charged a higher Penalty APR for purchases: In this case, any changes to APRs described below will not go into effect at this time. These changes will go into effect when the Penalty APR no longer applies to your account.

Revised Terms, as of 5/10/12

Transactions

Reference Numbers	Trans Date	Post Date	Description of Transaction or Credit	Amount
5884186PS0388W6YZ	2/22	2/23	Store #1	$133.74
854338203FS8OO0Z5	2/25	2/25	Pymt Thank You	$450.00-
564891561545KOSHD	2/25	2/26	Store #2	$247.36
1542202074TWWZV48	2/26	2/26	Cash Advance	$318.00
4545754784KOHUIOS	2/27	3/1	Balance Transfer	$785.00
2564561023184102331	2/28	3/1	Store #3	$34.32
045148714518979874	3/4	3/5	Store #4	$29.45
0547810511898718AF	3/15	3/17	Store #5	$72.25
		FEES		
9525156489SFD4545Q	2/23	2/23	Late Fee	$35.00
84151564SADS8745H	2/27	2/27	Balance Transfer Fee	$23.55
256489156189451516L	2/28	2/28	Cash Advance Fee	$10.90
			TOTAL FEES FOR THIS PERIOD	**$69.45**
		INTEREST CHARGED		
			Interest Charge on Purchases	$6.57
			Interest Charge on Cash Advances	$4.79
			TOTAL INTEREST FOR THIS PERIOD	**$11.36**

KEY ACTIVITY

Reading a Credit Card Statement (continued)

Interest Charge Calculation			
Your Annual Percentage Rate (APR) is an annual interest rate on your account.			
Type of Balance	**Annual Percentage Rate (APR)**	**Balance Subject to Interest Rate**	**Interest Charge**
Purchases	14.99% (v)	$533.32	$6.57
Cash Advances	21.99% (v)	$265.00	$4.79
Balance Transfers	0.00%	$575.67	$0.00
(v) = Variable Rate			

SOURCE: National Credit Union Administration. (n.d.). *Understand your credit card statement.* Retrieved August 1, 2018, from www.mycreditunion.gov/Pages/pocket-cents-understanding-credit-card-statement.aspx

What is the current balance? Where did you find it?

When is the payment due? Where did you find this information?

What is the minimum payment?

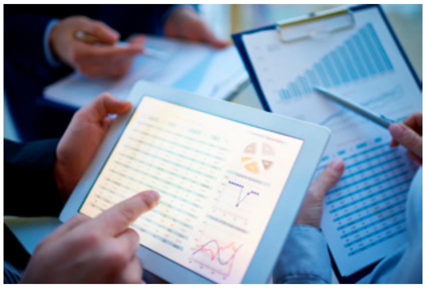
What happens if the payment is late? Where did you find this information?

How long will the balance take to repay if only the minimum payment is made each month assuming no new charges?

How long will the balance take to repay if making a fixed $62 payment each month assuming no new charges?

What is the APR on purchases? Cash advances? Balance transfers?

Describe three different kinds of transactions made during the month. Where did you find them?



COMPARISON SHOPPING FOR CREDIT CARDS AND LOANS

Before getting a credit card or loan, be sure to comparison shop. Comparison shopping is a key financial capability skill.

Key to Your Financial Future: Shopping for Credit Cards and Loans Checklist

Compare the same kind of loan or credit card from different creditors on key terms using this checklist to make sure you get the best deal.

	CREDIT CARD OR LOAN 1	CREDIT CARD OR LOAN 2	CREDIT CARD OR LOAN 3
1. Annual percentage rate (APR)			
2. Fixed or variable rate • If variable, when does the rate change? • By how much?			
3. Introductory rate • When does it change? • What does it change to? (credit cards only)			
4. Finance charge - total cost of the loan over the life of the loan (loans only)			
5. Fees not included in APR			
6. Penalty fees and rate • How much? • When do they kick in?			
7. Credit limit (credit cards only)			
8. Monthly payment amount (loans only)			
9. Prepayment penalties • How much? • When do they kick in? (loans only)			
10. Rewards (credit cards only)			
11. Other important terms or conditions			

There are some credit situations that can cause big problems for young people. Understanding credit situations likely to create problems and financial struggles is a key financial capability skill. In general, plan to avoid these situations.

KEY ACTIVITY

The Trouble With Some Credit Case Studies

Read each scenario and answer the questions that follow.

Jamal Visits a Payday Lender

Jamal was short on money. Living on his own since transitioning out of foster care, he knew where to get resources if he needed them. This month, he knew he would not be able cover his rent the following week with the amount in his checking account. And payday was still two weeks away.

Jamal went to Cash Fast and got a payday loan. In exchange for $500, he provided a $525 check post-dated for three days after the day he would be paid. He was confident he would have the cash to cover this loan in his account.

The following week, he paid his rent on time and in full. The next day, his car tire blew out. He used up all the money in his checking account to replace the tire. When payday came around, he really couldn't afford to hand over $500 to Cash Fast. So he renewed the loan for a fee — another $25.

It took Jamal six months to pay back the loan. He renewed it every two weeks. Each time he renewed the loan, he paid another $25.

How much did he pay to borrow $500 for six months?

Does this loan seem like a good deal?

KEY ACTIVITY

Susan Makes Minimum Payments on Her Credit Card Balance

Susan opened a credit card. She was 21 and had just transitioned from foster care. Working part time and going to school, she was so excited to have this new card with a $2,000 limit and a 21 percent interest rate. Within a month, she had charged $1,800 worth of clothing, furniture and even a plane ticket to visit her aunt in another state. When the bill came, she was surprised. She owed only $36. What a great deal!

For the next 12 months, she paid only the minimum required on the $1,800 she borrowed using her credit card.

	Month 1	Month 2	Month 3	Month 4	Month 5	Month 6
Balance	$1,800.00	$1,795.50	$1,791.01	$1,786.53	$1,782.07	$1,777.61
Payment	$36.00	$35.91	$35.82	$35.73	$35.64	$35.55
Interest paid	$31.50	$31.42	$31.34	$31.26	$31.19	$31.11
Ending balance	$1,795.50	$1,791.01	$1,786.53	$1,782.07	$1,777.61	$1,773.17

	Month 7	Month 8	Month 9	Month 10	Month 11	Month 12	TOTALS
Balance	$1,773.17	$1,768.74	$1,764.31	$1,759.90	$1,755.50	$1,751.11	
Payment	$35.46	$35.37	$35.29	$35.20	$35.11	$35.02	**$426.11**
Interest paid	$31.03	$30.95	$30.88	$30.80	$30.72	$30.64	**$372.85**
Ending balance	$1,768.74	$1,764.31	$1,759.90	$1,755.50	$1,751.11	$1,746.74	

After making her payments for 12 months, how much did she still owe?

How much interest did she pay?

How much principal did she pay off?

Does this credit arrangement seem like a good deal?

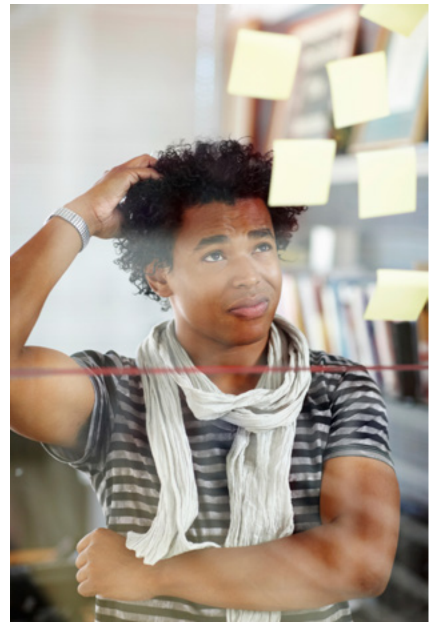
Even though Susan is paying the minimum balance required by the credit card company, she is paying just enough to cover the interest every month. Very little from each payment is going toward the principal.

If she had paid 5 percent instead of 2 percent, it would have taken her 11 years and cost $957 in interest.

If she had paid a fixed amount of $72 per month, it would have taken her two years and nine months to pay off the loan. She would have paid only $588 in interest.

KEY ACTIVITY

Xander Gets Upside Down in His Car Loan



Xander has been on his own for five years. After leaving foster care, he got a medical assistant associate degree. He has a great job as a medical assistant. The car he has had for the past four years died. He wants to get a new, reliable car. He doesn't have a down payment, but with dealer financing he can get a new SUV for below market price. The new SUV's value is $19,500. His price is $19,000. He borrows the full amount. His equity on the day he buys the car is:

$19,500 (asset value) - $19,000 (liability or loan amount)
= $500 (equity)

After one year, the SUV will be worth about $15,015. His loan balance would be $16,000. After one year of owning the car, his equity would be:

$15,015 (asset value) - $16,000 (liability or loan amount)
= -$985 (equity)‡

Even if he sold his vehicle for the full asset value (which is not always possible), he would have to come up with nearly $1,000 to pay off the loan.

Does this loan seem like a good deal?

Dakota Cosigns for a Friend

Dakota's friend has asked him to cosign for an auto loan. Dakota has worked hard to improve his credit. While in foster care, a family member used his credit fraudulently. He has finally built his credit and believes his scores on average are over 700. His friend needs a car to get to and from work. His friend also has two children and having a reliable car would really help him out.

After five months, Dakota finds out his friend has been late with every payment and has not made the most recent payment. He checks his credit reports and sees these negative entries on his credit reports. The bank has also sent Dakota a letter demanding the missed payment.

What should Dakota do?

Does this credit arrangement seem like a good deal?

‡ The depreciation rate used was determined using the Money-zine.com car depreciation calculator. The average depreciation in one year is $5,405.

KEY ACTIVITY

Danielle Buys Her Furniture Rent to Own

Danielle has saved enough money to get her own studio apartment. After years of sharing rooms and apartments, she is happy to be on her own. But she doesn't have any furniture. After paying the first month's rent and a security deposit, she has little to spend on things to put into the apartment. She visited secondhand shops at the encouragement of some friends. But then her partner told her about rent-to-own stores. She can get a complete living room set, a queen bed and mattress with a matching night stand and television for $89.96/week.

	COST TO BUY	WEEKLY PRICE	TOTAL PAYMENTS	NUMBER OF PAYMENTS
Living room set	$1,637	$29.99	$2,729	91
Television	$859	$19.99	$1,439	72
Queen bedroom set and mattress	$1,372	$39.98	$2,298	58
TOTALS	$3,868	$89.96	$6,466	

What are her weekly payments for this furniture?

If she saved money and purchased the same furniture, how much would she pay?

How much will she pay in total for this furniture?

Does this credit arrangement seem like a good deal?

WRAP UP:
Getting the Credit and Loans You Need

Congratulations on finishing this section of ***Keys to Your Financial Future.***

Let's check what you learned:

1. Credit is owing someone else money.

   ☐ True ☐ False

2. A creditor is someone who borrows money from an individual or business.

   ☐ True ☐ False

3. Capacity answers the question: Can you pay back the loan?

   ☐ True ☐ False

4. Which of the following features describe an installment loan? *(select all that apply)*

   ☐ a. You borrow a specific amount

   ☐ b. You borrow for a set amount of time.

   ☐ c. The amount you pay changes every month.

   ☐ d. Your monthly payment is the same unless you have a variable rate.

   ☐ e. You have a credit limit and can use up to that amount.

5. A secured loan has collateral or an asset attached to it. If you don't pay the loan, you can lose the collateral or asset.

   ☐ True ☐ False

6. Which of the following are consequences of late payments or default on a loan? *(select all that apply)*

   ☐ a. Negative entries on your credit reports

   ☐ b. Garnishment

   ☐ c. Lawsuits from creditors

   ☐ d. Unable to qualify for other loans

   ☐ e. There are no consequences

7. Cosigning a loan does not mean you are responsible for the loan. It's okay if you really like the person you are cosigning for.

   ☐ True ☐ False

Key Information From This Section

- ☐ **CREDIT IS THE ABILITY TO BORROW MONEY.** Credit can allow you to buy things now and pay for them later, including education, a car, a business or other assets. However, credit obligates or commits future income you have not yet earned.

- ☐ **PEOPLE WHO LEND MONEY ARE CALLED CREDITORS OR LENDERS.** They lend money to make money. They make money on interest and fees.

- ☐ **UNDERSTANDING HOW CREDIT DECISIONS ARE MADE CAN PREPARE YOU FOR APPLYING FOR A LOAN.** Remember, different lenders emphasize different criteria, but they'll generally review your capacity, character, collateral and capital.

- ☐ **WITH INSTALLMENT LOANS, YOU BORROW A SPECIFIC AMOUNT FOR A SPECIFIC PERIOD.** Your monthly payment will be the same. With revolving credit, you are approved up to a credit limit. Your monthly payment is based on what you borrow.

- ☐ **THERE ARE DIFFERENT CONSEQUENCES FOR NOT PAYING LOANS OR GOING INTO DEFAULT.** Understand the consequences so you can prioritize payments should you be short on funds to cover all your debt obligations.

- ☐ **LEARN ABOUT CREDIT SITUATIONS THAT CAN GET YOU INTO TROUBLE AND TRY TO AVOID THEM.** Remember, if you cosign for a loan, you are just as responsible for the loan as the person you are cosigning for, but you don't get the benefit of the loan.

ABOUT THE ANNIE E. CASEY FOUNDATION

The Annie E. Casey Foundation is a private philanthropy that creates a brighter future for the nation's children by developing solutions to strengthen families, build paths to economic opportunity and transform struggling communities into safer and healthier places to live, work and grow.

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ABOUT THE JIM CASEY YOUTH OPPORTUNITIES INITIATIVE

A unit of the Casey Foundation, the Jim Casey Youth Opportunities Initiative® works to improve outcomes for all young people in the United States ages 14 to 26 who have spent at least one day in foster care after their 14th birthday — a population of nearly 1 million. Working with 17 sites across the country, the Jim Casey Initiative influences policy and practices to improve outcomes for teenagers and young adults who have experienced foster care as they transition to adulthood.