

# ACTIVITY 1

## CREDIT CARD FACT SHEET

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The word credit originates from the Latin word *creditus* meaning *entrusted*. Credit means that someone will lend you money and give you time to pay it back, usually with *interest* (money paid for the use or borrowing of money). When purchasing goods and services with your credit card, you are getting a loan from the issuer of the credit card. It is not used in place of cash. Consumers use credit cards to buy things they want or need.

A credit card is a plastic card identifying the holder as a participant in a credit plan of a lender. Many stores and companies such as oil companies issue credit cards for use only at their place of business. Banks and other financial institutions issue credit cards, such as Visa or MasterCard, that can be used at any establishment that accepts credit cards.

Cardholders can purchase services, merchandise, or obtain cash advances (loans). Most credit cards are used as open-ended credit accounts or charge accounts, originally designed for the short-run money needs of consumers. These accounts have a credit limit (*the maximum amount you may charge*) and a flexible repayment schedule. The cardholder who pays the entire balance due within the grace period (*a period of time after the due date not subject to late charges*) avoids interest or finance charges. A *late charge* is a payment for not paying the balance owed before the due date. If a card offers a grace period, federal law requires a bill be sent to the cardholder at least 14 days before payment is due. A cardholder can repay any amount equal to or greater than the purchase price to eliminate interest charges.

A wise consumer will pay off credit card bills promptly. If you don't pay it off, you are taking out a loan and it can be very expensive. Would I take out a loan for dinner tonight? Avoid the minimum payment trap. People who pay the mini-

um think they are handling their finances, but it could take them a long time to pay off the bill. Many cardholders maintain balances and the average customer takes more than 15 months to pay for the charges.<sup>1</sup> When a credit card is used responsibly, the cardholder can build a good credit history. If not, it can ruin a person's credit record. A bad credit record is hard to fix and takes many years to correct.

Sixty (60%) percent of all families make credit card purchases. Worldwide, more than 90 million MasterCard, 41 million Discover, and 142 million Visa cards are issued.<sup>2</sup> Credit cards are issued by local and national businesses as well as banks. With the passage of the Fair Credit and Charge Card Disclosure Act in 1988, credit card issuers must inform consumers before they sign up about: (1) annual percentage rate (APR), (2) how monthly fees are calculated, (3) cost of all fees such as membership, transaction, cash advance and others, and (4) grace period.

Not all plastic cards are credit cards. The use of bank debit cards and smart cards is increasing. The debit card automatically deducts money from checking accounts. The smart card stores valuable information about the consumer on computer chips instead of magnetic strips. This allows businesses access to better information about the consumer so that they can provide personalized service. Some consumers are concerned about privacy issues associated with smart cards and credit cards knowing so much about them.

Credit cards help consumers satisfy their wants and needs, but how does the credit card affect the issuers of cards and businesses that accept purchases made by credit cards? Purchases made by credit cards issued by banks charge merchants a transaction fee. This fee is a percentage of the price of any good or service purchased with a

<sup>1</sup> E. Thomas Garman. (1993). *Consumer Economic Issues in America*. Houston: DAME Publications.

<sup>2</sup> Ibid.

## LESSON TEN

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### ACTIVITY 1 (CONTINUED)

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**Name** \_\_\_\_\_

credit card. Credit card issuers charge interest on the unpaid balances not paid during the grace period and they may collect an annual fee from cardholders. American Express and other companies issue gold or platinum status credit cards. These cards may have higher annual fees, but include extras such as travel insurance and other benefits.

The prime target for credit companies is the “baby boom” generation. Families headed by younger persons use consumer credit more than families headed by older persons. Higher income groups use credit more than lower income groups. Some companies target a younger market and issue cards to college students. According to a survey by MasterCard International, 32 percent of high school students and 62 percent of college students had at least one credit card in 1993.