Borrowing Basics
FDIC Money Smart for Young Adults

PNC is proud to work with the FDIC to offer their Money Smart program to our customers, to support lifelong learning in Financial Education.

Building: Knowledge, Security, Confidence
Objectives

- Define credit
- Explain why credit is important
- Identify three types of loans
- Identify the costs associated with getting a loan
- Tell how you are protected against discrimination in the lending process
- Identify the factors lenders use to make loan decisions
- Explain why it is important to be wary of rent-to-own and refund anticipation services
Hey Ramón, check out this new cell phone I bought. It has everything!

It was a really great deal. I signed some papers and only have to pay $30 a month!

Umm, do you know how long you have to keep it? And how can you pay for it—you always borrow money from me?

It's a $90 phone, so I'm sure I only have to pay for 3 months. And don't worry, bro...

...I got a "student credit card!"
Credit

• What is credit?
  – It is the ability to borrow money

• Having good credit makes it easier to borrow money in the future
Why is Credit Important?

• Credit:
  – Can be useful in times of emergencies
  – Is more convenient than carrying large amounts of cash
  – Allows you to make a large purchase (e.g., a car or house) and pay for it over time
  – Can affect your ability to obtain employment, housing, and insurance based on how you manage it
Collateral

• Collateral is:
  – Security you provide the lender
  – An asset (e.g., a car, home, or savings account)

• A guarantee is:
  – A form of collateral
  – For example: having a cosigner on a loan
Types of Loans

- **Credit cards**
  - Give you the ongoing ability to borrow money

- **Consumer installment loans**
  - Allow you to pay the same amount each month in installments for a set period of time
Activity 1: Installment Loan versus Rent-to-Own Services

Complete Activity 1 in your Participant Guide

– Break into 2 groups
– Read through your section of material
– List and describe 5 reasons to choose your payment method
Home Loans

• Home purchase loans
• Home refinance loans
• Home equity loans

Value of home $250,000.00
Minus debt -$200,000.00
Equity $50,000.00
Activity 2: Types of Loans

Complete Activity 2 in your Participant Guide

– Read the description of the purchase to be made
– Fill in the blank with the most appropriate loan type(s) for that purchase
Cost of Credit

- **Fees**
  - Charge for activities (e.g., reviewing your loan application and servicing the account)

- **Interest**
  - Charge for using financial institutions money
    - Fixed rates
    - Variable rates
Truth in Lending Disclosures

• The Federal Truth in Lending Act:
  – Requires banks to disclose charges so you can compare the actual cost of borrowing

• Lenders must disclose:
  – The amount financed
  – Annual Percentage Rate (APR)
  – Finance charges
  – Total payment
Activity 3: Borrowing Money Responsibly

Complete Activity 3 in your Participant Guide
- Answer each question
- Be prepared to explain your answers
Equal Credit Opportunity Act

• This act:
  – Prohibits discrimination during the loan application process
  – Restricts lenders from requesting certain information
  – Requires the lender to notify you in writing, within 30 days, if you have been approved or denied the loan
The Four Cs

- Capacity
- Collateral
- Character
- Capital
Capacity

• Refers to your ability to meet payments:
  – How long have you been working at your job?
  – How much money do you make each month?
  – What are your monthly expenses?
• Refers to the value of your assets and net worth:
  – How much money do you have in your checking and savings accounts?
  – Do you have investments (e.g., stocks, bonds) or other assets (e.g., a car)?
Character

• Refers to how you paid your bills or debts in the past
  – Have you had credit in the past?
  – How many credit accounts do you have?
  – Have you ever filed for bankruptcy, had property repossessed, or made late payments?
Free Annual Credit Report

Visit: www.annualcreditreport.com
Call: 1-877-322-8228
Mail:
Annual Credit Report Request Service
P. O. Box 105281
Atlanta, GA 30348-5281
Collateral

- Refers to property/ assets used to secure the loan
  - Do you have assets to secure the loan beyond your capacity to pay it off?
Barriers to Borrowing Money

- Making late payments
- Filing for bankruptcy
- Having property repossessed or foreclosed on because you cannot make the payments
- Having a court order requiring you to pay money to the lender
Legal Terms for Debt Actions

- Attachment
- Bankruptcy
- Collection account
- Foreclosure
- Garnishment
- Judgment
- Lien
- Repossession
Activity 4: Borrowing Barriers

Complete Activity 4 in your Participant Guide

- Reach each scenario
- Indicate which of the Four Cs are affected by each of the barriers to borrowing money
Activity 5: Loan Applications

Complete Activity 5 in your Participant Guide

– Review each section of the Uniform Residential Loan Application
– Match the required information with the appropriate C:
  – Capital, Collateral, Character, and/or Capacity
Credit Report

• A credit report tells lenders:
  – Who you are
  – How much debt you have
  – Whether you have made payments on time
  – Whether there is negative information about you in public records
Activity 6: John Q. Consumer

Complete Activity 6 in your Participant Guide

- Review the sample credit report
- Use the report to answer the questions about John’s credit history
Catch Phrases of Abusive Lenders

“125 percent of your home/car’s value”

“Incredibly low monthly payment”

“No upfront fees”

“Even if you have a bad credit history…”

“It is free and you have nothing to lose”

“Act now, this is a limited-time offer”
Predatory Lending Practices

• To guard against predatory lending:
  – Deal with reputable loan providers
  – Shop around to obtain the best terms
  – Read and understand all terms and conditions
  – Ensure you can afford and make payments according to the loan terms
True Cost of Alternative Financial Services

- Rent-to-own services
- Payday loan services
- Refund anticipation services
Rent-to-Own Services

• Allow you to use the item while you make monthly or weekly payments
  – The store owns the item until you make your final payment.

• Are generally more expensive than a consumer installment loans
Payday Loans

- Short-term loans (usually up to 2 weeks) that can be costly

<table>
<thead>
<tr>
<th>Loan Term</th>
<th>Fee</th>
<th>You write a check for:</th>
</tr>
</thead>
<tbody>
<tr>
<td>2 weeks</td>
<td>$30</td>
<td>$230</td>
</tr>
</tbody>
</table>
Refund Anticipation Loans

• Short-term loans secured by your expected income tax refund

• Consider electronically filing (e-file) your tax return and request direct deposit instead
Module Summary

HOW'S THAT NEW CELL PHONE?

I SHOULDN'T HAVE BOUGHT IT. IT WAS REALLY DUMB.
HOW COME?

THE PHONE CALLS ARE REALLY EXPENSIVE, AND I SIGNED A YEAR-LONG CONTRACT THAT I CAN'T GET OUT OF WITHOUT PAYING LOTS OF MONEY.

I JUST GOT TOO EXCITED. I SHOULD HAVE BEEN MORE CAREFUL.
Congratulations! You learned about:

• Credit and what “good” credit means
• Types of loans
• The cost of credit and the cost of using non-loan services
• How lenders make credit decisions