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COST OF CREDIT

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When buying on credit, you pay an extra charge called "interest," "time price differential" or "service charge." Although credit lets you use things while paying for them, you may spend more than you can afford.

HOW MUCH CAN YOU AFFORD?

Study your family situation. Are you spending for longtime family happiness and security? Conservative estimates suggest that after home mortgage a family can carry payments of 15 to 20 percent of monthly income after tax deductions. However, families with high housing expenses, several children, large medical expenses or unemployment problems cannot carry even 15 percent.

Figure what you can afford by listing categories of spending and record your expenditures for a period of time. Weigh the amount spent against your income. Is there money left for additional payments? Plan future expenditures based on what you spend now. Allow for unexpected expenses.

Ask yourself these questions when considering the use of credit:

- Is this item worth the added cost?
- Will the item last longer than the payment period?
- Could I save now to pay cash for future items?
- What is the difference between the cash price and the credit price?
- Could I pay less by choosing another form of credit?
- Could I make a larger down payment without upsetting the family spending plan?
- Do I pay off debts as quickly as possible?
- Can I meet this payment plus all other monthly expenses?

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CREDIT CHARGES

Texas laws governing charges for credit changed with passage of the Texas Consumer Credit Code, effective January 1, 1968. Under the new credit code, charges vary with the type and amount of credit and the length of payment schedule. Rates may vary from one institution to another but are subject to the same maximum limits.

Interest charges may not exceed 10 percent per annum except where provided for in the code. However, not all lending institutions charge maximum rates.

REGULATED LOANS

Regulated loans are cash loans up to and including \$2,500. The loan period is limited to 37 months for \$1,500 or less and to 43 months for more than \$1,500.

The following interest rates may be charged:

\$ 0 - 300	\$18 per hundred per year
\$300 - 2,500	\$ 8 per hundred per year

The interest on a \$400 loan for 12 months, payable in monthly installments, would be \$62. It is figured as follows:

$$\begin{aligned} \$ 0 - 300 \text{ at } \$18 \text{ per hundred is } 3 \times \$18 &= \$54 \\ \$100 \text{ at } \$8 \text{ per hundred} &= \$8. \\ \$8 + \$54 &= \$62 \text{ for } \$400. \end{aligned}$$

The dollar cost is \$62. The monthly payment is \$462 divided by 12 = \$38.50. Figure the true annual rate by the constant ratio method as follows:

$$R = \frac{2M \times F}{P(N + 1)}$$

M = Number of payments per year

F = Finance charge

P = Amount financed (principal)

N = Total number of payments

$$R = \frac{2 \times 12 \times 62}{400 \times (12 + 1)} = .349 = 34.9\%$$

ALTERNATE RATES OF INTEREST

On loans of \$100 or less the following amounts are legal and may be charged instead of the \$18 add-on interest charge:

Amount borrowed	Other charges
Any amount to \$29.99	\$1 per \$5 loaned.
Above \$29.99 to \$35	Not over 1/10 of the amount loaned, plus a handling charge not over \$3 per month.
Above \$35 to \$70	Not over 1/10 of amount loaned, plus handling charge not over \$3.50 per month.
Above \$70 to \$100	Not over 1/10 of amount loaned, plus handling charge not over \$4 per month.

Loans may not exceed 1 month for each \$10 loaned up to a maximum of 6 months.

A \$100 loan for 6 months at these rates requires 1/10 of \$100 = \$10 + \$4 per month for 6 months = \$24. \$10 + \$24 = \$34, the dollar cost for using \$100 for 6 months.

Applying the formula, the true annual interest rate is 116%.

$$\frac{2 \times 12 \times 34}{100 \times (6 + 1)} = \frac{816}{700} = 116\%$$

On all loans of \$100 or more, a lender may require a borrower to provide credit life insurance and credit health and accident insurance as additional loan protection. On loans of \$300 or more the lender may require the borrower to insure tangible personal property as security.

INSTALLMENT LOANS

These loans are repayable in consecutive, fairly equal, monthly installments. There is an add-on charge of \$8 per \$100 per annum for the full term of the loan with no limit on the amount loaned or the repayment period.

Credit life and credit health and accident insurance can be required on any installment loan regardless of the loan amount.

SECONDARY MORTGAGE LOANS

The bank, savings and loan association or any lender licensed under the Credit Code may offer

secondary mortgage loans at the add-on interest rate of \$8 per \$100 per annum for the full term of the loan with no limit on the loan amount or term. Any other lender is restricted to the maximum 10 percent per annum interest rate. The lender is entitled to charge appraisal and inspection fees not to exceed \$25 per tract of land, a credit investigation fee not to exceed \$12.50, attorney fees for preparing documents not to exceed \$35 and official filing, recording, construction permit fees, plus title insurance or title examination fees. In addition, the lender can require credit life insurance and credit health and accident insurance.

RETAIL INSTALLMENT SALES

This part of the Code applies to retail installment contracts or retail charge agreements involving sales of consumer goods or services. Each contract or agreement is required to be in writing with all charges and provisions disclosed. The term "time price differential" means the amount paid or payable for purchasing goods or services on credit.

The term "cash sale price" is the cash price of the good or service. "Time sale price" is the total of the cash price and all other charges, including the "time price differential."

The buyer is cautioned not to sign his name before reading the contract or when there are any blank spaces.

The agreement must show the following:

1. cash price including sales tax
2. trade-in
3. cash down payment
4. total down payment (trade-in plus cash down payment)
5. cash balance (cash price minus total down payment)
6. insurance coverages and premiums
7. official fees charged the buyer
8. principal balance (cash balance plus insurance plus official fees)
9. time price differential
10. time balance owed (principal balance plus time price differential)
11. time sale price (time balance owed plus total down payment)

From the "time balance owed," item 10, the number of installments, dates of payment and amounts must be clearly spelled out.

The act provides a maximum legal time price differential rate based on the size of the principal balance as follows:

Any amount up to	
\$500	\$12 per \$100 per annum
From \$500 to	
\$1,000	\$10 per \$100 per annum
Above	
\$1,000	\$ 8 per \$100 per annum

This amount is figured on the principal balance, item 8, from the date of the contract until the due date of the final installment.

A minimum time price differential rate can be charged on any retail installment credit and is established on the initial principal balance as follows:

Any amount up to \$25	minimum \$6
From \$25 to \$75	minimum \$9
Above \$75	minimum \$12

These may be charged regardless of the number of installments or the period of credit provided in the contract.

The contract spells out what can be charged for delinquent payments.

RETAIL CHARGE AGREEMENT

The credit code allows a maximum monthly charge on retail charge agreements (revolving credit). It is 1.5 percent on unpaid balances of \$500 or less (15 cents per \$10 per month) and 1 percent on any unpaid balance in excess of \$500 (10 cents per \$10 per month.)

A minimum time price differential not more than 75 cents per month may be charged for any billing cycle, and reasonable attorney fees and court costs may be added if the buyer defaults.

The charges for revolving charge accounts vary with how the seller computes the time price differential, even though the law sets maximum charges. The unpaid balance may be considered at the end of the present billing cycle, on the unpaid balance of the previous billing cycle or at the beginning of the cycles. It may be figured on the exact amount owed or on the midpoint in units of 10. Whatever the method, it must be used on all accounts.

Each month (not necessarily a calendar month) the buyer is furnished a statement showing these items: the unpaid balance at the beginning and at the end of the month, the dollar amount of each purchase or service, payments or other

credits made during the period, the time price differential for the period and a statement that the buyer can pay any unpaid part or balance at any time.

Be sure you understand the method of applying the time price differential so you can shop for the cheapest form of revolving credit. Some retail charge agreements do not use the minimum charge of 75 cents. If a \$40 balance is left, the charge is figured on the exact amount which would be 60 cents rather than 75 cents.

MOTOR VEHICLE INSTALLMENT SALES

The maximum time price differential charges in motor-vehicle installment sales depend on the "class" into which the vehicle falls. Beginning one month from the contract date, a charge of \$25 may be added or an amount determined as follows:

- Class 1. New cars, \$7.50 per \$100 per annum
- Class 2. New cars of prior models and used cars not over 2 years old, \$10 per \$100 per annum
- Class 3. Used cars 3 and 4 years old, \$12.50 per \$100 per annum.
- Class 4. Used cars over 4 years old, \$15 per \$100 annum; however, a charge of \$18 per \$100 is allowed, if the unpaid principal balance is \$300 or less.

The terms of the motor vehicle installment sales contract are basically the same as those of retail installment-sales agreements.

KNOW WHAT YOU CAN DO

If you use credit, know what the cost will be. Know the types of credit available. Compare and shop for the cheapest rate. Remember that costs may vary with the institution, business and your credit rating. Choose the type credit that fits your ability to pay.

Remember:

- Read the contract. Ask questions when you do not understand.
- Put your copy of the contract or agreement in a safe place.
- Make your payments on time.
- Guard your credit rating.
- Avoid perpetual indebtedness.

The author acknowledges the cooperation of William R. Crocker, Chief Counsel, Office of Consumer Credit Commission, Austin.

ADDITIONAL REFERENCES

State of Texas Credit Code
Office of Regulator Loan Commissioner
P. O. Drawer W. W. Capitol Station
Austin, Texas 78711

Using Our Credit Intelligently
National Foundation for Consumer Credit
1411 K. Street N. W.
Washington, D. C.

Consumer Beware
American Federation of Labor and
Congress of Industrial Organizations
815 Sixteenth Street, N. W.
Washington, D. C. 20006

Fact Booklet Series
Better Business Bureau
Boston, Massachusetts

Shopping For Credit
Council of Consumer Information
15 Gwynn Hall
University of Missouri
Columbia, Missouri 65201

Using Consumer Credit MP-343
Texas Agricultural Extension Service
College Station, Texas 77843