

# What You Need to Know About Payment Cards



FEDERAL RESERVE BANK  
OF PHILADELPHIA

# About the Federal Reserve

The Federal Reserve Bank of Philadelphia is one of 12 regional Reserve Banks in the United States that, along with the Board of Governors in Washington, D.C., make up the Federal Reserve System, the nation's central bank. To ensure a sound financial system and a healthy economy, the Fed conducts monetary policy, supervises and regulates financial institutions, maintains the payments system, and serves as the lender of last resort in a financial crisis.



The Philadelphia Fed is responsible for the Third District, which covers eastern Pennsylvania, southern New Jersey, and Delaware. Like other Reserve Banks, the Philadelphia Fed is involved in conducting monetary policy, supervising and regulating banks, and providing financial services to banks and the federal government.

The Board of Governors, which is accountable to Congress, oversees the Reserve Banks. Fed Governors and Reserve Bank presidents participate in Federal Open Market Committee decisions on national monetary policy.

## *Payment Cards Center*

The Federal Reserve Bank of Philadelphia established a Payment Cards Center to provide insights into developments in consumer credit and payments. The center carries out its mission through an agenda of research and analysis, as well as forums and conferences that encourage dialogue incorporating industry, consumer, academic, nonprofit, and public-sector perspectives.

Today, consumers use many different types of payment cards. Below you'll find answers to some of the most frequently asked questions about payment cards.



## Why does the Philadelphia Fed have an interest in payment cards?

Payment cards, such as credit, debit, and prepaid cards, are increasingly becoming payment vehicles of choice for many consumers. The Philadelphia Fed has had a long association with the payment cards industry, given the number of major card companies that historically have been located in the region, especially in Delaware. In 2000, the Bank established the Payment Cards Center to further its study of this growing segment of the financial services industry.

## What is a payment card?

A payment card is typically a 3 ½" by 2 ½" plastic card with either a magnetic stripe or a computer chip that stores the card user's data, including card number and expiration date. The most familiar types of payment cards have a magnetic stripe and include credit, debit, and prepaid cards.

*Credit Card:* A credit card is any card that may be used to borrow money or buy products and services on credit. The balance can be paid in full by a set due date or paid over time with interest, as long as the borrower makes monthly minimum payments in amounts specified by the card-issuing bank. Credit cards are issued by banks, retail stores, and other businesses.

*Debit Card:* A debit card is associated with a checking or other deposit account. Funds are drawn from the associated account to settle debit card transactions, such as retail purchases or ATM withdrawals. Cardholders authorize debit card transactions by signing their name or by entering a personal identification number (PIN).

*Prepaid Card:* Prepaid cards differ from credit and debit cards in that they offer consumers a way to pay early for future purchases. Value is prepaid into the card account, and the cardholder can spend these funds at a later date by presenting the card for payment at accepting merchants or, in some cases, by using the card with a PIN to withdraw cash at ATMs. The

cardholder may spend the balance on the prepaid card over time or all at once. Examples of prepaid cards include gift cards and payroll and travel cards.

### *Is it bad to have several credit cards?*

Not necessarily. It is more important to borrow responsibly and to pay bills when they are due. Some consumers may find it convenient to have several cards: one for small purchases they pay off each month, and one for larger purchases they spread out over time. A third card for emergencies or business purposes might also be appropriate.

### *What is a credit limit?*

A credit limit is the amount established by the card issuer as the maximum amount you may borrow to pay for purchases or cash advances; it is based on your creditworthiness.

### *Are APR and interest rate the same thing?*

They are the same. APR stands for annual percentage rate (of interest) and represents the annual interest rate that cardholders pay to borrow funds using a credit card's revolving line of credit. The APR may vary depending on the credit card and on the individual. The APR can change over time, but card issuers are required to tell consumers about any such change, either as part of the Cardholder Agreement, which governs the use of the credit card product, or through a Change in Terms notice.

### *If I pay my balance in full each month, will I be charged interest?*

Typically, no. Credit card holders who pay their balances in full each month by the payment due date receive an interest-free grace period, during which no interest is charged on their current balance until the next payment is due. Cardholders should

*Cash advances on credit cards are typically charged special fees and higher interest rates than when the card is used for purchases.*



carefully read the Cardholder Agreement to understand exactly the policies and procedures governing their payment cards.

### ***What is the minimum payment, and how is it calculated?***

The minimum payment is the least amount a credit card holder must pay each month to keep the account in good standing. The minimum payment is typically the greater of 2.5 percent of the outstanding balance or \$15. You should review your Cardholder Agreement or check with your card issuer to confirm the minimum payment terms for your credit card.

Making only the minimum payment will extend the time it takes to pay off the balance. As an example, on an account with a 15 percent interest rate where the minimum payment is the greater of 2.5 percent of the outstanding balance or \$15, making only the required minimum payment on a \$5,000 purchase will take 18 years, five months, at a total principal plus interest cost of \$9,530.30.

Remember that the minimum payment represents the least amount your issuer will accept to keep your account in good standing. You may always pay more than the minimum, and most cardholders do just that. If you find that you are consistently having trouble making any more than the minimum payment, you may wish to seek the expertise of a reputable consumer credit counseling agency.

### ***What is a minimum finance charge?***

If you have a very low balance, the finance charges will be very low and may be subject to a minimum finance charge set by the card issuer. For example, if you have a \$25 balance and pay an annual interest rate of 15 percent, the finance charge for one month will be approximately 32 cents. Many issuers have a minimum finance charge of 50 cents. Therefore, you would be charged 50 cents, not 32 cents, for the billing cycle.

## *What is the average credit card debt of families in the U.S.?*

Research by the Federal Reserve finds that 68 percent of American families had credit cards in 2010. About 55 percent of those families carried a balance from one month to the next. Among families carrying a balance at the time of the survey, the average balance was \$7,100.

## *What is a cash advance?*

These are funds advanced to you from your credit card line. You can authorize cash advances by using your credit card and its PIN at an ATM or in person at a bank. However, cash advances on credit cards typically involve special fees and higher interest rates than when the card is used for purchases. Be sure to check your Cardholder Agreement to determine how your card issuer treats cash advances.

## *Several types of fees, including late, overlimit, and penalty fees, can be assessed on payment card products. How can I avoid such fees?*

To avoid these types of fees, keep your spending under your credit limit and pay your bill before the due date indicated on the statement.

## *What is a credit report?*

It is a confidential report on a consumer's payment history as reported by the consumer's creditors to a credit bureau. The credit bureau may provide the information only to entities that have a "permissible purpose" under the law to review a consumer's report. Some examples of entities with permissible purpose include lenders, such as credit card issuers; insurance providers; government benefits providers; landlords; and potential employers. The federal law that regulates use of these reports is the Fair Credit Reporting Act (FCRA).

To obtain a copy of your credit report, see instructions on the back cover.



## How do I check my credit report?

In December 2003, President George W. Bush signed into law the Fair and Accurate Credit Transactions Act (FACTA). This legislation requires, among other things, that the three nationwide credit bureaus — Equifax, Experian, and TransUnion — provide consumers, upon request, a free copy of their credit report once every 12 months. To obtain a copy of your credit report from one or all three of the major U.S. national credit bureaus, visit [www.annualcreditreport.com](http://www.annualcreditreport.com) or call 1-877-322-8228. To request your report(s) through the mail, visit [www.annualcreditreport.com/manualRequestForm.action](http://www.annualcreditreport.com/manualRequestForm.action), download the form, print it, fill it out, and then mail it to:

Annual Credit Report Request Service  
P.O. Box 105281  
Atlanta, GA 30348-5281

## What is a FICO score and how is it used in the credit approval process?

A FICO score is a credit score developed by Fair Isaac Corporation. Credit scoring applies a mathematical formula to an individual's credit bureau information to predict the likelihood that he or she will repay a loan according to the terms of the loan agreement. A credit score attempts to condense a borrower's credit history into a single number. It is one piece of information used by financial institutions in evaluating individuals' creditworthiness. (For information on what goes into a FICO score, visit [www.myfico.com](http://www.myfico.com).)

In general, the higher a credit score, the better the terms a borrower will receive. Those with high credit scores may be approved for higher loan amounts and lower interest rates than those with lower scores. Very low scores could prevent you from being approved for a loan.

## *What should I do if my payment card is lost or stolen?*

Immediately call your card issuer and report the card as lost or stolen and follow up in writing. Be sure to check your statement for fraudulent transactions and immediately dispute those transactions with your issuer by phone and also in writing. Remember, your card numbers can be stolen even if you still have the physical card in your possession; therefore, it is important to review your statements monthly and to frequently check your bank account balances. Be sure to reconcile any purchases and corresponding amounts as well as banking account activity, particularly withdrawals, against your receipts.

## *If my credit or debit cards are used without my authorization, how much could I lose?*

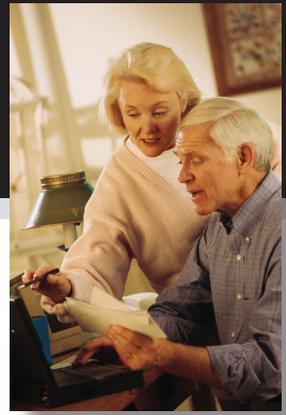
It is very important to notify your card issuer by phone and in writing as soon as you suspect that unauthorized charges have been made using your payment card.

For credit cards, federal law limits consumer liability to \$50 per card for unauthorized purchases. If you report the loss before your credit cards are used, the card issuer cannot hold you responsible for any unauthorized charges.

For debit cards, liability protection depends on whether the plastic card itself is stolen and used fraudulently. If it is, a time element is added to the protection: If unauthorized activity is reported within two business days, the liability limit is \$50. If unauthorized activity is reported within 60 days, the liability limit is \$500. If the fraud is reported more than 60 days after the customer received the statement showing the fraudulent activity, the liability is potentially unlimited. When thieves steal just the account number and use it either on its own or to produce a counterfeit plastic card, customers have zero liability for 60 days from receipt of the statement on which the fraudulent activity is reported and unlimited liability thereafter.

Many payment card issuers offer better liability protection for their customers than is required by law for either

*Phony e-communications can look real; legitimate companies will not ask for personal information such as passwords and account information by e-mail.*



credit or debit cards. You should check with your card issuer or refer to your Cardholder Agreement to review the issuer's policies regarding unauthorized card use.

### ***What is the best method of disputing charges on my credit card?***

In writing. Include the transaction number, amount, transaction date, posting date, name of the merchant, and the reason for the dispute. Most issuers provide a special form for this purpose and a special address. You may also call, but the dispute must be in writing to protect your rights. Your issuer may provide the form online and may accept online submission of the form as the equivalent of putting the dispute in writing.

### ***What is “phishing”?***

It is a high-tech scam that uses e-mails, pop-ups, and websites — that look like they are from a legitimate company with which you do business — to fool you into revealing personal or financial information the perpetrators can use to commit fraud. Remember: Phony e-communications can look real, and legitimate companies will not ask for information such as passwords and account information by e-mail.

### ***Is credit counseling harmful to my credit score?***

If you need credit counseling, there is a good chance your credit has already been severely damaged. In most cases, counseling will improve your credit score over time by helping you to follow a budget and to make regular payments to your creditors.

## *How can I find a reputable credit counseling agency?*

When developing a list of potential counseling agencies, do your research. Many universities, military bases, credit unions, housing authorities, and branches of the U.S. Cooperative Extension Service operate nonprofit credit counseling programs. Also, your financial institution, local consumer protection agency, and friends and family may be good sources of information and referrals. Once you've developed a list of potential counseling agencies, check them out with your state's attorney general, local consumer protection agency, and Better Business Bureau. They can tell you if consumers have filed complaints about them. Then, interview the final "candidates."

The Federal Trade Commission suggests that consumers be wary of counseling organizations that:

- Charge high up-front or monthly fees for enrolling in credit counseling or a debt management program (DMP);
- Pressure you to make "voluntary contributions," another name for fees;
- Won't send you free information about the services they provide without requiring you to provide personal financial information, such as credit card account numbers and balances;
- Try to enroll you in a DMP without spending time reviewing your financial situation;
- Offer to enroll you in a DMP without teaching you budgeting and money management skills;
- Demand that you make payments into a DMP before your creditors have accepted you into the program;
- Encourage you to withhold timely payment from your creditors.

*Your card numbers can be stolen even if you still have the physical card in your possession; therefore, it is important to review your statements monthly.*



### ***If I need advice on structuring my credit card payments, how can I get help?***

Reputable consumer credit counseling organizations can advise you on managing your finances, help you to create a budget, provide free educational materials and workshops, and, if necessary, assist you in working out repayment plans with creditors. Their credit counselors are certified and trained in the areas of consumer credit, money and debt management, and budgeting. Counselors discuss your entire financial situation with you and help you develop a personalized plan to solve your money problems.

### ***What is a debt management plan (DMP) and how does it work?***

A credit counseling agency may recommend that you enter a debt management program (DMP). You should sign up for a DMP only after a certified credit counselor has spent time thoroughly reviewing your financial situation and has offered you customized advice on managing your money. In a DMP, you deposit money each month with the credit counseling organization, which uses your deposits to pay your unsecured debts, like credit card bills, according to a payment schedule the counselor develops with you and your creditors. Your creditors may be willing to accept reduced payments if you enter into a debt repayment plan.

To obtain a free copy of your credit report from one or all three of the major U.S. national credit bureaus (Equifax, Experian, and TransUnion), visit [www.annualcreditreport.com](http://www.annualcreditreport.com) or call 1-877-322-8228. To request your report(s) through the mail, visit [www.annualcreditreport.com/manualRequestForm.action](http://www.annualcreditreport.com/manualRequestForm.action), download the form, print it, fill it out, and then mail it to:

Annual Credit Report Request Service  
P.O. Box 105281  
Atlanta, GA 30348-5281

## For More Information

The Federal Reserve Bank of Philadelphia has other brochures on credit topics.

To obtain copies of these brochures, or for additional copies of this one, please contact:

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Public Affairs – Publications**

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