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HEG94-195 Credit: How to Establish, Protect, and Use It

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Credit

How to Establish, Protect, and Use It

This NebGuide discusses how to obtain credit, suggests steps to take if credit is denied, and provides guidelines for managing your credit accounts.

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Buy now -- pay later! How many times have you been encouraged to use future income to pay for present needs and wants? Indeed, credit has become a way of life for many American consumers. While abuse of credit has created problems for some, credit itself should not be viewed as a villain. When used properly, credit can be an effective tool to help individuals and families reach financial goals. While credit can be an important part of a financial plan, the amount used must be controlled carefully.

Credit Advantages

For most people credit is essential for big-ticket items such as homes, automobiles, appliances or educational purposes. Few people have enough cash saved for major purchases.

Some households lack adequate emergency funds to cover unexpected expenses. Having credit available during times of financial emergencies can be important.

Credit is a convenience. Credit cards can eliminate the need for carrying large sums of cash or writing numerous checks. In many locations, a credit card is accepted more readily than a personal check.

Using the product while paying for it is another advantage. Some people prefer making payments while enjoying an item rather than setting aside money for a future purchase.

Credit allows consumers to take advantage of seasonal sales or to avoid anticipated price increases.

Interest and finance charges can be claimed as deductions on federal income taxes.

Credit Disadvantages

Credit is not free -- financing adds to the total cost. Overspending is more likely to occur. Because credit is convenient to use, some consumers fall into the trap of impulse spending rather than planned spending. There is also the tendency to look only at the required minimum monthly payment and not the total amount of the debt.

Credit usage commits future income. Borrowers are liable for their debts regardless of changes that occur in the future. If your income changes due to a job cutback or layoff, or an illness or disability, the debt that seemed easy to manage earlier could become a major threat to financial security. Or, if living expenses increase but income does not, that debt would add to the drain of monthly expenditures.

Qualifying for Credit

To qualify for credit, you must show potential creditors that you are creditworthy. While companies use various criteria to judge credit qualifications, ability to repay debt and willingness to do so are the primary considerations. While scoring systems vary from one creditor to another, characteristics usually examined include *income*, which measures ability to repay, and *credit history*, which indicates willingness to repay. Your credit history is a record of contracted debt such as charge accounts at department stores, installment loans, credit card accounts, and mortgage payments. Lenders believe how debt has been handled in the past is an indication of how credit obligations will be met in the future. While many consumers prefer to operate on a "pay as you go" system, cash transactions do not count towards establishing a credit history.

Other factors that lenders look for are *residence*, *employment record*, *current assets*, and *legal age* (in Nebraska, age 19) to obtain credit. Owning versus renting your home, the number of years you have been at your residence, and how long you have been employed at your job are viewed as measures of your stability and count towards your total credit score. *Debt outstanding* is also considered; for example, a substantial amount of indebtedness could affect your ability to repay a new obligation.

Under the Equal Credit Opportunity Act, credit cannot be denied because of age, sex, marital status, race, color, religion, or national origin. In addition, you cannot be denied credit because you receive public assistance or because you have exercised your rights under federal consumer credit protection laws (e.g., you sued a creditor you believed was violating these laws). The law basically provides that information cannot be required unless it is required of all qualified applicants. However, it does not guarantee that you will receive credit; you still must show that you are creditworthy.

Establishing a Credit History

Establishing your creditworthiness takes time. Unfortunately, when credit is needed, it is usually needed right away. To be prepared for situations when you need credit (e.g., financial emergencies), take steps now to build a credit history. Whether male or female, single or married, you need to establish your own credit identity.

In the past, many married women relied on their husbands' credit ratings. Then, when they became divorced or widowed, credit was difficult to get on their own. Even today women can encounter problems obtaining credit unless preventive action is taken.

Obtaining Credit

The following suggestions show you how to establish your own credit identity. Depending on your situation, some recommendations will be more helpful than others. If you have your own income or live in a small community where you are well known, obtaining credit could be relatively easy.

- *Open and maintain checking and savings accounts in your own name.* Be careful not to overdraw the checking account, and if possible, add to savings regularly. While this is not an indication that you can handle credit, it will show prospective lenders your ability to handle your own financial affairs.
- *Work at either a part-time or full-time job for a few months before applying for credit.*
- *Apply for a charge account at a local retail or department store.* If you are married and want the account in your name only, do not use your spouse's name and income to obtain the credit. If your income is low, start with a smaller independent store where you have shopped before. Limit the number of places where you first apply. Once credit is received, make payments for any purchases promptly. Do not apply for another credit card until you have established a good payment reputation.
- *Request any credit under your legal name.* A married woman who uses her social title (e.g., Mrs. John Jones) is likely to find the account listed under her husband's name. If married, you can use one of the following: first named and maiden name; first name and husband's surname; or first name and a combined surname (e.g., Susan Smith, Susan Jones, or Susan Smith-Jones).
- *Apply for an installment loan to purchase furniture, a major appliance, or a car.* If you do not meet the income requirements, consider asking a relative or friend to cosign the note. You will be responsible for payments, but the cosigner must bear the risk of assuming payments if you default on the loan.
- *Apply at your local bank for a small loan.* Or, if you are a member of a credit union, apply for a loan there. If you do not have a specific use for the borrowed funds, place them in a savings account, money market fund, or a short term certificate of deposit. Consider the interest you pay as the cost of establishing a credit identify.
- *Ask if you qualify for an overdraft privilege on your checking account.* Even if you never use it, the fact that were accepted could be viewed favorably later.
- *If you are married, apply for joint credit.* Since June 1, 1977, any credit accounts opened jointly by a husband and wife must be reported in both names. Accounts opened before that date could still be listed only under the husband's name unless a specific request was sent to the credit company asking that credit history information be listed under both names.
- *Ask that a joint account be changed to a separate account under your name.*

Once some of the above steps have been taken, then consider the following:

1. Apply for a gasoline or a national department chain store credit card.
2. Apply for a bank credit card such as a Visa or MasterCard.

If Credit is Denied

After applying for credit, you should receive an acceptance or rejection notice within thirty days. When credit is denied, you must be told either the specific reason or that you have the right to ask why you were rejected. If the denial was based on information in a credit report, you are entitled to know which credit reporting agency provided the information. If you ask to see your file within thirty days of the rejection notice, the credit agency cannot charge a fee. A fee can be charged, however, if you request a *written* summary.

If the file contains errors, the credit bureau must investigate and correct any misinformation. Any information that cannot be verified must be removed. If you do not agree with the report, you can write a

brief statement describing your version of the dispute. This statement then becomes a part of your file. Request that the credit bureau send the corrected report to any creditor who received the original report in the past six months. Then ask the company to reconsider your credit application based on the corrected information.

What if your file does not contain any negative information and you still are unsure why your application was denied? Do not blame the credit bureau. The bureau itself does not give credit ratings; it merely collects and stores information that is provided to its members for a fee. As mentioned earlier, creditors use different scoring systems for granting credit.

Your next step is to contact the credit department of the company that turned you down. Tell them you want the specific reason for being denied credit. Do not give up if the response is unsatisfactory. Write again to the company's credit division (carbon copies to the credit division manager and/or president of the company could also be in order). Indicate why you disagree with their findings or describe any contributing factors that led to the situation (e.g., due to cutbacks at work, your income last year was lower than usual). Explain why you are a good credit risk. Sometimes companies will reconsider an application if you give them good reasons to do so.

If taking these actions does not bring favorable results, apply to a different creditor. Perhaps you will qualify under a different lender's scoring system. Be prepared to be persistent until credit is received.

If you believe that your rejection was a result of discrimination (that is, someone else in a similar situation but of a different age, race, sex, marital status, etc. would be approved), contact the company and remind them of your rights under the Equal Credit Opportunity Act. Possible steps after trying to resolve the issue include contacting a federal agency such as the Federal Trade Commission or Federal Reserve Bank in your district, or requesting legal assistance.

Protecting Your Credit Rating

Many consumers have little knowledge about the information in their credit file or even where the information is located. If you do not know where your credit bureau is located, look under "Credit Reporting Agencies" in your telephone book yellow pages or ask your creditors to which bureaus, if any, they report credit transactions.

You are entitled to know what is in your credit file. Most credit bureaus will charge you a fee for that information unless you were denied credit in the past thirty days based on your credit report. Before you can have access to your report, you must verify that you are the individual whose name is on the file. Ask the credit reporting agency its procedure for disclosing file information. Most credit bureaus have forms to complete before you can see a summary of the file. This summary can be reviewed with you in person at the bureau, over the telephone with an agency employee, or sent via mail with an explanation of the report. Federal law (the Fair Credit Reporting Act) does not give you the right to handle your file physically -- only that you have the access to the information.

If you find errors that could affect your credit rating, take the steps described earlier to correct your file. Do not be surprised if some credit transactions or accounts are not listed. Some stores or institutions do not report to the credit bureau, and some report irregularly. If there are accounts that you want included, ask the companies to report that information to the credit bureau.

There are times when you should contact your credit bureau. Before you move to a new community, check your credit report for correct and updated information. This step could prevent problems when you apply for credit at your new location.

If you are a female who has recently married *and* changed your name, you need to inform your creditors and the credit bureau. Request that the credit bureau consolidate your past credit history under your new name so that your records remain intact and not under two separate names.

If you are a married woman who opened accounts with your husband before June 1, 1977, be sure those accounts are reported under both names. If you previously have not taken this action, do so as soon as possible. Simply write to the creditors and indicate that under the Equal Credit Opportunity Act, you want all credit information listed under both names. Include in each letter the account number, the names you want listed (remember to use legal, not social, titles) and your address. If accounts opened during that period are now closed, check your credit bureau file. If the accounts are listed only in your husband's name, ask that they also be listed in your name.

Guidelines for Using Credit

Achieving a good credit rating can take time, but reestablishing one after abusing credit can take even longer. Therefore, it is imperative that you carefully manage your credit use. As you read the following suggestions for using credit, check your own practices to see if there are adjustments you can make.

Know the cost of your credit transactions. Know not only the annual percentage rate (APR), but the actual dollar cost. Compare rates when you shop for credit. Ask yourself if the convenience or other advantages are worth the added cost.

Maintain a record of all credit card account numbers. With that record, keep each company's address and telephone number in case a card is lost or stolen.

Keep a record of purchases and a running balance due for each credit account. Always be aware of the *total* amount owed and not just the monthly payment.

Make payments on time. If circumstances prevent your paying bills promptly, contact the creditors and let them know when and how much you will pay. (NebGuide HEG 83-183, *Negotiating with Creditors*, describes steps to take when you have difficulty meeting credit obligations).

Limit the number of credit cards you carry. Never leave cards accessible to others. If you have cards that are not used often, keep them in a locked strongbox at home or in a safe deposit box. If you have a large number of credit cards, ask yourself if there are some that you can eliminate.

During a credit card transaction, keep your eyes on the steps involved. Be sure that the card only imprints one ticket, check the accuracy of the dollar amount before signing, and check that the card returned is yours. As a precautionary measure, request carbons from the credit receipt and destroy them. These carbons contain all of the information needed for someone else to make charges to your account.

Check monthly statements against your credit card receipts. If you find an error, write the company immediately. The Fair Credit Billing Act outlines procedures for creditors *and* consumers when errors occur. Your bill should describe these procedures.

Never lend your card or give your account number to another party to use. In most situations, do not give your account number over the telephone. An exception would be if *you initiated the call* to a reputable company. Under no circumstances should you give your account number to a person *who calls you*. The solicitor could plan to use your card for fraudulent purposes.

Read any credit contract carefully before signing it. If you are uncertain about any part of the contract, ask for clarification. Do not sign until you are satisfied the contract is accurate.

Never take on more debt than you can afford or use credit to live beyond your income. Be aware that credit obligates future income. Using credit involves a risk that future income and expenses can handle that commitment.

Before setting aside this NebGuide, take a few minutes to review the points that relate to you. Do you need to establish credit? What are two or three steps you can take to get started? Do you need more information? What adjustments can you make to improve your credit practices? Remember, while there are laws to protect your credit rights, you are the one primarily responsible for your credit status.

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B-1k, Money Management

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