



# Lending 101

## The Basics





# Loan Categories and Credit Types

## Loan Categories

**Secured loan** - a loan that is protected by an asset or collateral (ex. home or auto). The item purchased can be used as collateral and a lien is placed on the item. The deed or title is held by the lender until the loan has been paid in full, including interest and all applicable fees. Other items such as stocks, bonds, or personal property can be put up to secure a loan as well.

**Unsecured Loan** - a loan that is issued based only on the borrower's creditworthiness, rather than by a type of collateral. Borrowers generally must have high credit ratings to be approved for an unsecured loan.

## Credit Types

**Open End Credit** – (revolving) is a credit plan in which the creditor has a reasonable expectation of repeated transactions, stipulates the terms of those transactions, and provides for a finance charge that may be computed periodically on any outstanding balance (credit card, line of credit).

**Closed End Credit** - a loan in which the proceeds are dispersed in full when the loan closes and must be repaid, including any interest and finance charges, by a specified date (auto, mortgage, student).



# Credit Cards

## What is a Credit Card?

A credit card is a card issued by a financial company giving the holder an option to borrow funds, usually at point of sale (POS). Credit card issuers charge interest and are primarily used for short-term financing.






Credit Cards originated in the United States in the 1930s; their use was widespread by the 1950s.

They are issued by banks, credit unions, retail stores, oil companies and finance companies.

Some credit cards are only honored in a particular store (Macy's or Kohl's) but others are general purpose cards for use anywhere VISA, Mastercard, Discover or American Express are accepted.

## How does a credit card work?

Once approved for a credit card

-  Pay for an item or service with your card.
-  Store transmits sales information to credit card company.
-  Credit Card company approves or denies the transaction.
-  Credit card company bills you for purchases.
-  You get a monthly bill that you must pay.



# Vehicle & Personal Loans

## Vehicle Loans



New or Used car, truck, van, SUV and motorcycles are typically financed.



Title will be given or held for collateral and have lien placed in the lender's name.



Insurance (full coverage) on the vehicle will be required.



Loan amount is based on the Sales Price for new vehicles or NADA (National Automobile Dealers Association) for used vehicles.



A down payment may be required.



## Personal Loans

A loan that establishes consumer credit that is granted for personal use; usually unsecured and based on the borrower's integrity and ability to pay.

Secured personal loans would require something of value offered as security until the loan is paid in full. Example: car, jewelry, boat, equity, etc.



# Mortgage and Home Equity Loans

Mortgage - a loan in which property or real estate is used as collateral. The borrower enters into an agreement with the lender (usually a bank or credit union) wherein the borrower receives money to purchase the property then makes payments over a set time span until the lender is paid in full.

The most common term is a 30 year mortgage but 20, 15, and 10 year terms are also available.

Home Equity Loan - a type of loan in which the borrower uses the equity of the home as collateral. The loan amount is determined by the value of the property, which is determined by a licensed appraiser. Most lenders will loan up to 80% of the homes value.

Example of equity:

Appraised Value:	\$ 200,000
Mortgage Balance:	<u>-\$ 80,000</u>
Equity in Property:	\$120,000

What lenders will loan:

Appraised Value	\$200,000
80% of value	\$160,000
<u>subtract mortgage</u>	<u>\$ 80,000</u>

Possible loan amount: \$ 80,000



# Educational & Other Loan Types

## Educational or Student Loans

Federal loans are borrowed funds that you must repay with interest. A federal student loan allows students and their parents to borrow money to help pay for college through loan programs supported by the federal government.

Private student loan is a non federal loan issued by a lender such as a bank or credit union. They can have fixed or variable interest rates. Rates vary from lender to lender.



## Other types of Loans:

- Small Business Loans
- Payday Loans
- Peer to Peer Loans
- Salary Advance Loans



# What you need to apply?

## You must be 18 years old to enter into a loan agreement

- Complete application – with Name, Address, Date of Birth, Social Security Number, Employment information.
- 💰 Proof of income – paystubs covering a 30 day period.
- ✅ Identification.
- 📋 List of debts.
- 📄 If purchasing a car – dealer sheet or bill of sale.

## What happens next?

- ✅ Lender will review application.
- 📁 Request a copy of your credit report from one of the three Credit Bureaus.
- 💰 Verify income.
- ÷ Calculate your debt to income ratio (total monthly debts divided by total income = D/I Ratio).
- OK If your credit is satisfactory and you can afford the payment your loan will be approved.





# Credit Score and Credit Report

## What makes up your Credit Score?

Your credit score is very important. Your FICO (Fair Isaac Corporation) credit score is comprised of:

- Payment History (35%)
- Credit Capacity (30%)
- Length of Credit (15%)
- Accumulation of Credit (10%)
- Mix of Credit (10%)



FICO credit scores range from 350 to 850

The higher the credit score the better 850 = A+, 350 = E

## What is in a Credit Report?

- 1 Name, address, social security number, previous address, employer, previous employer and date of birth.
- 2 Public record information – judgments, liens and bankruptcies.
- 3 Trade lines – credit account/loan date opened, high credit, balance, payment and payment history.
- 4 Inquiries – who has requested your credit history.





# Interest Rates

A rate which is charged or paid for the use of money. Interest rates are typically noted on an annual basis, known as the Annual Percentage Rate (APR).

Basically the cost to use the lenders money.

Example:

Amount borrowed	\$1,000.00
Interest rate (yearly)	10%
Term	12 months
Monthly payment	\$ 87.93
Total Interest over 12 months	\$ 55.13

You will repay a total of \$1,055.13 over the life of the loan.

## Simple Loan Tips

Don't spend more than you make.

Understand the terms and conditions of your loans.

Charge to a credit card only what you can pay in full monthly.

If you can't pay the credit balance in full each month, always make the minimum payments.

Always pay on time.



# Glossary of Terms

**Appraisal** – an estimate of current market value of the property.

**Collateral** - something of tangible value (vehicle) pledged to assure loan repayment and subject to repossession upon default.

**Creditor** – a person or firm to whom money is due.

**Default** - Loan default is the failure to repay a loan according to the terms agreed to in the promissory note.

**Deed** – the legal document that establishes the property as security for payment of the loan.

**Equity** - is the difference between the value of the assets/interest and the cost of the liabilities of something owned.

**Interest** – the cost to borrowing money from a lender.

**Lien** - a right to keep possession of property belonging to another person until a debt owed by that person is discharged.

**Mortgage** – a type of security instrument that pledges real estate as security for a loan.

**Note** (promissory note) – a loan agreement that establishes a promise and obligation to repay the debt to the lender.

**Revolving loan** – an arrangement which allows for the loan amount to be withdrawn, repaid, and redrawn again in any manner and any number of times, until the arrangement expires.

**Title** - is a legal form, establishing a person or business as the legal owner of a vehicle.

**Secured loan** - a loan which contains a provision that, upon default, the lender may claim the pledged property called collateral as payment of the debt.

**Unsecured loan** - (signature loan) a loan that is granted on the basis of creditworthiness and signature. It is not secured with collateral.

