Loan to Own

Participant Guide

Building: Knowledge, Security, Confidence

FDIC Financial Education Curriculum

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LENDING TERMS

Loan Terms

Installment loan – A loan that is repaid in equal monthly payments or installments for a specific period, usually several years.

Secured loan – A loan where the borrower offers collateral for the loan. The borrower gives up his or her right to the collateral if the loan is not paid back as agreed.

Collateral – The asset (anything owned that has monetary value) a borrower promises to give to the lender if the borrower does not pay back the loan.

Unsecured loan – A loan where the lender does not require collateral.

Cost Terms

Annual percentage rate (APR) – A measure of the cost of a loan expressed as a yearly percentage rate. When shopping for the best loan rates, compare the APRs rather than the interest rates, since APRs reflect the cost of interest and other finance charges.

Fixed-rate loan – A loan that has an interest rate that stays the same throughout the term of the loan. Most installment loans have fixed rates.

Variable-rate loan – A loan that has an interest rate that might change during any period of the loan, as written in the loan agreement or contract.

Finance charge – The dollar amount the loan will cost. It includes items such as interest, service charges, and loan fees.

CONSUMER INSTALLMENT LOAN VERSUS RENT-TO-OWN

Consumer Installment Loans	Rent-to-Own Services
Secured installment loans are loans that are repaid in equal monthly payments for a specific period and are secured by the item you purchased. You can use the item you purchased while you are paying.	Rent-to-own allows you to use an item for a period of time. You make weekly or monthly payments in exchange for using the item. You do not have to purchase the item. However, if you decide to purchase the item, the store may set up a plan for you to rent the item until it is paid off. The store is the legal owner until you make the final payment. If you miss a payment, the store may repossess the property, which means you do not own it.
With installment loans, you are charged interest and you can shop for the best deal by comparing APRs.	Rent-to-own agreements are technically not loans, so no “interest” is charged and, often, no credit check is performed. The difference between the cash price and your total payment is just like interest you would pay on a loan.
Generally, installment loans are less expensive than rent-to-own agreements.	By making the weekly payments, you will pay much more than if you paid cash or used an installment loan.

CONSUMER INSTALLMENT LOAN VERSUS RENT-TO-OWN
(Continued)

EXAMPLE:

Chris is trying to decide between getting an installment loan and using a rent-to-own service to buy a television.

A local electronics store was selling the television Chris wanted for $1,500. A nearby rent-to-own store advertised the same model for $55 every other week. After seeing the advertisement, Chris went to the rent-to-own store to get more details. The manager told Chris he would own the television in 52 payments or 2 years. Chris multiplied $55 x 52 weeks and got $2,860.

Chris also found out that if he misses one payment, the rent-to-own service will take the television back. If he makes 50 payments on time – that is 50 x 55 = $2,750 – and misses payment 51, he loses the television and is out $2,750.

The manager told Chris that with rent-to-own, he could return the television with no obligation. Chris did another quick calculation. If he used the rent-to-own company and returned the television after a year, he would pay $1,430 – that is 26 weeks x $55.

Chris decided to purchase the television at the electronics store for $1,500. He obtained a 2-year installment loan with a 12 percent APR.

Chris made timely payments and paid off his loan in 2 years. He paid a total of $1,695.00. His monthly payments for the installment loan were $70.61, which is less than what he would have paid with a rent-to-own agreement – that is $55 x 52 weeks = $2,860

Consumer Installment Loan	Rent-to-Own
Advertised price = $1,500 12% APR for 2 years $70.61 x 24 months = $1,695 **Chris saved $1,165**	Advertised price = $55 every other week (hidden costs) $55 x 52 weeks = $2,860

Although $55 every other week sounds affordable, it actually costs more in the end.

FEDERAL TRADE COMMISSION PUBLICATIONS ON BUYING A CAR

The Federal Trade Commission or FTC has many publications that provide information to help you buy a car at the best price. At the FTC Website, you can download brochures such as:

- Buying a New Car – which includes tips on how to choose a car, information on negotiating the price, and considerations when financing a car.
- Buying a Used Car – which includes information explaining different payment options, dealer sales, private sales, and warranties.

Other publications include:

- Financing a Car.
- Fueling Up.
- Leasing a Car.
- Renting a Car.

You can also call the FTC at the phone number listed on page 17 of this Guide to request copies of its brochures.

CAR LOANS VERSUS CAR LEASES

Factors	Car Loans	Car Leases
Ownership potential	Car belongs to you and the bank that gave you the loan until you have paid off the loan. Then, the car becomes yours.	You are essentially renting the car from the dealership. The lease is like a rental agreement. You make monthly payments to the dealership for a set number of years. But the car does not belong to you. When the lease ends, you have to return the car to the dealership.
Wear and tear	No additional costs for wear and tear in your loan agreement.	Most leases charge you extra money for any damage found at the end of the lease that goes beyond "normal wear and tear."
Monthly payments	Payments are higher; however, at the end of the loan, you own the car.	Payments are lower because you are not purchasing the car; the dealership still owns it. Once your lease ends, you turn the car back in and the dealership can sell it or lease it to another customer. You may decide to purchase the car at the end of the lease; however, the total cost ends up being more than it would have been if you had bought the car instead of leasing it.
Mileage limitations	No mileage restrictions.	Leases restrict the number of miles you can drive the car each year. If you exceed the mileage allowed, you have to pay the dealer for each mile over the limit, according to your lease. For example, a dealer may charge you 15 cents for every mile that you drive over 24,000 miles in 2 years. If you drive the car an additional 3,000 miles, you would owe the dealer $450 for those miles.

CAR LOANS VERSUS CAR LEASES (Continued)

Factors	Car Loans	Car Leases
Auto insurance	May cost more during the loan than it will after the loan is repaid because the lender may require more coverage, but usually still less expensive than auto insurance for leased cars.	Usually costs more if you lease a car than it does if you buy. Most car leases require you to carry higher levels of coverage than purchase agreements do. Some insurance carriers may also consider leasing to be higher risk than purchasing.
Cost	Probably will cost more in the short term than a car lease; your total loan and monthly payments are likely to be higher. However, once the loan is repaid, the car is yours.	Probably will cost less in the short term than a car purchase; your total loan and monthly payments are likely to be lower. However, if you exceed the mileage on a leased car and/or decide to buy it outright once your lease has expired, it will end up costing you more.

Make sure you find out what the requirements are and get a cost estimate from your insurance company before you decide whether to lease or buy.

Remember, you will have to have insurance coverage for your new car before you can legally drive it away from the dealership.

BEWARE OF DEALER/LENDER RELATIONSHIPS

Instructions

- Read the scenario carefully.
- Write down some things that Sam could have done differently.
- Be prepared to explain your answers.

Scenario

Sam assumed the dealer would give him the best deal and did not shop around for a car loan. After all, he was able to negotiate the best price at this dealership – $6,000 for a used pickup truck.

The dealer told Sam that if he put up $1,000 as a down payment, he could get a car loan for 16 percent. Sam accepted the agreement without researching other possibilities.

This is what happened:

- The car dealer had called several lenders in the area for Sam. Lender A told the dealer that Sam qualified for a $5,000 car loan for as low as 10 percent.
- However, Lender A had an agreement with the dealer stating that for any rate over 10 percent, the lender and the dealer would split the profit. This gives the dealer an incentive to work with Lender A and to charge Sam a high interest rate.
- The difference between a 16 percent loan and 10 percent loan is $921. That means Sam paid $921 more than he had to. The dealer and Lender A split the $921.

What could Sam have done differently?

BEWARE OF CAR TITLE LOANS

Michael had $500 in unexpected medical expenses and needed a loan. He saw a television commercial that declared, "If you have a car, you can get a loan." Michael had a car worth about $2,500, so he decided to apply for the loan.

The finance company Michael saw in the commercial loaned him $500 at 20 percent interest per month. Note that the finance company did not advertise the APR. The finance company took his car title as collateral and Michael kept the car.

With a 20 percent monthly interest rate on the $500 loan, Michael owed $600 at the end of the month -- the $500 loan plus $100 in interest.

Michael could not repay the $600 at the end of the month. The lender could have repossessed the car. However, the lender gave Michael the option of just paying the $100 interest and gave him until the next month to pay the loan. At the end of the next month, Michael still owed $600 ($500 loan + another $100 in interest).

By the 1 of one year, Michael had paid $1,200 in interest for his $500 loan – $100 every month = $1,200! This equates to a loan with a 240 percent APR. Finally, Michael received a bonus from work and was able to pay off the $600.

This is an expensive way to borrow money!

THE SHADY CONTRACTOR

Instructions

- Read the scenario carefully.
- Answer the questions.
- Be prepared to explain your answers.

Scenario

Shady Contractor came by Jim's house and offered to install a new roof. Shady Contractor's price sounded fair. Jim said he was interested but could not afford Shady Contractor's services at that time.

Shady Contractor said Jim should not worry. Shady Contractor could arrange for financing through a lender he knew. Shady Contractor sounded honest and sincere, and Jim really wanted his roof fixed, so he agreed.

Shady Contractor started work on the roof. A few days later, the lender asked Jim to sign some documents. Jim was alarmed that the lender rushed him through, without letting him read the documents. Shady Contractor threatened to walk off the job if Jim did not sign the loan papers.

Later, Jim realized he had signed a home equity loan. The interest rate, points, and fees were very high. Jim felt cheated, but took comfort in the thought that at least his roof would be fixed. However, soon after the loan closed, Shady Contractor stopped coming to fix the roof. The roof work was not completed.

Jim found out the lender had paid Shady Contractor directly – it was part of the contract agreement that Jim did not read. Now that Shady Contractor had his money, he did not care whether he completed the job. Jim had a difficult time paying his loan and had to find someone else to finish fixing his roof.

Where did Jim go wrong?

What should he do now?

UNSECURED INSTALLMENT LOAN TIPS

- If you plan to use an unsecured installment loan to consolidate your other loans, make sure the new APR is lower than your current APR.

- As with any other loans, you could become overwhelmed and unable to make the payments. If you have trouble paying your bills, you might consider getting credit counseling.

- Beware of debt consolidation traps. These are loans that you get in order to help pay off what you owe on several credit cards. They can be either secured loans, such as home equity loans, or unsecured loans.

- Beware of companies and Websites that charge high rates and application fees. Look for hidden charges. Ask for references before signing an agreement.

- Choosing the wrong debt consolidation loan can make matters worse and put you further into debt. Shop around so that you have the information to decide on the debt consolidation loan that best meets your needs and budget. Research different lenders and collect quotes before deciding.

- Good credit counseling agencies can help you budget and negotiate with your lenders to make loan payments more manageable.

- To learn more about how to choose a credit counselor, attend the Money Smart module Charge It Right. The Money Matters module has helpful budgeting tips.

WHAT DO YOU KNOW? – LOAN TO OWN

Instructor: ___________________________________ Date:________________________

This form will allow you and the instructors to see what you know about loans both before and after the training. Read each statement below. Please circle the number that shows how much you agree with each statement.

	Before the Training				After the Training			
I know:	Strongly Disagree	Disagree	Agree	Strongly Agree	Strongly Disagree	Disagree	Agree	Strongly Agree
1. How to identify various types of installment loans.	1	2	3	4	1	2	3	4
2. Why installment loans cost less than rent-to-own services.	1	2	3	4	1	2	3	4
3. The factors lenders use to make loan decisions.	1	2	3	4	1	2	3	4
4. The questions to ask when purchasing a car.	1	2	3	4	1	2	3	4
5. The advantages and disadvantages of borrowing against a home.	1	2	3	4	1	2	3	4

EVALUATION FORM

This evaluation will allow you to assess your observations of the Loan to Own module. Please indicate the degree to which you agree with each statement by circling the appropriate number.

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
1. Overall, I felt the workshop was: [ ] Excellent [ ] Very Good [ ] Good [ ] Fair [ ] Poor					
2. I achieved the following training objectives:					
a. Identify various types of installment loans.	1	2	3	4	5
b. Explain why installment loans cost less than rent-to-own services.	1	2	3	4	5
c. Identify the factors lenders use to make loan decisions.	1	2	3	4	5
d. Identify the questions to ask when purchasing a car.	1	2	3	4	5
e. Describe the advantages and disadvantages of borrowing against a home.	1	2	3	4	5
3. The instructions were clear and easy to follow.	1	2	3	4	5
4. The overheads were clear.	1	2	3	4	5
5. The overheads enhanced my learning.	1	2	3	4	5
6. The time allocation was correct for this module.	1	2	3	4	5
7. The module included sufficient examples and exercises so that I will be able to apply these new skills.	1	2	3	4	5
8. The instructor was knowledgeable and well prepared.	1	2	3	4	5
9. The worksheets are valuable.	1	2	3	4	5
10. I will use the worksheets again.	1	2	3	4	5
11. The students had ample opportunity to exchange experiences and ideas.	1	2	3	4	5

12. My knowledge/skill level of the subject matter before taking the module.	0	1	2	3	4	5
13. My knowledge/skill level of the subject matter upon completion of the module.	0	1	2	3	4	5

EVALUATION FORM (Continued)

Instructor Rating

Please use the response scale and circle the appropriate number.

Response Scale: **5 Excellent** **4 Very Good** **3 Good** **2 Fair** **1 Poor**	**Name of Instructor**
Objectives were clear & attainable	**5 4 3 2 1**
Made the subject understandable	**5 4 3 2 1**
Encouraged questions	**5 4 3 2 1**
Had technical knowledge	**5 4 3 2 1**

What was the most useful part of the training?

____

____

____

What was the least useful part of the training?

____

____

____

GLOSSARY

Annual percentage rate (APR)

The APR is a measure of the cost of your loan expressed as a yearly percentage rate. When shopping for the best loan rates, compare the APRs rather than the interest rates since APRs reflect the cost of interest and other finance charges.

Capacity

One of the Four Cs of loan decision-making, capacity is your present and future ability to meet your payment obligations. This includes whether you have enough income to pay your bills and other debts.

Capital

One of the Four Cs of loan decision-making, capital refers to the value of your assets and your net worth.

Car lease

A car lease is an agreement between you and the car dealer that allows you to rent the car for a period of time. You make monthly payments to the dealership, but the car does not belong to you. When the lease ends, you have to return the car to the dealership.

Car title

This is a legal document that indicates who owns the car. The bank that lends you the money to pay for the car keeps the title until you pay off the loan.

Character

One of the Four Cs of loan decision-making, character refers to how you have paid bills or debts in the past. Your credit report is one tool lenders use to consider your willingness to repay your debts.

Collateral

One of the Four Cs of loan-decision making, collateral is a property or an asset that you promise to give to the bank if you cannot pay back the loan.

Equity

Equity is the value of your home minus the debt.

GLOSSARY (Continued)

Finance charge

The finance charge is the dollar amount the loan will cost you. It includes items such as interest, service charges, and loan fees.

Fixed-rate loan

This is a loan that has an interest rate that stays the same throughout the term of the loan. Most installment loans have fixed rates.

Home equity loan

If you own your home, you have the option of borrowing against the value of your home. This is called a home equity loan.

Installment loan

This is a loan that is repaid in equal monthly payments, or installments, for a specific period of time, usually several years**.**

Loan pre-approval

Loan pre-approval occurs when a financial institution calculates how much money you can borrow. It is typically a free service and does not obligate you to accept a loan offer from the institution.

Participation fee

A participation fee is money that some dealer finance companies might charge you to get a low interest rate.

Secured loan

A secured loan is one where the borrower offers collateral for the loan.

Title loan

A title loan is a short-term (usually 1 month) loan that allows you to use your car as collateral to obtain money.

Unsecured loan

An unsecured loan is a loan that is not secured by collateral**.**

GLOSSARY (Continued)

Variable-rate loan

This is a loan that has an interest rate that might change during the period of the loan, as written in the loan agreement or contract.

FOR FURTHER INFORMATION

General Resources

Federal Consumer Information Center (FCIC)

The Federal Consumer Information Center (FCIC) provides free online consumer information to help the public. The FCIC produces the Consumer Action Handbook, which is designed to help citizens find the best source for assistance with their consumer problems and questions.

www.pueblo.gsa.gov

800-688-9889

Federal Deposit Insurance Corporation (FDIC)

Division of Supervision & Consumer Protection
2345 Grand Boulevard, Suite 1200
Kansas City, MO 64108
877-ASK-FDIC (877-275-3342)
email: consumer@fdic.gov
www.fdic.gov

Federal Trade Commission (FTC)

The FTC publishes a variety of consumer education brochures.
www.ftc.gov/ftc/consumer.htm
877-382-4357

Firstgov.gov: The Federal Government's Web Portal

FirstGov.gov is the official gateway to all government information.

www.firstgov.gov

U.S. Financial Literacy and Education Commission

MyMoney.gov is the U.S. government's Website dedicated to teaching all Americans about financial education.

Whether you are planning to buy a home, balancing your checkbook, or investing in your 401k, the resources on MyMoney.gov can help you.

Throughout the site, you will find important information from 20 federal agencies.

www.mymoney.gov

888-My-Money (888-696-6639)

FOR FURTHER INFORMATION (continued)

Buying a Car

The Federal Trade Commission (FTC) has information that can help you buy a car and help you get the best price. The Website www.ftc.gov/bcp/menu-auto.htm has brochures such as:

- *Buying a New Car* – includes tips on how to choose a car, information on negotiating the price, and considerations when financing a car.
- *Buying a Used Car* – includes information explaining different payment options, dealer sales, private sales, and warranties.

Home Improvement

For information on home improvement, including how to hire contractors, how to understand your payment options, and how to protect yourself from home improvement scams, read the FTC brochure, *Home Sweet Home…Improvement*. You can find the brochure at the following Website:

www.ftc.gov/bcp/conline/pubs/services/homeimpv.pdf.

Legal Services

If you think you are a victim of a scam, contact an attorney. Most communities have programs that provide free legal services to individuals with little or no income. Look in the community services pages of your phone book or look in the white pages under "Legal Services of…" for the phone number of the local program.

The American Bar Association has a directory of pro bono programs (volunteer lawyer programs). The programs use local lawyers who have agreed to provide free legal services. To find a program in your area, you can go to the following Website:

http://www.abanet.org/legalservices/probono/directory.html.