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# *Credit*

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There are three potential solutions, depending on the needs of the client, which are important to understand when working with credit scores:

- 1) Credit Repair
- 2) Re-establishing or Building Credit
- 3) Maintaining Good Credit

Following is some helpful information about each area.

## Credit Repair

There are several solutions to repairing your credit and we have contact information for firms that can help you. Some of them charge a monthly fee and some charge a flat one-time fee. Depending on the circumstances, one firm might be more advantageous than another. It is the sole decision of the client to determine which, if any, of these options fits best for them.

# Re-establishing Credit

## STEP 1 - DEPOSIT, BORROW, AND PROSPER!

Go to Bank A and open a savings account with your \$1,000 (or whatever amount you have allocated). This should be an interest-bearing account earning the highest rate you can find. Take your passbook home and wait three days.

Return to Bank A (dressed and poised for success) and ask to see a loan officer. Take your passbook with you, and explain to the officer that you wish to take out a loan, for which you are willing to place your savings account as collateral. This is the easiest type of loan to obtain because it is completely secured with cash. Be prepared to name a reason for the loan, although it should be granted regardless of the purpose because it will be backed by your savings account. Make sure you obtain an installment loan, amortized over one year with monthly payments required. Remember, you are building credit, so a loan that is due all in one lump sum at the end of 180 or 365 days will not serve your purpose. While a credit check is not always made for this type of loan, be prepared to acknowledge any bad marks on your credit record and explain that you are trying to re-establish your credit. Assure him/her that you will faithfully make your loan payments.

Assume you get a loan for 90% - or \$900 - of your savings account, with a 6% interest rate. On a \$900 loan you would pay \$29.52, owing the bank a total amount over one year of \$929.52. Your monthly payments will be \$77.46.

Once this loan is made, Bank A will freeze your \$1,000 so your loan collateral cannot be withdrawn. However, each time you make a payment on your loan, an equal amount (less interest) will be unfrozen in your account and available for withdrawal.

Take your loan check for \$900 to Bank B and open another savings account with this amount. Wait three days, and get your second loan - this time for \$810 (90% of \$900). Your monthly payments here will be \$69.71. (Again, assuming 6% interest)

Now use your \$810 and open an account at Bank C. Wait three days, and obtain a 90% loan for \$729, with monthly payments due of \$62.74.

Savings	Balance	Loan	Payment	Interest Paid
Bank A	\$1,000.00	\$900.00	\$77.49	\$29.52
Bank B	\$900.00	\$810.00	\$69.71	\$29.57
Bank C	\$810.00	\$729.00	\$62.74	\$23.91

## DON'T PANIC!

By the time you obtain your third loan, about two weeks have passed. You now have three bank loans totaling \$2,439 and \$729 in cash (your loan from Bank C). How will you pay these loans back? It's easy. Use enough of your \$729 to make your first payment on your Bank A loan (\$77.46). Do the same at Bank B and Bank C. You should now have made payments that are ahead of their due dates by about one week at Bank A, two weeks at Bank B, and three weeks at Bank C. You have used about \$200 of your \$729, but you have also freed up frozen funds that can be withdrawn later.

Now wait about another two weeks and repeat the loan payment process described above, making another set of payments with your remaining cash. At this point, you should be approximately one full month ahead on all three loans.

With the balance left from your cash loan, make your third set of payments on the second payments' due date. By now, your \$729 should be almost depleted. Approach each bank and withdraw the funds that have been unfrozen to use towards your next set of payments.

Continue this process until at least six payments have been made on each loan. You can payoff your loan in full, if you wish, after that point. Do not pay them off before six months, because this is the time frame usually considered when a payment history is calculated as a possible credit reference.

#### WHAT DID THIS REALLY COST?

In our example, the interest rate charged on the loans was 6%. And, your savings accounts were drawing 2% interest, making your net interest only 4% (6%-2%). We will assume the loans were for one year (12 months) and that you did not pay them off early. Bank loan A for \$900 charged \$29.52 interest, from which we subtracted \$20.18 - the 2% interest you gained from your \$1,000 savings - for an actual annual cost of \$9.34. If you paid off your loan in six months, it would have cost you even less! Overall, it costs pennies to re-establish your credit using this method!

That's a very small amount to pay for three fast and easy credit references that indicate your ability to acquire bank loans in varying sizes, make your payments ahead of schedule, and pay the loans off completely before due. These activities will all look very impressive on your new credit report! And, you should still have your original \$1,000.

Now is a good time to contact your local credit bureau (ask your banks which one they report to) and have this new credit information added to your profile. The bureaus will send you a credit addition form to complete and mail back. There is usually a small fee for each item to be added. They should also send you an updated copy of your new credit report.

#### STEP 2 - SECURED CREDIT CARDS

##### How Secured Credit Cards Work:

Now it's time to use these bank references to obtain a credit card. Select one of the banks you particularly liked doing business with and use your initial \$1,000 to make a deposit there. After about one week, pick up an application form for either a Visa or MasterCard and fill it out completely at home. Be certain that the card you are applying for allows for cash advances, and include your other two bank references on the application. Then meet with a loan officer at the bank and give him/her your completed form, saying that you are willing to have your \$1,000 frozen to secure a credit card with a \$1,000 line of credit. This type of secured credit plan is very common and is available to new credit builders as well as credit builders with a bad history. Similar to your bank loan, your savings is used as collateral for any debts you may accrue using the card. The card will look like any other Visa or MasterCard, so only you and the bank know it is secured by your savings.

##### Shopping to Build Credit

Once you have your card, use it. It is important now to again demonstrate a good payment record. A credit card that never gets used can actually reflect negatively on your profile!

Go to your local shopping mall and find a store that carries a returnable item in the \$500 to \$800 range (remember; your credit limit is \$1,000). You can select a piece of jewelry, a television, audio or video equipment, or other merchandise within this price range. Make sure you understand the store's return policy - you will need to be able to return the item later for a credit on your charge account, not just store credit. Purchase the single item with your new Visa or MasterCard, take it home, and safeguard against damage or theft. After several days, go back to the store and return the item, requesting a Credit on your card.

When you receive your first monthly statement for your card, you will notice a column marked Payments/Credits. Your credit for the returned item will show up in this column, although it looks the same as if you had paid for the item in full. Anyone examining your credit record will see that you made a sizeable purchase and a very early payment.

#### Obtain a Cash Advance

There is one final step to establishing your good credit record with a credit card company. Stop by a different bank than the one that issued your credit card and ask for a cash advance. Visa and MasterCard allow any lending institution that honors their cards (almost all) to make cash advances for varied amounts up to your credit limit. Some allow only a 25% cash advance, while others will loan your entire amount. Be advised that borrowing money in this manner usually costs more in interest than your card charges for merchandise, so it is not a good way of routinely obtain loans. But it is useful for our credit-building purposes under this plan. Since you will be charged interest on your cash advance from the day you receive it, you may want to time this transaction toward the end of your billing cycle.

Let's assume that you get a 50% cash advance on your \$1,000 limit, or \$500. Don't spend the money. Put it away and wait for your next monthly statement. Use the money to promptly pay back your cash advance charge on your bill. Now you have used a large amount of your credit limit on two occasions, and your record indicates both were paid back in full. Your credit history is looking better and better!

### STEP 3 - UN-SECURED CREDIT CARDS

#### Low Interest Pays Off

Before taking specific steps to obtain an unsecured credit card, it really pays to shop around for a bank issuing Visa or Mastercard at the lowest possible interest rate. The national average is presently at about 19 to 20 percent. At this rate, an average balance of \$650 will cost you \$123.50 annually in interest charges. The same \$650 balance will only cost you \$78 on a 12% card - a savings of \$45.50 per year.

You also want to consider any annual fee charged for use of the card, which can range from \$20 to \$50 for premium cards such as MasterCard Gold and Visa Gold. While Gold cards traditionally require a higher annual fee, they typically offer higher credit limits. For the purposes of this plan, we do not recommend obtaining a Gold card. Take a look also at the grace period various banks allow between the time of purchase and when interest starts to accrue. If a bank offers no grace period, you will still be charged interest on your balance in full after each billing period. Again, to find out about rates, fees, and grace periods, you can pull out the Yellow Pages and call around locally. The business sections of major newspapers also often carry ads by local banks promoting the features of their credit cards. However, you do not need to apply for an unsecured card from a local bank. Computer networking makes it easy to quickly access any bank, and most are eager to have new credit card customers, regardless of where they live. You can find a list of U.S. banks offering low interest rates for Visa and MasterCard in the Bank-lists booklet contained in this document.

#### Approaching the Bank

Once again, have the new information about your secured credit card included in your credit bureau file. Now go to a bank and apply for whichever credit card (Visa or MasterCard) you do not already have, using your bank loans and current credit card as references. When the bank refers to your credit file, they will find you have an impressive payment history and another credit card with no outstanding balance. They should be more than willing to give you a regular, unsecured bankcard.

## Freeing up your \$1,000

At last, you need to have your \$1,000 savings account unfrozen and the credit card released from its secured status. Go back to the bank where you began this process, and inform the loan officer you now have an unsecured Visa or MasterCard. Explain that you received this card based upon your excellent payment history you established with their bankcard. Ask now to have the hold placed on your savings released. If he/she is hesitant, suggest that you will leave your money in the savings account, but no longer want it frozen. If the officer still seems reluctant, you can politely say that you will then have to return the credit card and close your account with them. In most cases, the bank will not want to lose you as a customer and will honor your request.

However, if these efforts fail, then go ahead and return your card and close your account. Go to the bank that gave you your unsecured credit card. Tell them that you like their services and rates better than where you previously banked and want to shift your Visa or MasterCard (whichever one you do not already have there) to that bank. Your second unsecured credit card should arrive in the mail soon after!

## STEP 4 - DEPARTMENT STORE CREDIT CARDS

### Instant Credit

With the first three steps completed, you should feel like a credit building pro and be proud of your new credit profile. This next step is easy. Because you already have a Visa and MasterCard, the credit world is wide open and waiting for you to sign on.

Most major department stores offer a form of instant credit - providing you with their store credit card just because you possess a major credit card, so they can collect the interest instead of Visa or MasterCard! Best of all, department store cards are issued on an unsecured, deposit-free basis! You usually will be asked to fill out a brief application form, show your I.D., present at least one major credit card - and you are accepted! This can sometimes be done right while you are making your purchase, or at a special customer relations desk. Many stores are even offering free gifts or special discounts to customers applying for instant credit. Be cautious, however, to apply only for cards in stores that you normally shop at. A dormant credit card does not look good on your credit report.

While many stores of all sizes now offer their own credit cards, for our credit-building exercise it is best to obtain one from a major department store chain with locations around the country.

### Department Stores Offering Instant Credit

Below is a partial list of U.S. department stores offering instant credit. Many may have store locations in your area. All stores listed here report to the credit bureaus.

- |                 |                   |                 |
|-----------------|-------------------|-----------------|
| . Bacons        | . Castner Knott   | . Halls         |
| . Lazarus       | . Macy's          | . May Company   |
| . Neiman Marcus | . J.C. Penny      | . Maas Brothers |
| . Broadway      | . Dillards        | . Jordan        |
| . Lord & Taylor | . Marshall Fields | . Marsh         |
| . Nordstrom     | . Home Depot      | . Mervyns       |

## STEP 5 - NURTURING YOUR CREDIT

Congratulations! By now you have three bank loans, Visa, MasterCard, and perhaps several major department store credit cards. We have planted all the seeds you need to cultivate a healthy credit profile. Now it's up to you to take care of your new credit record and allow it to grow with you as you build a more secure financial future.