

## Topic 2: Compare different types of payment card

After completing this topic, you will be able to:

- define, understand the purpose of, and compare the features of debit and credit cards;
- define, understand the purpose of, and compare the features of other cards, including:
  - store cards;
  - charge cards;
  - prepaid cards;
  - cash cards; and
  - contactless cards;
- understand what a ‘card limit’ is;
- understand the different charges on cards and the different charging structures;
- understand what is meant by ‘interest-free credit period’; and
- understand the meaning of ‘minimum payment’ and the consequences of meeting only these requirements.

### Different types of payment card

In this topic, we will look at the different plastic cards used to make payments. Some of them are more flexible than others and can be used to do more things. Some are a way of accessing money that is already yours; others are a way of borrowing in the short term. We will look at their different features and at what each is used for.



**What different types of card have you heard of?**



#### Activity 2a

- a) **List as many organisations as you can think of that manage payment cards (for example, Visa).**

**b) List as many organisations as you can think of that issue credit cards.**

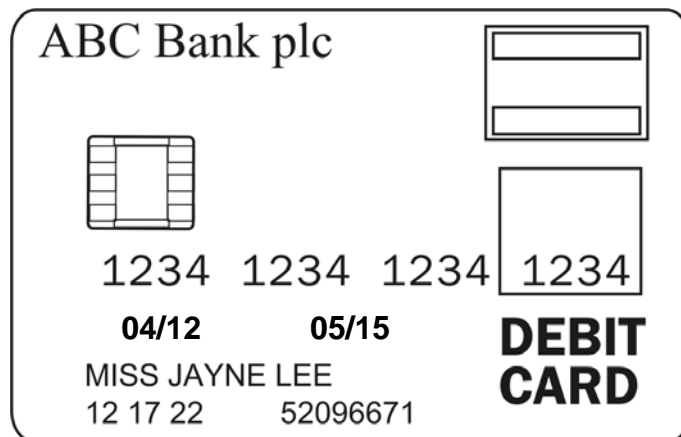
## Debit cards

Banks and building societies give customers a debit card so that they can access the money in their current account. Account holders can use debit cards to get cash from their accounts using an automated teller machine (ATM), and to make payments for goods and services either in person or over the telephone, by mail order or via the Internet.



### Activity 2b

**ABC Bank plc has given Jayne Lee a debit card.**



**a) What is the name of the bank that issued the debit card?**

**b) What is Jayne's current account number?**

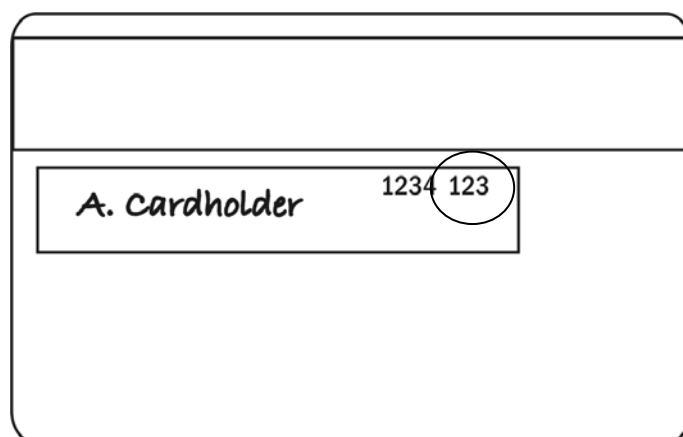
**c) What is the debit card number?**

**d) Where is the chip on the card?**

**e) What is the card's expiry date?**

## Using debit cards for mail order, telephone and Internet payments

When a debit cardholder uses their card to pay over the telephone or by mail order, they cannot type in their personal identification number (PIN) and they must *never* tell the merchant what their PIN is. Also, when a debit cardholder buys on the Internet, it is not safe for them to type in their PIN. Instead, when a debit cardholder makes a transaction from a distance, they are asked for the card security number that is written on the back of their debit card, as illustrated below.



## Getting cashback using a debit card

Debit cardholders can get cash when they pay for goods in shops that offer 'cashback'. The amount of cash that they want is added to the total amount of the transaction. This is the amount that is authorised and taken from their current account to pay the shop.

A maximum of £50 can be withdrawn in cash in this way per transaction.

This cashback service applies only to debit cards.



### Case study

Jayne goes into her local supermarket to get her food for the weekend. She also needs some cash, so she decides to use her debit card to pay for her food and get cashback.

Jayne's food shopping comes to £23.17 and she asks for £30 cashback. The checkout assistant types '£53.17' into the chip and PIN terminal. This is the amount that is authorised and the amount that is taken from Jayne's current account.

## Limits and charges on debit cards

The 'limit' on any kind of card is the maximum that you can spend on it. Because a debit card is used to access your own money, your 'limit' is how much you have in your current account. Once you have spent all of the money in your account (plus any overdraft that you might have arranged with the bank), you cannot use your card for any more transactions until you have put some more money into your account.

Sometimes, there is a charge for using a debit card to withdraw money from an ATM that belongs to a bank that is not your own bank. It may be as little as £1 or £1.50 per transaction.

There is also occasionally a small charge when you use your debit card to pay for things online – for example, airline tickets. This might be £3 or £4, or a small percentage of the value of the transaction.

## Advantages and disadvantages of debit cards

One advantage of a debit card is that it allows you to access the money in your account at any time of day or night.

One disadvantage is that you are limited to spending the amount that you have in your account.

## Credit cards

Credit cards are a type of rolling credit. They allow you to borrow money to buy things and pay it back over a period of your choice.



### Case study



Anna, who is 19 years old, has a debit card linked to her current account at Big Bank. Whenever she uses her debit card to pay for something, money is taken out of her current account.

Anna thinks of it as 'buying now and paying now':

For me, a debit card means 'Buy now and pay now'.

Anna also has a Big Bank credit card. Every time she uses her credit card, she is borrowing a little bit of money from Big Bank. Every month, she gets a statement showing all of the occasions on which she used her credit card to make purchases and a total at the bottom of how much she owes the bank. (The credit card transactions are kept separate from her current account transactions.)

Anna has to make a payment to Big Bank every month, but she can choose whether to repay the whole amount, or to repay only a small amount and carry the debt forward to next month.

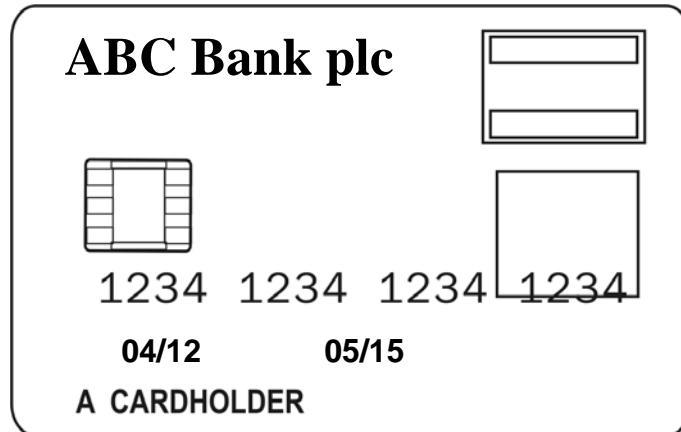
- If she chooses to repay all of the money that she has borrowed straight away, she will pay no interest to Big Bank – so she has been able to borrow free of charge.
- If she chooses to repay only a small amount to Big Bank, she will be charged interest on the part that she does not repay.

For me, a credit card means 'Buy now and pay later'.



**Activity 2c**

Below is a diagram of a credit card.



a) *Where is the Visa symbol?*

b) *Where is the credit card number?*

c) *Where is the chip on the card?*

d) *Where is the card's expiry date?*

**e) Where is the cardholder's name?**

## Using credit cards in ATMs

It is not only debit cards that you can use in ATMs; you can also use credit cards to withdraw cash from ATMs, and over the counter in banks in your own country and while travelling in other countries. These withdrawals are loans known as 'cash advances'.

Most credit cards charge interest on cash advances from the day on which the transaction is made. This means that even if a cardholder repays the balance on their credit card in full when the statement arrives, they will pay interest on any cash advances. This interest is charged daily from the day of the transaction to the day on which the cardholder's payment is credited to their card account.

Credit card advances are usually a very expensive way of borrowing money because credit card interest rates tend to be much higher than approved overdraft interest rates.



## Using credit cards in shops

Credit cardholders can tell if a merchant accepts their type of card by looking for the card symbol at the till.

Just like debit cards, credit cards have a chip and a cardholder must type in a PIN when they make a purchase. The amount spent on the credit card will appear on the next statement, along with the name of the shop.

## Using a credit card at a distance

Just like debit cards, credit cards have a card security number written on the back. It is printed on the cardholder's signature panel. This number is used when making a credit card transaction at a distance, such as when using it to pay for things bought online or over the telephone. Cardholders cannot type a PIN into a secure computer in these cases, so they tell the merchant or type in the card security number instead.

## Did you know?

The bank that issues the card is called the 'issuer'.

The shop or other supplier that accepts the card as payment is called the 'merchant'.

The bank that the merchant uses to process the card payment for them is called the 'merchant acquirer'.

## Limits and charges on a credit card

When you first get your credit card, you will be given a 'credit limit' – that is, a maximum amount that you can borrow on the card. If you exceed the limit, your transactions may be refused, or they will be paid and you will be charged for going over the agreed limit. Sometimes, if you are good customer, the card issuer will increase your credit limit – but only if it thinks that you can afford to borrow that much and not struggle to pay it back.

Some credit card companies make an annual charge for providing the card. There may be other charges, such as when you buy things online – especially items of high value. You may get charged an additional £5 or £10 for paying by credit card. You will also incur a charge if you use the credit card to get money out of an ATM. In this case, because you are not accessing your own money, you are borrowing cash from the credit card company instead, so there will be a cash advance fee.



As well as interest charges, other fees include:

- late payment fees (if your monthly payment is late);
- an 'over the credit limit' fee (if you spend over your pre-agreed credit limit); and
- a returned payment fee (if you set up a direct debit to make the minimum monthly payment to your credit card and, on the day that the payment was due to be taken, there was not enough money in your current account to do so).





### Activity 2d

The following are the fees and charges on a Lloyds Bank Advance Credit Card as at January 2014.

<b>Fees</b>	No annual fee	
<b>Charges</b>	Cash withdrawals	3% (min £3.00)
	Overseas transactions	2.95% (of equivalent sterling value of the transaction)
	Copies of statements	£6.00
<b>Default charges</b>	Late payment	£12
	Over credit limit	£12
	Returned payment	£12

You can avoid additional charges. Please stay within your credit limit and ensure that your payments are received on time.

Source: [www.lloydsbank.com](http://www.lloydsbank.com)

**a) Look at the fees for cash withdrawals. How much would it cost to use this credit card to take £100 out of an ATM in the UK?**

**b) Why do you think Lloyds Bank carries the warning about avoiding additional charges?**

## Repayment

A cardholder receives a statement every month detailing what they have spent and what they owe the credit card company, and they can then decide how to repay.

The cardholder has three choices, as follows.

- **Repay the balance completely**

If they do this, they will not be charged any interest.

- **Repay the minimum balance**

A cardholder must make a minimum repayment that is equivalent to more than a single month's interest. This means that the repayment will cover the whole of that month's interest plus some of the amount outstanding.

If the cardholder does this, it will take them a very long time to repay the card balance, as the case study below shows.



## Case study

Fiona has a credit card. She spent £100 on the card when she first got it and makes only the minimum repayment of 4 per cent.

Month	Debt from previous month £	Interest on debt @1.6% per month	New purchases on card £	Amount owed this month	Repays minimum at 4% £	Debt rolled over to next month £
Jan	0	0	100.00	100.00	4.00	96.00
Feb	96.00	1.54	0.00	97.54	3.90	93.64
Mar	93.64	1.50	0.00	95.14	3.81	91.33

In Fiona's case, if she continues to make only the minimum repayments, she will still owe the credit card company £40 at the end of three years!

- **Repay a sum larger than the minimum balance**

If the cardholder does this, they will repay the card balance more quickly than by repaying only the minimum balance and so will end up paying less interest. This is a method that they might use if they do not have quite enough to repay the whole amount.

Anything that the cardholder pays to the credit card company will be subtracted from the amount that they owe and the amount that they have available to spend on the card will go up by this amount.

## Interest-free credit period

Borrowing on a credit card is free of interest as long as you repay the whole amount within the interest-free period. The interest-free period varies between cards, but is commonly between 50 and 59 days. This depends on when the purchases were made,

when the credit card statement is due and on the policy of the individual credit card provider. For example, Barclaycard Platinum gives the cardholder a maximum of 56 days' interest-free (as at 31 January 2014).

## Introductory offers

Many credit cards offer low introductory rates to new customers and this can make them a cheap way in which to borrow over a short period – for example, six months. Depending on your credit limit, you can buy fairly large items in this way and repayment is more flexible.



### Activity 2e

**Max has a new credit card on which he has been given a credit limit of £1,000. During May, he goes shopping and makes several purchases using his card. No money leaves his bank account, but now he owes the money to the credit card company.**

**At the end of the month, Max receives his statement from the credit card company. It shows the details of all of his purchases and tells him that he owes the company a total of £800. The statement shows his credit limit of £1,000 and also tells him that his available credit at the moment is £200 – that is, the amount of credit that he has not yet used. It also tells him that he must make a minimum repayment of £50.**

**Max does not have £800, but he wants to repay more than the minimum to keep down the interest that he will have to pay. He chooses to repay £500.**



**a) How much does Max owe to the credit card company after this repayment?**

**b) What is his available credit after this repayment?**

## Did you know?

More than 14 million people are using their credit cards for everyday spending, with one in five carrying three or more cards.

More men than women carry multiple cards, with one in four men having three or more credit cards, compared with one in six women.

Source: [www.moneysupermarket.com](http://www.moneysupermarket.com) (cited in the *Daily Telegraph*, March 2010)

## Advantages and disadvantages of credit cards

One advantage of a credit card is that you can buy something and pay for it later.

One disadvantage is that you have to pay high interest rates if you do not repay your balance in full straight away.



**Can you think of some other advantages and disadvantages of credit cards? (For example, think about what might happen if you had too many credit cards and if you were not very good at budgeting.)**

## Store cards

Some stores issue cards that you can use only in that shop. These may offer you discounts on the items that you buy using the card – especially when you first apply. Store cards work like credit cards, but tend to have higher rates of interest.

Although you may be eligible for special offers at a shop to which you go a lot, the interest rate quoted for that store's card can be up to twice the rates charged by credit card companies. The amount owing can soon add up if you do not repay the bill for several months.



A lot of people who have taken out a store card had no intention of making a big purchase before they went shopping. But because store cards are available at the point of sale, and are very quick and easy to sign up to, they have ended up spending more than they had planned. Sales staff can be very persuasive and customers do not always think about the consequences of what they are doing.

You should look at the APR carefully when considering taking out a store card.

For example, at January 2014, a comparison of rates quoted on provider websites was as follows.

	<b>Provider</b>	<b>Card interest (Variable APR)</b>	<b>Overdraft interest rate (EAR)</b>
<b>Stores</b>	New Look	28.9% (Service offered by Ikano Bank)	Not applicable
	Debenhams	19.9% (Service offered by Santander Cards UK Ltd)	Not applicable
<b>Banks</b>	Barclays	34.9% Barclaycard Initial	Free overdraft up to £200 19.3% for overdrafts of £200–£5,000 Barclays Bank Account
	First Direct	19.9% Credit Card	Free overdraft up to £250 15.9% for overdrafts over £250 First Account



### Activity 2f

The Office of Fair Trading (OFT), which was the regulator of consumer credit until April 2014, produced the following ‘Top ten tips’ on store cards.

1. **An initial discount may be good, but it depends on how quickly you pay off the balance.**
2. **Be APR wise – how much will you pay on an uncleared balance?**
3. **Is there an interest-free period and how long is it? What will the interest rate be afterwards?**
4. **Check all details of the agreement and do not be afraid to ask questions.**
5. **You do not have to take out any payment protection insurance, because it is expensive.**
6. **Compare with other ways to pay.**
7. **A store card is a serious credit commitment for which you need to budget.**
8. **Beware of pushy sales staff and do not be lured into taking out a store card if you do not want to do so.**
9. **You do not have to sign on the spot – if in doubt, take the agreement away, read it and seek advice before you sign.**
10. **If you get into payment difficulties, talk to the lender as soon as possible.**

**Look at these pieces of advice and think about why they are sensible.**

## Limits and charges on store cards

Store cards work in much the same way as credit cards when it comes to credit limits and charges. The credit limit tends to be a lot smaller, however, because you can use the card only in the shop that issued it.

## Advantages and disadvantages of store cards

One advantage of a store card is that you may qualify for discounts in the shop that issued the card.

One disadvantage is that if you do not repay your whole balance and you choose to leave some outstanding instead, you will be charged a really high rate of interest on the amount left outstanding.



### Activity 2g

**Look again at the Top Ten tips in Activity 2f above. Can you think of two more disadvantages of store cards?**

## Charge cards

A charge card is used for making payments in a similar way to a credit card, except that you *must* repay the balance in full when the statement arrives.

The main providers of charge cards are American Express and Diners' Club.

## Limits and charges on charge cards

Charge cards have quite high credit limits – and some have no limit at all (although if you were to try to buy a car for £40,000 using a charge card, the retailer would call the card company first for confirmation that you will be able to pay).

Because the balance of a charge card has to be paid in full at the end of the month, it is not a 'rolling credit' type of card like a credit card. You are borrowing the money only for a few weeks – sometimes only for a few days. There is no interest to pay, but there is usually an annual fee.

### Did you know?

The annual fee for an American Express Preferred Rewards Gold charge card is £125 a year from the second year. (It is free for the first year.)

Charge card companies make their money by charging the retailer instead of the customer.

## Advantages and disadvantages of charge cards

One advantage is that you could have no credit limit and yet be able to buy something really expensive with your charge card. For example, if you were to have recently sold your house and still be waiting for the money to come through, you would be able to go out shopping for new things for your new house because you would know that, by the time the charge card statement had come, the money from your recent house sale would be in your bank to repay it.

One disadvantage is that you can borrow the money only for about a month and that you have to repay the balance in full when your statement arrives.

## Prepaid cards

Prepaid cards look like credit and debit cards, and they offer the same ability to purchase products and services, but with a crucial difference: you can spend only the balance that has been preloaded onto the card. This means that there is no risk of running into debt, because the card has no credit or overdraft facility.

Prepaid cards are also used as gift cards, for things such as music or books. They can be bought in many shops and have been preloaded with a set amount.

The benefits of the prepaid card include the following.

- **Availability**

There is no credit check, which means that you can get a card without worrying about your credit history. All prepaid card providers will, however, carry out an identity check to confirm that you are who you say you are.

- **Control**

Prepaid cards are an ideal way in which to budget for yourself or to help to manage your children's spending. Like a credit card, you get a full breakdown of

spending on the card, so you can see what has been purchased, from whom or where, and when.

- **No debt risk**

With a prepaid card, there is no chance of spending too much, because you are limited to the amount that you put on your card.

- **Ease of use abroad**

Prepaid cards are a good option if you are going overseas. They are popular with students going on gap years and children going abroad on school trips, because parents can load them up in the UK. The benefits are not restricted solely to young travellers, of course: any holidaymaker can take advantage, because prepaid cards offer a good alternative to travellers' cheques. They are safe and you will probably be offered a better rate of exchange as you spend.

## Contactless cards

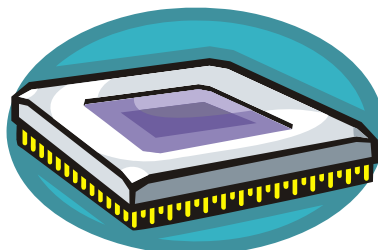
Known as 'wave and pay', or 'tap and go', 'cashless' and 'contactless' cards are a way of paying for everyday items, such as coffee or newspapers, simply by swiping your credit or debit card across a reader. You do not need to use a PIN to authorise a payment, meaning that this type of payment card can be used to speed up the way in which low-value purchases are made.

In the UK, payments of up to £20 can be made without a PIN or signature.

### Did you know?

The big credit card companies each have their own system: Mastercard has PayPass and Visa has PayWave. The contactless chips will be included in debit and credit cards when they are renewed. It is estimated that one in seven UK residents now has a contactless card.

In East Asia, the chip found in a plastic card is placed in an everyday item, such as a mobile phone or a watch. This is then pushed against a sensor to pay in a shop.



Source: BBC News





**How useful do you think it would be to have a contactless payment chip in your mobile phone?**

## Cash cards

Cash cards are plastic cards that account holders can use in branches and ATMs to take cash out of their accounts. Cash cards cannot be used for anything other than getting cash – that is, they cannot be used for buying things in shops. They are often given instead of a debit card to account holders under the age of 18.

## Limits and charges on cash cards

When using a cash card, you are limited to the amount that you have in your current account plus the amount of any overdraft. The only charges made on cash cards are those made for using the card in an ATM that belongs to a bank other than your own – and only some banks make this charge.

## Advantages and disadvantages of cash cards

One advantage of cash cards is that you can use them to get cash out an ATM at any time of the day or night.

One disadvantage is that you cannot use a cash card in shops.



## Activity 2h

**a) Complete the following table to show whether each card can be used for the tasks listed.**

	<b>Can be used to:</b>	<b>Cash card</b>	<b>Debit card</b>	<b>Credit card</b>
1	Take money out of a current account in a bank branch			
2	Borrow money			
3	Withdraw money from an ATM			
4	Pay in a shop			
5	Pay over the Internet			
6	Pay in shops when abroad			
7	Buy now and pay weeks later			
8	Get cash back in some shops			

**b) Which card should the following people use?**

- **Abigail wants to buy clothes and pay from her current account.**
- **Beth wants to buy books and borrow the money for a few weeks.**
- **Dave wants to buy an expensive pair of shoes and spread the cost over a few months.**
- **Erik wants to download music from the Internet and pay straight away.**
- **Fleur wants to get euros while she is in France and pay from her current account.**

	<b>Cash card</b>	<b>Debit card</b>	<b>Credit card</b>
Abigail			
Beth			
Dave			
Erik			
Fleur			



## Review questions

1. When debit cardholders use an ATM to withdraw cash, are they:
  - a) borrowing money?
  - b) taking money from their current account?
2. Can debit cards be used to buy goods and services over the Internet?
3. What is 'cashback'?
4. Can cardholders use their debit cards to pay out more money than they have in their accounts?
5. Do debit cards have expiry dates?
6. When credit cardholders use their cards to withdraw cash from an ATM, are they:
  - a) borrowing money?
  - b) taking money from their current account?
7. When do cardholders pay interest on purchase transactions?
8. Can cardholders use their credit cards to pay out more money than they have?
9. Do credit cards have expiry dates?
10. How do credit and debit cardholders prove who they are when making a purchase over the Internet?

## Learning activities



### Internet

- Visit a selection of credit card issuers, such as [www.amazon.co.uk](http://www.amazon.co.uk), [www.lloydsbank.com](http://www.lloydsbank.com) and [www.co-operativebank.co.uk](http://www.co-operativebank.co.uk), and compare their fees and introductory offers.
- Visit [www.americanexpress.com/uk/](http://www.americanexpress.com/uk/) and select 'Reward cards'. Look at the incentives if you apply for the credit cards. Look at the features of the five charge cards. Is the Platinum card worth an annual fee of £450? Why do the charge cards not quote an interest rate?
- Visit [www.mastercard.co.uk/index.html](http://www.mastercard.co.uk/index.html). Explore the site and look at the section in 'Education' headed 'Choosing a card'. Next, go to 'Products', then 'Credit card issuers' and look at the number of Mastercard issuers. How many of them did you name in Activity 2a?
- Visit [www.theukcardsassociation.org.uk/Advice\\_and\\_links/consumer-advice.asp](http://www.theukcardsassociation.org.uk/Advice_and_links/consumer-advice.asp). Read the advice guide entitled 'Cards: A guide for young people'.



### Group

Using some price comparison websites or providers' websites, draw up a list of some of the many credit cards that are available. Divide up your work, so that you look for those that are 'best buys' for:

- interest rates;
- introductory offers;
- additional products; and
- low fees.



### Individual

Visit some high-street shops and ask for details of their store cards. Pick up some leaflets, if possible, and then draw up a comparison table showing the typical APR and any initial discounts or special offers.



## Key points for Topic 2

You should now understand:

- how to define 'cash card', 'debit card', 'credit card', 'store card', 'charge card', 'prepaid card' and 'contactless card', and be able to list advantages and disadvantages of each;
- what a 'card limit' is;
- different types of charge on cards;
- what the 'interest-free credit period' is;
- what the 'minimum repayment' is and what can happen if you meet only this requirement.