Credit card choice depends on how you use your credit card. If you carry a balance on your credit card, look for a low APR.

Choose the Best Credit Card

By law, credit card companies must tell consumers the interest rate and other costs of using their credit cards. This information is in a disclosure statement and is set up in a table format. You’ll find disclosure statements on credit card applications. If a card offer is made by phone and the card has an annual fee, the caller must verbally give you the disclosure information. If the card has no fee or the fee doesn’t go into effect until the card is used, the caller can mail you the information.

Understand Credit Card Terms

Annual percentage rate (APR) – The annual interest rate that the card issuer charges on the unpaid balance of the credit card. Some credit cards have set rates; for other cards with variable rates the interest rate changes. The disclosure statement gives the guidelines used to decide what the variable interest rates will be. If a credit card offer has an unbelievably low rate, it probably is an introductory rate. After the introductory period is over, the rate will increase. A low rate would be five percent while 21 percent would be high.

Grace period – The length of time you have to pay your bill before interest is charged on the purchases. Most companies offer 20-25 day grace periods. Even though companies have grace periods, most charge interest from the day you make a purchase if you already have a balance on the credit card.

Annual fee – The charge you pay once a year for the right to use a credit card.

Minimum finance charge – The least you’ll have to pay if you have a balance on a credit card, usually two to four percent of the balance.

Transaction fees – Fees you have to pay for cash advances, late payments, or charging over your credit limit.

Periodic rate – The APR divided by 12.

Download other Credit Card Smart fact sheets at: http://uiedev.extension.uiuc.edu/creditcardsmarts/
Analyze the Offers

Issuers of credit cards use different methods to compute the monthly finance charge. Most companies use the average daily balance method to figure finance charges. They add the new purchases to any old debt after the end of the grace period and divide by the number of days in the billing cycle to compute the balance on which you pay interest. Beware of a “two-cycle” average daily balance method. It uses the total of the average daily balances for two billing cycles even if you paid the balance off the previous month. This will be eliminated on June 1, 2010 when the Credit Cardholders’ Bill of Rights Act goes into effect.

Credit card choice depends on how you use your credit card. For example, if you always pay your monthly bill in full, the best type of card is one that has no annual fee and gives you a grace period so you don’t pay interest if you pay your balance each month. If you carry a balance on your credit cards, look for a lower annual percentage rate and the average daily balance method of computing the finance charge.

If you carry a balance on your credit card, use the information below to estimate how much you pay each year to use your credit card. You’ll find your average monthly balance on your credit card statements.

Calculate Finance Charges

Average monthly balance you carry on card _____ x the periodic rate of _____ = interest paid _____ x 12 months = _____ + annual fee (if any) of _____ = Total yearly cost of _____.

(If you get cash advances, pay late, or go over your credit limit, add the transaction fees to your total.)

Example: Average monthly balance of $1250 x periodic rate of 1.5% (1250 x .015) = interest paid $18.75 x 12 months = $225 + annual fee (if any) of $20 = Total yearly cost of $245.