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Loans

Do you ever borrow money? Where can you borrow money? Is borrowing money a good idea?

Sometimes people need large amounts of money to pay for things they need. Cars, houses, and a college education cost thousands of dollars. Or they might need money for a new washing machine or a lawnmower. When you borrow money, you get a loan. A loan lets you buy things that you cannot pay for all at once. Using a credit card is one form of a loan.

You might get a loan from a friend or family member. This can cause stress on your friendship or family relationship. There are also people or businesses that make loans to people. They often charge high interest rates. That can make the cost of a loan very expensive. Another option is a bank loan. Banks will loan money to people if the people seem likely to pay back the loan.

Words to know:

- loan
- credit risk
- interest
- cosigner
How does it work?

To get a bank loan, you must fill out an application. The bank will check the information you give. It must make sure you are a good credit risk. That means it is likely you will pay back the money you borrow. You must make enough money to pay back the loan. It also means that you pay your bills on time each month.

When you borrow money, you pay interest. Interest is the cost of using someone else’s money. Bank loans, like credit cards, have an interest fee. The interest fee is based on how much money you owe.

Example: If you borrow $1,000.00 at 5% interest a year, you must pay back:

\[
\begin{align*}
$1,000.00 & \quad $1,000.00 \\
\times 0.05 & \quad + \quad 50.00 \\
$50.0000 & \quad $1,050.00 = \text{total loan cost if paid in one year.}
\end{align*}
\]

If you pay off the loan in two years, here is what happens. After one year, your new loan amount is $1,050.00. In the second year, 5% interest will be added to that amount.

\[
\begin{align*}
$1,050.00 & \quad $1,050.00 \\
\times 0.05 & \quad + \quad 52.50 \\
$52.5000 & \quad $1,102.50 = \text{total loan cost at the end of two years.}
\end{align*}
\]

Each month, you must pay back a part of money you owe plus the interest fee. Your payment must reach the bank by the due date they set. It must be on time. If you do not pay on time, you will be charged a late fee. That will increase the amount of money you owe.
Bank loans help people get expensive things they need. However, they may take years to repay. Look carefully at this example of a bank loan application. Use it to answer the questions that follow.

<table>
<thead>
<tr>
<th>Consumer Loan Application</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>What type of loan are you applying for?</strong> ______________________, for a term of ___________ months.</td>
</tr>
<tr>
<td><strong>Amount requested</strong> ___________ for the purpose of ________________</td>
</tr>
</tbody>
</table>

**Applicant**

Name (First, M.I., Last)  
Social Security Number  
Date of Birth  
Address  
County  
City  
State  
Zip Code  
Home Phone  
Previous Address (if less than 1 year)  
City  
State  
Zip Code

**Employment**

Employer’s Name  
Self Employed  
☑ Yes  ☐ No  
Address  
Phone Number  
Occupation (Job)  
☐ Full Time  
☐ Part Time  
How Long  
Yrs. / Mos.  
Gross Salary/Income  
________________every__________ (week, two weeks, month, or year)  
Previous Job (if less than 3 years)  
How long

**Other Sources of Income (second job, pension, rental income, etc.)**

Monthly Amount $  
Source  
Monthly Amount $  
Source

**Nearest Relative**

Name (First, M.I., Last)  
Relationship  
Address  
Phone
Bank Accounts

Checking with

Savings with

Financial Information. List all loans, credit cards, etc.

<table>
<thead>
<tr>
<th>Creditor</th>
<th>Purpose</th>
<th>Monthly Payments</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

IMPORTANT: READ BEFORE SIGNING

I promise that the statements contained herein are true and complete to the best of my knowledge. I understand the lender (the Bank) will keep this application whether approved or declined. I allow the Bank to check my credit and employment history and to answer questions from others about its credit experience with me. The Bank may request a credit report in connection with this application for credit and any credit update, renewal, or extension of this credit. Upon request, the Bank will tell me whether or not a consumer report was obtained, and if such a report was obtained, the Bank will furnish me with the name and address of the consumer reporting agency furnishing the report.

________________________________________  ______________________
Applicant Signature                      Date

1. List three kinds of financial information you must provide on a loan application.
   a. ____________________________________________
   b. ____________________________________________
   c. ____________________________________________

2. The application asks how long you have lived at your address. It also asks how long you have had your job. Why do you think the bank wants this information?
   ____________________________________________
   ____________________________________________
   ____________________________________________
Questions to Ask Before Getting a Loan

Each loan will have different interest rates and rules. If possible, check with more than one bank about a loan. Ask questions before you make a decision. Then choose the bank that offers the best loan to fit your needs. These questions might help you:

- How much income do I need to get the loan?
- How much interest will I have to pay?
- When will I have to start making payments?
- How many payments will I have to make?
- What will my monthly payment amount be?
- How much is the late fee?
- When will I have to pay a late fee?

What is a Cosigner?

Sometimes a bank will not give you a loan. You might get the loan if you have a cosigner. A cosigner agrees to repay your loan to the bank if you cannot. A cosigner promises to make your monthly loan payments to the bank if you cannot.

Should You Cosign a Loan for Someone Else?

Think very carefully before you cosign a loan for someone. If you cosign a loan, you could become responsible for paying it back.

What Do You Think?

3. Which of the following is not a good reason to borrow money?
   a. You need a car to get to work.
   b. You need to pay college tuition.
   c. You want to buy a diamond ring.
4. When taking out a loan you should think about:
   a. Whether you really need to borrow money.
   b. How much you need to borrow.
   c. Whether the monthly payments will fit in your budget.
   d. All of the above.

5. A friend asks you to cosign a loan. The friend has had three different jobs in the past two months. He wants to use the loan to buy a $20,000 truck. Do you think you should cosign the loan? Why or why not?

________________________________________________________________
________________________________________________________________
________________________________________________________________

6. Explain why cosigning a loan might be a problem for you.

________________________________________________________________
________________________________________________________________
________________________________________________________________

7. Pedro is thinking about borrowing money from the bank to buy a new car. What questions should he ask before he signs the loan contract?

________________________________________________________________
________________________________________________________________
________________________________________________________________

End of Lesson 5

Unit 4 - Financial Literacy