

SMALL FARMS RESEARCH CENTER FACTSHEET

COLLEGE OF AGRICULTURAL, LIFE AND NATURAL SCIENCES



United States Department of Agriculture

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Debit Cards vs. Credit Cards

Learn about the important differences and when to use each.

In the wake of the recession and the economic uncertainty that has come with it, many Americans have cut back on their spending and also made a greater effort to limit or reduce their credit card debt.

A logical way to do this is to use a debit card more often instead of a credit card. Using a debit card, you are only spending money you actually have in your bank account, not building up further debt that will saddle you with higher finance charges. This is especially appealing as credit card issuers raise interest rates, or lower credit limits, in an uncertain credit environment.

But it's important to keep in mind the differences between credit and debit cards. They look alike—most debit cards are now branded with Visa or MasterCard—and mostly function alike. But debit cards generally don't offer as much protection to the consumer as do credit cards.

The most important difference is the liability incurred by the cardholder when the card is lost. For a credit card, this liability is limited by law to \$50, and you have 60 days to make a claim in writing to your credit card company. For a debit card, your liability is limited to \$50 only for the first 2 days, and after that goes up to \$500. After 60 days, you are liable for the full balance in your account. In some cases, this loss can be devastating and lead to other consequences, such as credit defaults that will impair your credit rating. Some banks are voluntarily limiting liability on debit cards, but this is not a legal obligation.

There are other disadvantages to debit cards, stemming from the fact that it is your own money that is involved in the transaction. For instance, if you have a dispute with a merchant, you may lose access to your money, which remains in the merchant's possession, until the matter is resolved.

For many people, it can be difficult to keep track of their account balance, because, unlike with checks, there's no place to record debit card transactions and carry forward the new balance. If you make a charge that exceeds your available balance, your bank may impose an overdraft fee instead of simply declining the charge. This scenario has led to stories about people paying a \$30 fee for buying a \$3.50 cup of coffee.



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Even with the availability of balance checks at an ATM machine or online, frequent use of a debit card runs the risk of losing track of your account balance—especially if you have a joint checking account and your husband or wife also has a debit card on the same account.

Trying to rent a car or register at a hotel with a debit card can lead to other pitfalls. Often, debit cards simply are not accepted for these purposes. Or, if they are, the merchant will place a hold on the money in your account and it won't be available to you. Then you find yourself easily incurring an overdraft fee when you draw on your account for other purposes. Hotels, especially, will often place a hold on the total amount of your anticipated bill which includes room charges for the length of your stay, plus a small incidentals fee, at the time of your check-in.

There are advantages to using credit cards that debit cards simply don't have. Chief among these is building a positive credit history. Responsible use of a credit card account can improve your credit score, which is becoming more important in a tight credit environment. Here, oddly enough, you are better off carrying a balance rather than paying off your credit card in full every month—you have to have credit in order to develop a credit history.

Even to the extent you pay off or pay down the credit card balance, you have profited from the “float” you got between the time you made the purchase and the time you pay your bill, which can sometimes be a month or longer. You've had free use of this money during that time, unlike when you use a debit card to immediately withdraw money from your account.

Credit cards have evolved to include other protections and services. For instance, a large purchase that is delivered to your home will often benefit from insurance in case of damage during delivery. Many credit card programs carry automatic travel or car insurance when the card is used to buy airline tickets or rent cars.

Plus, most credit cards now carry reward points for purchases, which can be redeemed for travel or other products and services. Debit cards rarely have a rewards program. Of course, you may “pay” for these rewards by way of an annual fee, but the protections offered by a credit card and the rewards often make this a worthwhile expense.

It's no accident that credit cards are more enticing than debit cards—they are much more profitable for the banks. They earn money from the high interest rates on balances, from the increasingly high interchange or “swipe” fees they charge merchants, and from the onerous penalty rates they often impose.

Before using either credit or debit cards, keep in mind the differences between them and use each type of card appropriately.

Reference: [http:// www.credit.com](http://www.credit.com)



Cooperating Units: USDA Office of Advocacy and Outreach (OAO), USDA/NIFA/ Beginning Farmers and Ranchers Development Program (BFRDP), USDA/OAO/Outreach Assistance for Socially Disadvantaged Farmers and Ranchers (OASDFR) Program, Alabama Cooperative Extension Systems, and Alabama A&M University.

