

Debit vs. Credit... Are they the Same?



Even though debit cards and credit cards look alike, they are very different.

What is a Debit Card?

The purchases that you make using a debit card come directly from a checking account that you open at a local financial institution (such as a bank or credit union).

Although debit cards have a logo (i.e. Visa or MasterCard), a debit card is not a loan and does not have the same influence as a credit card in building your credit history. Because debit card transactions come directly from your account, you must have the funds in your account to use it.

What is a Credit Card?

Credit cards are an open-ended and unsecured loan that you will have to pay back. You can open a credit card from your local financial institution, department stores, or directly from credit card issuers. Because credit cards are revolving accounts, you can carry a balance, should you choose not to pay your balance in full each month. Credit cards are not tied to an account at a local financial institution and you can incur interest and fees on any unpaid balances. Credit cards have a logo and can help build credit if managed appropriately. If you are trying to build your credit score, try not to charge more than 20%-30% of your approved limit and pay your bills on time.

What happens when you swipe a debit card and select debit?

- Payment comes directly from your checking account.
- The retailer will ask you to enter a 4 digit Personal Identification Number to process the payment. When this happens, your bank or credit union account decreases immediately.
- Local stores prefer that you select debit because it is a less expensive option for them, but you need to be aware that you are opening yourself up to greater risk and liability if identity theft occurs. Debit cards are protected by law through the Electronic Funds Transfer Act and if a card is reported as lost within two business days, you are liable up to \$50; if reported within 60 days, the liability for loss is \$500; and after 60 days, the liability for loss is unlimited.
- There may be rewards offered for using a debit card. Check with your financial institution on what rewards, if any, they offer for use.
- Debit cards may have a limit per day for the total amount of transactions that can be made and may limit the amount of the transactions you may make. Check with your financial institution what limits may exist for your card.
- By using a debit card, you can get cash back from some retailers in addition to any purchases you make because the funds are coming directly from your account. There are sometimes fees associated with this process.

- When using a debit card at a gas station, you may experience a hold on your account until the transaction clears (up to 3 days). This amount could range from \$1.00 up to double the amount of your gas purchase. Contact the gas station for more details.

What happens when you swipe a debit card and choose credit?

- Payment still comes directly from your checking account.
- Retailers will sometimes require you to sign your name to authorize the payment to take place (no Personal Identification Number will need to be entered).
- Your bank or credit union checking account may or may not decrease immediately. Check with your local financial institution for their policy.
- Debit card purchases will “hit” or clear your account at varying times. This is often contingent on when merchants batch and submit their daily transactions (i.e. this could be hourly or once a day) and may be delayed even more by choosing the credit option. Remember to balance your account on a regular basis and compare with your monthly account statement.
- When using a debit card at a gas station, you may experience a hold on your account until the transaction clears (up to three days). This amount could range from \$1.00 up to double the amount of your gas purchase. Contact the local retailer for more details.
- Similarly, when using a debit card for payment of services like a car rental, the merchant will generally place a hold on your account for the entire amount of the rental for the length of the agreement. This can require a card holder to carry a much higher balance in their checking account during the rental period so that funds may be available for purchases above the held amount. This can tie up hundreds of dollars depending on your rental or service agreement.
- The liability for loss is the same as if you were using the debit card as a debit card. Debit cards are protected by law through the Electronic Funds Transfer Act and if a card is reported as lost within two business days, you are liable up to \$50; if reported within 60 days, the liability for loss is \$500; and after 60 days, the liability for loss is unlimited.



What happens when you use an actual credit card?

- The funds to pay for the purchase will come directly from the card issuer. Each credit card has an approved maximum limit that you can use to pay for goods and services. This limit has been granted to you by the card issuer when you signed the credit card agreement.
- When making a purchase using a credit card, you will always select credit and be asked to sign your name to authorize the payment. It is important to review all communications from your card issuer so you understand the policies and fees associated with the use of this card.
- Once the transaction takes place, the issuer is notified and your approved limit decreases

immediately. Transactions may not show up immediately on your credit card statement until it has cleared.

- Charges will apply (interest) if you carry a balance or your card offers no grace period and you incur interest charges. Fees and penalties can be imposed. It is important to read the credit card agreement.
- Overspending can occur, since the credit limit may be higher than the amount that you can afford.
- The local retailer may pay more in transaction fees when you use credit. However, the liability for loss in instances of identity theft when using a credit card is covered by the Truth in Lending Act. There is no liability for loss if reported in two business days; after two business days, your liability for loss is only up to \$50.
- The card issuer may offer “rewards” for the use of credit; check with your card issuer.
- Some credit cards will have a cash back option. Contact your card issuer to find out the APR (i.e. interest and fees) that is associated with this service.
- If you “max out” your credit card or charge your entire available limit, this may affect your credit score negatively.
- Some credit cards may allow you to make purchases that exceed your approved limit, for a fee. Be sure to read and understand all terms and conditions in your card holder agreement.
- Some credit cards offer “no interest” or “low interest” introductory offers. Make note of when these offers end, and what your new interest rate will be. Be sure to read and understand all terms and conditions in your card holder agreement.



References

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