

Credit Cards

“Comparing costs and benefits of buying on credit is key to making a good purchase decision.”

— *Spending and Credit Standards*,
JumpStart Coalition Benchmarks



Teacher Background

Looking at statistics one might easily say that the United States is a nation of credit card holders. In 2001, 185 million consumers held one or more credit cards, the national credit card debt was \$660 billion, and the average debt per household, \$8,400.* Each year a growing number of individuals file bankruptcy, in part because of their credit card debt, and in 2002, 1,508,578 filed (up 7.8% from 2001).** Another fact of a different magnitude is that one man in the U.S. made the *Guinness Book of World Records* by acquiring 1,358 different credit cards.

Advantages

Credit cards offer consumers a myriad of advantages including the convenience of making purchases online, shopping now and paying over an extended period of time, and gaining access to goods and services in almost every country in the world. Many credit cards even offer the advantage of frequent flier airline miles or a charitable contribution made in the name of the cardholder each time a purchase is made. A credit card purchase could help a college alumni association, the Sierra Club, or a religious group. There are cards to meet the needs of everyone, including secured credit cards for those who have been turned down for a card without a security deposit.

Costs and Benefits

In this lesson students will analyze the costs and benefits of credit card purchases. They will complete a comparison shopping activity for credit cards that will prove that not all cards are created equal. They will be able to explain interest (APR) and describe how the longer people take to pay off balances, the more expensive the goods and services they purchased. One activity in this lesson provides an opportunity for students to calculate the amount of interest and fees that cardholders could pay for an item. Students will understand that credit card purchases can be far more expensive than they thought.

*www.cardweb.com/cardlearn/stat.html

**www.uscourts.gov/Press_Releases/FYBY1.pdf

Student Objectives

- ▶ Students will be able to compare and list the differences among four credit cards (i.e., fees, interest, credit limit).
- ▶ Students will be able to identify and provide examples of the costs and benefits of credit card use.
- ▶ Students will be able to analyze potential pitfalls of credit card use for college students and other young adults.
- ▶ Students will be able to calculate the annual percentage rate (APR) and fees on a credit card.



- ☞ How do credit cards work for consumers?

Vocabulary

annual fee

A charge by some credit card companies for use of the card and services.

annual percentage rate (APR)

A rate that shows the total cost of credit annually. It includes a percentage of the principal as interest on a loan plus other costs (e.g., points on a mortgage loan, service charges).

consumer debt

Debt that has been incurred primarily for the purchase of consumer goods.

credit card

A plastic card with a magnetic stripe on one side that can be used to purchase goods and services. The issuing company records the purchases, bills the purchaser, receives payment, and subsequently settles the purchaser's debts with the providers of goods and services. The card can also be used to transact bank business (e.g., withdrawing funds from one's checking account). Some credit cards offer cash advances to its holders.

credit rating

A formal evaluation of an individual's or business' credit history and capability of repaying obligations by a credit reporting agency. The credit rating is based on the number of outstanding debts and whether debts are being repaid in a timely manner.

credit score

Numeric value compiled from information in a credit report using a standardized formula that

Connections to Content Standards

NCEE Voluntary National Content Standards in Economics: 1, 2, and 7

Jump\$tart Coalition Personal Financial Management Guidelines: IIa, IIb, IIIa, and IIIb

ranks the risk of default according to the person's credit history. A score is based on past payment history, the amount of credit available, and other factors. Scores range from 300 to 850. Scores under 620 make obtaining loans with good terms difficult.

disclosure statement

The release or reporting of relevant information.

due date

On a credit card account, the date by which the minimum payment must be received every month, without incurring a late fee or other penalty.

finance charge

The cost of credit, including interest paid by a customer or a consumer for a consumer loan or credit. Under the Truth in Lending Act, the finance charge must be disclosed to the customer in writing. It may include other charges associated with credit transactions such as cash advance fees.

grace period

The time allowed by law for payment of an amount due.

installment plan

A sum of money due as one of several equal payments for a purchase spread over an agreed period of time.

minimum payment

On a credit card account or loan, a fixed percentage of the balance due which must be paid each month (e.g., 2% or 3%).

overlimit fee

A fee that is added to a credit account when the amount owed exceeds the limit on the account.

reloadable card

An electronic, stored value card that permits a user to increase the value on the card (e.g., prepaid credit card, store cash card). A ***nonreloadable card*** has a fixed value stored on it (e.g., disposable phone card).

revolving credit

System of retail credit (e.g., department store or bank credit cards) in which buyers make periodic payments on purchases and service charges. The service charge is based on the outstanding balance; if the buyer pays the entire balance, no service charge accrues.

secured credit card

A credit card that is secured against loss by other assets (often by money placed in a savings account with the credit card company).


Materials Needed

- ✓ Student Handout 11-A, *To Market, To Market: Comparison Shopping for a Credit Card*
- ✓ Student Handout 11-B, *Calculating the Cost of Credit Card Purchases*
- ✓ Credit card marketing materials (especially those targeting college students and young adults). To acquire brochures:
 - From Citigroup:*
 - “Money Matters for Young Adults” — (800) 669-2635
 - “College Guide to Personal Money Management” — (800) 833-9666
 - From Visa:*
 - “Knowledge Pay\$ and the “Inform” series — (888) 847-2606
- ✓ Credit card application forms, sample credit card statements


Connecting with the Internet

 www.bankrate.com

Bankrate.com. At this site comparisons can be made among the various interest rates and fees that are offered by credit card companies.

 www.ftc.gov/bcp/con-line/pubs/credit/choose.htm


Choosing and Using Credit Cards. The Federal Trade Commission (FTC) offers tips on shopping around for credit cards on this webpage.

 www.creditcardnation.com/legislation.html

Credit Card Nation. Provides a listing of federal and state legislation that seeks to regulate or to study regulation of credit cards.

 www.credittalk.com

Credit Talk. Developed by Mastercard International and Debt Counselors of America. A website on credit for young adults.

 www.collegeparents.org/partnersMasterCard.html

Money Talks. This is an educational program for parents of high school- and college-age students developed by Mastercard International and College Parents of America.

 www.ncsl.org/programs/lis/credcard.htm

National Conference of State Legislators (NCSL). Included on the Credit Cards & College Students page are news briefs, studies, and links to legislation regarding solicitation on college campuses.

 www.studentcredit.com/learn.htm

StudentCredit.com. Students can visit this website to learn how credit cards work and how to manage them properly.

Procedures



1 Ask students to imagine how it is possible to buy something they really want in person (or electronically) without using money they have today (i.e., it is all about credit). Distribute and/or post advertisements and brochures about credit cards. Provide students time to go online and connect with some of the suggested websites, if computer access is available. Ask students to read the information and list what credit cards are offering to consumers. They will need this information later in the lesson to complete a “comparison shopping trip” for a credit card.

In small groups, have students discuss ways that credit card companies target or attract certain consumers (i.e., college students and young adults). Have a student from each group report to the class. Ask students to also describe any personal experience they have had with credit cards.

2 Have students work in the same groups to discuss and list possible advantages or disadvantages of having a credit card. A composite list of advantages and disadvantages should be written on the board. A sample student list could include:

Advantages of Using Credit Cards

- Buy clothes now and enjoy while still paying for them.
- Establish a credit rating.
- Obtain cash advances when broke.
- Rent sports equipment, videos, DVDs and other things that require a credit card.
- Help out with emergencies.
- Enjoy a sense of having money to spend (i.e., well being).
- Earn special bonuses like airline frequent flyer mileage when used for purchases.
- Be able to act on the spur of the moment without money.
- Easily buy tickets to events (over the phone and via the Internet).

Disadvantages of Using Credit Cards

- Paying more for a product or service (if balance is not paid off on time).
- Paying large finance or interest charges.
- Being tempted to spend too much (i.e., living beyond one’s income).
- Suffering the stress of making payments.
- Paying off cards can become a huge financial burden.
- Paying for purchases continues even after they are worn out or gone.
- Cards can become a nightmare if stolen or lost.
- They can make it “too easy” to shop.
- Using one card to pay off another card (i.e., downward spiral).
- Minimum payments can mean years to pay off the balance on some accounts.
- Credit card companies may charge a fee just for having the card.

3 Ask students to discuss the trade-offs involved in credit card use and the responsibility of the card holder. Describe how the first responsibility for people considering the use of credit cards is to do some comparison shopping (i.e., analyzing fees, interest rates, credit limit, etc.), Distribute Student Handout 11-A, *To Market to Market — Comparison Shopping for a Credit Card*. Students will complete the handout using the brochures and advertisements or by going online to various bank sites that offer credit cards. This can be assigned to a small group or individuals.

4 Read the directions on Student Handout 11-A and review any words on the comparison chart they do not understand. Have the students report back their findings. Students might post their charts for review by others in the class. Ask what major differences they discovered from one credit card to another. Discuss the importance of reading the small print to determine the rate of interest, annual fees, and overlimit fees that are included.

5 Distribute Student Handout 11-B, *Calculating the Cost of Credit Card Purchases*, and ask students to calculate what this cardholder will have paid in interest and fees at the end of one year. Review the directions that follow.

Use the interest rate of 18% and annual fee of \$49 to complete this chart. In Month 1, there was a balance due of \$3,000. The borrower will make a monthly payment of \$200 and keep new purchases of goods and services at \$115 per month. Calculate the interest for each month (balance x 1.5%). To obtain the balance for the next month, *subtract* the payment from the balance and *add* cost of new purchases plus monthly interest and fee. For example: $\$3,000 - \$200 = \$2,800 + \$115 + \$94 = \$3,009$. (NOTE: The annual fee is paid only once per year.)

6 Organize students to review and check each other's calculations on the cost of credit card purchases (Student Handout 11-B). Review that there are costs and benefits to credit card transactions. The cost to the consumer illustrated on the handout is \$555.91 (cumulative interest and fees for one year). At the end of the year, the balance in that credit card account is approximately \$2,572. (See page 97 for calculations.)

Encourage students to make further calculations. For example, after Month 6, they could choose higher monthly payments and/or fewer purchases, and compare results.

7 Summarize the lesson by having each student participate in reviewing the advantages and disadvantages of credit card use. Also review with students the importance of consumers “shopping for credit cards” by analyzing interest rates, fees, and credit limits.



Calculating the Cost of Credit Card Purchases
(Answer Key to Student Handout 11-B)

Month	Balance	Payments	Purchases	Interest & Fee	Interest & Fee (Cumulative)
1	\$3,000	\$200	\$115	\$49 \$45	\$94
2	\$3,009	\$200	\$115	\$45.14	\$139.14
3	\$2,969.14	\$200	\$115	\$44.54	\$183.68
4	\$2,928.68	\$200	\$115	\$43.93	\$227.61
5	\$2,887.61	\$200	\$115	\$43.31	\$270.92
6	\$2,845.92	\$200	\$115	\$42.69	\$313.61
7	\$2,803.61	\$200	\$115	\$42.05	\$355.66
8	\$2,760.66	\$200	\$115	\$41.41	\$397.07
9	\$2,717.07	\$200	\$115	\$40.76	\$437.83
10	\$2,672.83	\$200	\$115	\$40.09	\$477.92
11	\$2,627.92	\$200	\$115	\$39.42	\$517.34
12	\$2,572.34	\$200	\$115	\$35.59	\$555.93

**EXTENDING
THE LESSON**

- Students research and write reports on college students and credit card debt. Ask students to consider the issues related to credit card companies providing cards to young adults (college students without the income to repay the amount they charge). Credit Card Nation (www.creditcardnation.com) is a site where students can begin their research. Students report their findings to the class.
- Students compare rates and fees on various “secured” credit cards. They should describe and report on the costs and benefits of secured credit cards. Ask students to list reasons why a consumer might apply for a secured credit card.
- Students research and develop graphs to show consumer debt as a percentage of disposable income over the last twenty years. Consumer debt includes installment purchases, credit card debts, and all loans except mortgages. Ask students to evaluate any changes in consumer debt. Students may begin their research at the Federal Reserve Board of Governors website (www.federalreserve.gov). Students write a report and give a presentation to the class using visuals such as charts, graphs, and PowerPoint.

Student Handout 11-A

TOPIC 4: Credit—A Matter of Trust

Name of Student _____

To Market, To Market

Comparison Shopping for a Credit Card



Directions

Read credit card brochures and disclosure statements, make phone calls, or go online to compare credit card offers. A good rule is always to *compare* four or more credit cards before applying for one.

- ☛ Be sure to read all the small print on brochures or disclosure statements before you complete the chart.

Credit Card (Name of Company)	Sponsoring Organization	Annual Fee	Credit Limit (if listed)	APR	Minimum Payment	Grace Period
<i>Examples:</i> Citibank Visa Capital One Mastercard	<i>Examples:</i> National Wildlife Federation Working Assets United Airlines					
1.						
2.						
3.						
4.						

Student Handout 11-B

TOPIC 4: Credit—A Matter of Trust

Name of Student _____

Calculating the Cost of Credit Card Purchases



Directions

Use the interest rate of 18% and an annual fee of \$49 to complete this chart. In Month 1, there was a balance due of \$3,000. The borrower will make a monthly payment of \$200 and keep new purchases of goods and services at \$115 per month for the year.

Calculate the interest for each month (balance x 1.5%). To obtain the balance for the next month, *subtract* the payment from the balance and *add* cost of new purchases plus monthly interest and fee. For example: $\$3,000 - \$200 = \$2800 + \$115 + \$94 = \$3,009$. (NOTE: The annual fee of \$49 is paid only once.)

Interest rate: **18%** (APR); **1.5%** monthly

Annual fee: **\$49**

Month	Balance	Payments	Purchases	Interest & Fee	Interest & Fee (Cumulative)
1	\$3,000	\$200	\$115	\$49 \$45	\$94
2	\$3,009	\$200	\$115	\$45.14	\$139.14
3	\$2,969.14				
4					
5					
6					
7					
8					
9					
10					
11					
12					

Notes