

Shopping for a Credit Card

LESSON DESCRIPTION AND BACKGROUND

According to a report published in May 2018 by the Federal Reserve*, consumer credit in the United States has reached an all-time high of almost \$4 trillion. Revolving credit, which is primarily credit cards, is \$1.4 trillion—meaning that credit card debt accounted for over one-third of all household debt. That same report showed that 83 percent of adults in the US have at least one credit card. Of those with credit cards, over 90 percent have more than one card. About half of all credit card users have a revolving balance on one or more of their cards, while the other half pay them off each month.

Using credit cards has become a widely accepted practice throughout our economy; however, they are also the source of financial distress for people who overuse or abuse them. This lesson is designed to help students make informed choices when choosing and using credit cards. It explains the key concepts associated with credit cards as well as the basic components of a credit card statement.

ECONOMIC AND PERSONAL FINANCE CONCEPTS

- Credit
- Interest

NATIONAL STANDARDS FOR FINANCIAL LITERACY

- **Standard 4 Using Credit, Grade 12, Benchmark 1** – Consumers can compare the cost of credit using the annual percentage rate (APR), initial fees charged, and fees charged for late payment or missed payments.

COMMON CORE STATE STANDARDS

- **CCSS.MATH.Content.HSA.SSE.B.4** – Derive the formula for the sum of a finite geometric series (when the common ratio is not 1), and use the formula to solve problems.
- **CCSS.MATH.Content.HSF.LE.B.5** – Interpret the parameters in a linear or exponential function in terms of a context.
- **CCSS.ELA-Literacy.CCRA.R.10** – Read and comprehend complex literary and informational texts independently and proficiently.
- **CCSS.ELA-Literacy.W.9-10.7, CCSS.ELA-Literacy.W.11-12.7** – Conduct short as well as more sustained research projects to answer a question (including a self-generated question) or solve a problem; narrow or broaden the inquiry when appropriate; synthesize multiple sources on the subject, demonstrating understanding of the subject under investigation.
- **CCSS.ELA-Literacy.W.9-10.9, CCSS.ELA-Literacy.W.11-12.9** – Draw evidence from literary or informational texts to support analysis, reflection, and research.
- **CCSS.ELA-Literacy.L.9-10.6; CCSS.ELA-Literacy.L.11-12.6** – Acquire and use accurately general academic and domain-specific words and phrases, sufficient for reading, writing, speaking, and listening at the college and career readiness level; demonstrate independence in gathering vocabulary knowledge when considering a word or phrase important to comprehension or expression.
- **CCSS.ELA-Literacy.RH.11-12.2** – Determine the central ideas or information of a primary or secondary source; provide an accurate summary that makes clear the relationships among the key details and ideas.

* Report on the Economic Well-Being of U.S. Households in 2017—Federal Reserve Report issued May, 20, 2018.
<https://www.federalreserve.gov/newsevents/pressreleases/other20180522a.htm>

- **CCSS.ELA-Literacy.RH.11-12.9** – Integrate information from diverse sources, both primary and secondary, into a coherent understanding of an idea or event, noting discrepancies among sources.

OBJECTIVES

The student will

- describe differences among credit cards, including fees, annual percentage rates, grace periods, and credit limits.
- describe the information included on a credit card statement.
- evaluate the costs and benefits of using a credit card to purchase goods and services.

TIME REQUIRED

Two or three 45-minute class periods

MATERIALS

- **Slides 15.1–15.3**
- **Exercise 15.1: Comparing Credit Cards**, one copy per student
- **Exercise 15.2: Calculating Your Interest Rate**, one copy per student
- **Exercise 15.3: Reading Your Credit Card Statement**, one copy per student
- Copies of three credit card offers for small groups
- One sheet of blank paper for each student

ADDITIONAL RESOURCES

Visit <https://www.econedlink.org/resources/collection/fffl-9-12/> to find presentations, interactives and other great technology tools to enhance your teaching of this lesson.

PROCEDURE

1. Ask students the following questions.

- a. How many of you have a credit card? **(Answers will vary. If no students have credit cards, ask whether they know people who do.)**

- b. What do you buy with your credit card? **(Answers may include such things as gas, clothing, fast food, cell phone accessories, music downloads, and other internet purchases.)**
- c. Why do people use credit cards? **(Answers may include convenience, safer than carrying cash, lack of funds for making the purchase, etc.)**
- d. What is the interest rate on your credit card? **(Answers will vary, but most students will probably not know the answer. The average interest rate varies but tends to be about 15-18 percent.)**
- e. Why is the interest rate important? **(Higher interest rates mean higher payments and higher actual purchase prices for goods and services if the total amount is not paid each month.)**

2. Explain that people get credit cards for many different reasons and that credit cards have different features, such as different interest rates and special promotions. For example, people who travel frequently may find credit cards to be more convenient than other forms of payment and they provide a record of all purchases. Others may prefer the security of using them online while other users may want to build points for airline purchases. Remind students that credit cards are not cash; they are short-term loans that must be repaid with interest. Using credit cards can have many benefits, but they also can cause financial problems for people who charge more than they can repay.

3. Give each student a copy of **Exercise 15.1: Comparing Credit Cards**. Ask the students to read the exercise and work in small groups to complete the activity in Part 4. (Note: You will need to access credit card offers either from a local bank or downloaded from a reliable source such as <https://www.bankrate.com/credit-cards/>.) Review the answers to the questions in the activity.

- a. What characteristics would you look for if you carried a balance and wanted to save money on a credit card? **(Low APR, no annual fee, other fees.)**

b. What features would you look for if you planned to pay off your balance each month? (**Long grace period, rewards for use, no annual fee.**)

c. Which card would your group choose? (**Accept a variety of reasonable answers.**)

4. Remind students that **Exercise 15.1** described the basic features of a credit card. Tell students that they will watch a short video to help them understand how credit card interest is calculated. Ask them to focus on the following questions.

a. Why do you divide the APR by 365? (**To get the average daily balance.**)

b. Why would your average daily balance change during a one month period of time? (**It changes whenever you make a payment.**)

c. How can you reduce the amount you pay in interest each month? (**Pay your bill in full; increase your monthly payment; get a card with a lower interest rate.**)

5. Show the credit card video at <https://youtu.be/BoyrMi7pNSo>. To follow up, use the information in **Slides 15.1–15.3** which outline the information presented in the video. Discuss with students to see if they have additional questions. Remind them other methods may be used to calculate interest, but this one is the norm for the credit card industry.

6. Distribute a copy of **Exercise 15.2: Calculating Your Interest Rate** to each student. Have students complete the exercise. You may choose to have them work in small groups. Review the steps and answers before continuing. (**Answer: $19\%/365 = .00052$; $\$1,000 \times 10 = \$10,000$; $\$1,500 \times 20 = \$30,000$; $\$40,000/30 = \$1,333.33$; $\$1,333.33 \times .00052 \times 30 = \20.80 in interest.**)

7. Tell students that reading and understanding their monthly credit card statement is part of the responsibility of having a credit card. Explain that it provides a summary of their account activity for the past month as well as other information about their account. Distribute a

copy of **Exercise 15.3: Reading Your Credit Card Statement** to each student. Use the following web site to show students how to read the information on their monthly statements and define the terms in the activity: <https://www.mycreditunion.gov/Pages/pocket-cents-understanding-credit-card-statement.aspx>.

8. Review the following terms with students before they complete Section 2 of the exercise.

a. Summary of account activity (A summary of the transactions on your account—your payments, credits, purchases, balance transfers, cash advances, fees, interest charges, and amounts past due. It will also show your new balance, available credit and the last day of the billing period).

b. Payment information (Your total new balance, the minimum payment amount and the date your payment is due. A payment generally is considered on time if received by 5 p.m. on the day it is due.)

c. Late payment warning (Any additional fees or higher interest rates that may be charged if your payment is late.)

d. Minimum payment warning (An estimate of how long it can take to pay off your balance if you make only minimum payments. Also estimates of how much you likely will pay, including interest, to pay off your bill in three years, assuming you have no additional charges.)

e. Notice of changes to your interest rates (Interest rates may increase if you trigger the penalty rate by exceeding your credit limit or making late payments. The credit card company must tell you at least 45 days before your rates change.)

f. Other changes to your account terms (If your credit card company is going to raise interest rates or fees or make other significant changes to your account, it must notify you at least 45 days before the changes take effect.)

g. Transactions (A list of all the transactions that have occurred since your last statement, such as purchases, payments, credits, cash advances, and balance transfers.)

- h. Fees and interest charges (Credit card companies must list the fees and interest charges separately on your monthly bill. Interest charges must be listed by type of transaction).
- i. Year-to-date totals (The total that you have paid in fees and interest charges for the current year.)
- j. Interest charge calculation (A summary of the interest rates on the different types of transactions, account balances, the amount of each, and the interest charged for each type of transaction.)
9. After reviewing these terms, have students complete Part 2 and discuss their answers. Ask students if they have additional questions about the credit card statement or terms. Remind them it is important to review their statement each month.
- a. How much did Teresa Torres charge on her credit card in October? **(\$523.20)**
- b. What is the credit limit on this credit card? **(\$2,100.00)**
- c. How much of that credit is available at the time of this statement? **(\$1,576.80)**
- d. How does her previous balance compare to the new balance shown on this statement? **(She had a larger balance last month but paid it in full. Her previous balance was \$1,686.15 compared to her current balance of \$523.20.)**
- e. Was she charged any interest on her purchases this month? If so, what was the amount? If not, why was there no interest added to her account? **(No interest or finance charges were added to her account because she paid the previous balance in full.)**
- f. How much would she need to pay on this statement to avoid paying any interest? **(She needs to pay the total amount of \$523.20)**
- g. What is the annual percentage rate for purchases on this account? How does that differ from the annual percentage rate for cash advances? **(Her APR is 19.8% on**

purchases; 21.8% on cash advances. Note the daily rate of interest is also shown on the statement.)

- h. What would happen to the interest rate if she missed a payment or made a late payment on this account? **(She would have to pay a \$35.00 fee and her interest rate could increase up to 29.99% on future purchases.)**
- i. Suppose Teresa decided to make only the minimum payments on her October purchase, with no other charges on this account. How long would it take her to pay it off? How much interest would she pay? How much would her purchase really cost? **(It would take her 1.5 years to pay off the purchase; she would pay \$627 for her purchase instead of \$523.20—an increase of \$103.80, which is almost 20 percent more than the actual purchase price.)**
- j. Looking at this statement, do you think Teresa is handling her credit card responsibly? Why or why not? What would you recommend? **(She seems to be using the card responsibly because she is paying off her total amount each month. It is recommended that she continues to charge only what she can afford to pay without making monthly payments and to continue making payments on time.)**

CLOSURE

1. Tell students they will probably use a credit card sometime in their lives. They may also start receiving a variety of credit card offers when they graduate from high school or college. Remind students that legislation requires them to meet the card issuer's income criteria or have a cosigner to qualify for a credit card, regardless of their age. Remind students that using credit cards has several benefits, such as providing a record of all purchases, convenience, not requiring them to carry large amounts of cash, backup in case of emergencies, etc. However, they also have a responsibility to use them wisely because card holders can get into trouble rather easily if they overspend or use them carelessly. Using

credit cards means they are borrowing money to purchase goods and services, and those purchases must be repaid with interest if they cannot pay the total charges each month. Carrying high balances on credit cards can become a vicious cycle and create problems trying to pay their monthly bills. Staying aware of the amount they charge, understanding the basics of their credit agreements, being informed about potential changes, closely reading their monthly statements, and understanding their rights and

responsibilities will help reduce future problems with their credit cards and protect their financial future.

ASSESSMENT

Give each student a blank sheet of 8x10 paper. Have them develop a poster providing information about credit cards for their friends or family. Ask for volunteers to explain their posters to the class.

SLIDE 15.1

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Calculating Credit Card Interest

1. Find your ANNUAL PERCENTAGE RATE (APR). It should be on your credit statement and in the agreement you signed when opening the account. Interest rates are subject to change, so it is important to read all communications from the company issuing your card.

For this example, let's use 14 percent.

2. Divide your APR by 365 to find your daily percentage rate.

$$14\%/365 \text{ days in a year, or}$$

$$14\%/365 = .00038$$

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SLIDE 15.2

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3. Calculate the average daily balance of your account.

Suppose you start the month with a balance of \$2,500, then make a \$600 payment on the 15th. That drops your balance to \$1,900 for the rest of the month.

$$\$2,500 \times 15 = \$37,500$$

$$\$1,900 \times 15 = \$28,500$$

$$(\$2,500 \times 15) + (\$1,900 \times 15) = \$66,000$$

or

$$\$37,500 + \$28,500 = \$66,000$$

$$\$66,000/30 = \$2,200$$

Shopping for a Credit Card

SLIDE 15.3

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4. Calculate your interest for this month.*

Your daily rate of interest is .00038 and your average daily balance is \$2,200.

$$\$2,200 \times .00038 \times 30 = \$25.08$$

5. Using this example, your interest for this month would be \$25.08.

**Most credit card companies use 30 days for all months except February. Some may also calculate rates on based 360 days a year instead of 365, but any difference is minor.*

Shopping for a Credit Card

Comparing Credit Cards

Using credit cards isn't necessarily bad. However, you need to be cautious when using them. They can be a tool to help you manage your monthly expenses when used wisely—but can wreck your monthly budget and create financial problems for years to come when overused or abused. Understanding the basics of credit cards will help you make better choices about which card is best for you. The following information will help you make more informed decisions about credit cards.

Part 1. Credit Card Facts

- Credit cards are a type of revolving credit, which means your monthly payments depend on how much you charge on your card rather than being a set amount for a specific number of months.
- Household debt on credit cards is about \$1.4 trillion—making it about one-third of all debt owed by U.S. families.
- Students graduating from college have an average credit card debt of \$6,800 in addition to an average of \$33,000 in student loans.
- Over 83 percent of all adults in the US have at least one credit card; 90 percent of those with credit cards have more than one. The average number of credit cards accounts is 2.3 per family.
- Almost 50 percent of credit card holders pay the total amount charged every month and carry no balance forward. For those who carry a balance, the average amount owed is \$4,500 per person or \$8,700 per family.
- Households with lower incomes tend to have more credit card debt than households with higher incomes. As average income increases, average credit card debt decreases. However, the percent making minimum payments is about the same for all income levels.
- Making minimum payments or carrying a balance each month increases the total amount paid for the goods and services purchased with a credit card. For example: Suppose the interest rate is 17 percent and there is a \$10,000 balance on the account. The minimum payment would be about \$240 a month, and it would take 340 months (over 28 years!) to pay off the card—with no additional charges on it.) That's a total of \$13,607 in interest.

Part 2. Credit Card Basics

Understanding the basics of credit cards can help you make better choices when making credit decisions. Not all credit cards are alike. Here are some ways in which they differ.

- **The annual fee.** Some credit cards charge an annual fee, and some do not. The amount of the annual fee may vary from card to card. Most people who have a strong credit record can find cards that do not charge an annual fee.
- **Other fees.** Credit cards usually charge stated fees for late or missed payments, going over your credit limit, or making certain transactions such as cash advances.

- **The annual percentage rate (APR).** The APR can vary from card to card by several percentage points. Furthermore, some credit cards offer a low APR for the first few months and then increase it after three or six months. The APR on cash advances often differs from the APR for purchases.
- **The grace period.** Almost all credit cards have a grace period, which is the amount of time you have to pay the balance without paying interest. It generally starts the first day of the billing cycle and lasts for specified number of days. While grace periods vary from one card to another, they tend to be 21 to 25 days. The longer the grace period, the more interest-free days the cardholder has to pay the balance before incurring interest. (Note: Cash advances on a credit card may not have a grace period.)
- **The way interest is calculated.** The interest on credit cards is calculated using the average daily balance. By using this method, the APR is divided by 365 and then multiplied by the average of each day's balance for the billing cycle. While there are other ways to calculate interest, the average daily balance has become the standard for credit card companies.
- **The credit limit.** This is the maximum amount of money a cardholder can charge. A higher credit limit gives the cardholder flexibility but can also lead to credit card balances that are difficult to pay off.

Part 3. Other credit card features, services, and incentives

Credit cards also differ in the types of services and features offered, which may influence your decision when choosing a card. However, you should carefully compare the benefits of these incentives with the potential costs associated with the interest rates and other basics. Following are some of the additional features, services, and incentives offered by credit card companies.

- High or no credit limits.
- Rewards such as cash back, gifts, airline miles, discounts on gasoline or other purchases.
- The number of merchants who accept the card.
- Travel services such as covering the rental car insurance deductible, discounts on hotels, travel-life insurance, cash advances, or ATM privileges.

Part 4. Credit Card Comparison Chart

Follow the directions provided by your teacher to complete the chart below.

	Card #1	Card #2	Card #3
APR (annual percentage rate): Is it fixed or variable?			
Penalty APR and trigger events when it is charged			
Annual fee			
Late fee			
Over-the-limit fee			
Transaction fees (balance transfers, cash advances, etc.)			
Grace period			
Method of computing account balance			
Rewards for use			

EXERCISE 15.1

Lesson 15: Shopping for a Credit Card

After completing this chart, answer these questions.

- a. What characteristics would you look for if you carried a balance and wanted to save money on a credit card?

- b. What features would you look for if you planned to pay off your balance each month?

- c. Which card would your group choose?

Calculating Your Interest Rate

Using the information provided in **Slides 15.1–15.3**, calculate the following monthly interest rate.

APR	19 percent
Beginning Monthly Balance	\$1,000
New purchase on the 10th	\$500
Days in billing cycle	30

Reading Your Credit Card Statement

Part 1. Define the following terms, using your own words.

- a. Summary of account activity

- b. Payment information

- c. Late payment warning

- d. Minimum payment warning

- e. Notice of changes to your interest rates

- f. Other changes to your account terms

- g. Transactions

- h. Fees and interest charges

- i. Year-to-date totals

- j. Interest charge calculation

Part 2. Use the following credit card statement to answer the questions on the following page.

CARD Statement

A Account Number 1234 1234 1234 1234
C Statement Closing Date 11/09/19
C Credit Line \$2,100.00
D Credit Limit \$1,576.80

B TERESA TORRES
 123 ANY STREET
 CITY CA 12345

E **Account Summary**

Previous Balance	\$1,688.15
- Credits	\$0.00
- Payments	\$1,688.15
+ Purchases & Other Chgs	\$523.20
+ Cash Advances	\$0.00
+ FINANCE CHARGE	\$0.00
= New Balance	\$523.20

F **Payment Information**

New Balance	\$523.20
Scheduled Minimum Payment	\$35.00
Scheduled Payment Due Date	12/01/19

Late Payment Warning: If we do not receive your minimum payment by the date listed above, you may have to pay a late fee of up to \$35.00 and your APR's will be subject to increase to a maximum Penalty APR of 29.99%.

Minimum Payment Warning: If you make only the minimum payment each period, you will pay more in interest and it will take you longer to pay off your balance. For example:

If you make no additional charges using this card and each month pay...	You will payoff the balance shown on this statement in about...	And you will end up paying an estimated total of...
Only the minimum payment	1.5 years	\$627
\$49	1 year	\$596 (Savings=\$31)

I

If you would like information about credit counseling services, call 1-800-555-5555.

Rate Information

YOU MAY PAY YOUR BALANCE IN FULL AT ANY TIME
 YOUR RATE MAY VARY ACCORDING TO THE TERMS OF YOUR AGREEMENT
 NOTICE: SEE REVERSE SIDE FOR IMPORTANT INFORMATION ABOUT YOUR ACCOUNT

Type of Balance	Corresponding ANNUAL PERCENTAGE RATE	Daily FINANCE CHARGE RATE	Average Daily Balance
PURCHASE(S)	19.80%	.05424%	\$.00
CASH ADVANCE(S)	21.80%	.05972%	\$.00

Composite ANNUAL PERCENTAGE RATE 21.80% **J** Days in Billing Cycle 25

K **Transactions**

Trans Post	Reference Number	Description	Credits	Charges
10/08 10/08	XXXXXXXXXXXXXXXXXXXX	MERCHANT NAME		523.20
10/08 10/09	XXXXXXXXXXXXXXXXXXXX	PAYMENTS	1,686.15	

Detach an mail with check so that your payment is received no later than the "Payment Due" date. See reverse for important additional information.

Account Number 1234 1234 1234 1234
 New Balance \$523.20
 Scheduled Minimum Payment \$35.00
 Scheduled Payment Due Date 12/01/19

L **Amount Enclosed** \$

12/01/19

PAYMENT ADDRESS
 123 ANY STREET
 LOS ANGELES, CA 90030-0086

TERESA TORRES
 123 ANY STREET
 CITY, CA 123456

EXERCISE 15.3

Lesson 15: Shopping for a Credit Card

- a. How much did Teresa Torres charge on her credit card in October?
- b. What is the credit limit on this credit card?
- c. How much of that credit is available at the time of this statement?
- d. How does her previous balance compare to the new balance shown on this statement?
- e. Was she charged any interest on her purchases this month? If so, what was the amount? If not, why was there no interest added to her account?
- f. How much would she need to pay on this statement to avoid paying any interest?
- g. What is the annual percentage rate for purchases on this account? How does that differ from the annual percentage rate for cash advances?
- h. What would happen to the interest rate if she missed a payment or made a late payment on this account?
- i. Suppose Teresa decided to make only the minimum payments on her October purchase, with no other charges on this account. How long would it take her to pay it off? How much interest would she pay? How much would her purchase really cost?
- j. Looking at this statement, do you think Teresa is handling her credit card responsibly? Why or why not? What would you recommend?