Standard 8: **The student will describe and explain interest, credit cards, and online commerce.**

Credit Cards: More Than Plastic

Priority Academic Student Skills
Personal Financial Literacy

Objective 8.1: Compare costs and benefits of using credit cards and making online purchases (e.g., interest rates, fees, repayment schedules, and personal information protection). 🕮
Objective 8.2: Evaluate options for payments on credit cards (e.g., minimum payment, delayed payments, or payment in full).

Lesson Objectives

⇒ Describe how credit cards are used to purchase today's wants with tomorrow's money.
⇒ Compute the total cost of purchasing goods using credit cards at different interest rates when making minimum payments.

Austin receives two credit card applications, both stating he is preapproved for a credit card at 1.5% interest. Austin thinks that sounds pretty great. After all, there are several things he would like to buy, and his friends have credit cards. So, he signs both applications and mails them back to the company.

Norman receives the same two offers in the mail. He does not want another credit card, so he just throws them in the trash can.

Wichita also receives the offers. She reads both carefully to decide if either would be beneficial to her. One offer states the 1.5% introductory rate is good for six months, then converts to 22% on all charges. The other 1.5% introductory rate is good only for balance transfers. She shreds both offers before throwing them away.

Who made the best choice?

Personal Financial Literacy Vocabulary

Credit card: A plastic card that authorizes the delivery of goods and services in exchange for future payment with interest, according to a specific schedule.

Revolving credit: A consumer line of credit that can be used up to a certain limit or paid down at any time.

Introduction

Credit cards are more than plastic used to make purchases. They are a specific form of consumer credit originating in the United States during the 1920s when individual companies, such as hotel chains and oil companies, issued them to customers to make purchases at their businesses. The use of credit cards has grown tremendously since then and is now one of the primary sources of purchases for most consumers in the country.

Credit card accounts are an example of open-end consumer credit, often called revolving credit. While credit cards are a convenient way to make purchases, they also tend to promote "impulse spending" and overspending. Spending money is fun and easy; paying off credit card bills is not!

Lesson

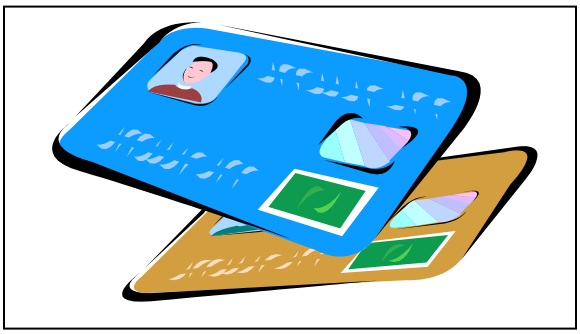
The growth of credit cards goes back to the late 1950s when the Bank of America in California issued the first bank credit card. It was called BankAmericard, but was renamed Visa in 1976. Other banks followed with other credit card plans, and the rest is history. Today, the average U.S. citizen owes more than $10,000 in open-end credit, and most of it is credit card debt!

A credit card is different from a debit card; debit cards remove money from your checking account when a purchase is made. A credit card is also different from a charge card; charge cards must be paid in full at the end of each month.

PRESENTATION

The multimedia slide presentation for this lesson outlines the content in this section. You may want to use it with your students, or print off the slides to use as lecture notes.

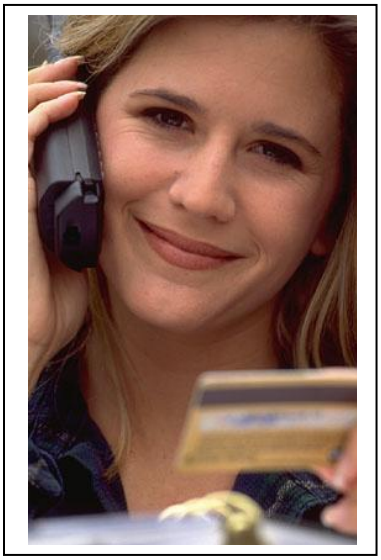
Credit cards, on the other hand, are revolving credit loans that must be repaid to the credit card issuer and, if not paid in full at the end of the month, accumulate interest on the balance due. When you use a credit card to make a purchase, the credit card company pays the merchant for your purchase. The credit card company sends you a bill called a statement at the end of the month showing what purchases you made, any additional fees you owe, and the total amount that you owe. In addition, your statement shows the minimum payment you are required to pay each month.



When you receive the statement, you should take a few minutes to review it to ensure it is correct. Credit card companies can, and do, make mistakes. Also, reviewing your statement provides an opportunity to make certain no one else is using your card number and making purchases without your permission. Should you find something wrong when reviewing your statement, you have the right to dispute the charges. All disputes need to be handled in a timely manner; otherwise, you must pay for those charges, with interest. The process for disputing incorrect charges or other errors with your account is outlined on the back of your monthly statement.

Interest on Credit Cards

Generally, you will not pay any interest on your purchases if you pay the entire amount in full each month. If you do not pay in full, however, the credit card company will charge interest on the entire amount from the date of your purchase. Information on how interest is charged may be given on the back of your monthly statement.



Credit card interest rates vary from zero to about 30 percent. Low interest rates are frequently special incentives to encourage you to use that credit card and may be only temporary. In addition, they may or may not cover all purchases on your credit card. Before making purchases, transferring balances, or getting cash advances in hopes of a low interest rate, be sure you read the fine print carefully and understand the credit terms.

Using credit cards for a cash advance means you are borrowing money from the credit card company. While convenient, it tends to be one of the most expensive ways to borrow money. Even if you think you can repay it by the end of the month with little or no interest, chances are you will end up paying high interest rates on the loan.

And, if you do not have money in the middle of the month, you probably will not have it at the end of the month either. It is best to avoid this practice except in extreme emergencies.

CREDIT CARD TIP #1
Making minimum payments on your credit cards means you are overspending or overcharging on your cards.

Credit card companies often offer other special incentives tempting you to use them instead of other means of payment. Some of these incentives include frequent flyer points on airlines, cash back on purchases, and gift certificates. These rewards are certainly great fun to receive, but they can also be very costly unless you are already in the habit of paying the total balance on your credit card each month. In many cases, you may end up paying more in interest than the value of the reward. That is not good money management or decision making. Keep in mind that credit card companies are in business to make money — not to give it away.

Credit cards are classified as **revolving credit**, which means you can use the amount for which you are approved as long as you continue making payments on it. However, revolving credit has more flexible terms than other forms of credit. For example, credit card companies can change the interest rate, late fee charges, other fees, and terms of credit at any point — as long as they notify you in advance of the change.

Increases in interest rates and other fees can impact the amount of the monthly payment and wreck your budget rather quickly. Even though those mailings from the card companies look pretty boring, taking a few minutes to read them will help you monitor any changes in your rights and responsibilities with your creditors. Most credit card companies will notify you about 30 days in advance of making any changes.

Before accepting and using any credit card, be sure you read the terms very carefully. Credit card terms vary greatly and can easily become a financial nightmare when the bills start rolling in.

COMPLETE: Comparing Credit Cards – Activity 8.1.1
Ask your teacher to review your answers before continuing with this lesson.

Your Credit Card Statement

Each month you should receive a statement from your credit card company. While statements from different card companies do not look the same, they generally have the same information. Some of the main parts of the statement include:

***Purchases or new charges*:** This section contains a list of everything you have purchased or anything charged to your bill since the last statement. It should also show the rate of interest you are paying on those charges. Cash advances tend to have higher interest rates, but will also be listed on your statement. If you find something listed in this section that you have not purchased or authorized, then you need to contact the credit card company immediately. Otherwise, you will be responsible to pay for it.

Payments and credits: This section of your statement shows how much you have paid on your balance since the last statement. Again, you want to check to be sure they have credited your account with any payments you have made since the last statement.

***Due date or pay-by date*:** In order to avoid any late fees, you need to be sure the credit card company receives your payment before this date. It is best to mail your payment at least ten days before this date to ensure it arrives in time to be processed by the due date. Late fees can be hefty, and they add to the burden of paying off your credit card. In addition, late payments are generally reported to the credit bureaus and will drop your FICO credit score. Paying bills online tends to shorten the time-frame and will help guarantee your payment arrives on time.

Credit limit: Your credit limit is the maximum amount you are allowed to charge on your credit card without incurring additional "over the limit" fees. Be sure to watch your limit monthly to ensure you are aware of how much cushion you have before reaching that limit. Over-the-limit fees can run as high as $50; in addition, you will be charged interest on those fees.

Reading your statement each month is your protection against errors or incorrect charges on your credit card as well as being charged unnecessary fees. Those incorrect charges, fees, and other potential problems with your statement can be a budget buster! You, and only you, are responsible for monitoring the monthly activity on your credit card. Any time you see an item you do not recognize, whether it is a charge or a fee, call the company and ask for an explanation.

Making Minimum Payments

In addition to the information noted above, your credit card statement will also indicate your minimum monthly payment. This amount is the payment you must make to keep your account current; any amount less than the minimum will still results in late fee charges added to your bill and to your minimum payment the following month. And, the credit card company will probably increase your interest rate. If you make a habit of paying less than the minimum, the credit card company has the right to demand the entire amount immediately. Paying less than the minimum is a good sign you need to quit spending!

Even though a minimum monthly payment is the amount shown on your statement, it is not the amount you SHOULD pay each month. The minimum payment is basically just enough to cover the interest charges, and little, if any, is applied to your principle. As a result, you will be paying for your purchases for more years than you use the item you purchased.

CREDIT CARD TIP #2
Save all charge receipts for the month and match them with the bill when it comes in.

Suppose you buy a new notebook computer for $2,000 and charge it on your credit card. How long will it take you to pay off the balance if you make minimum payments? The table below shows what happens when you make minimum payments for that $2,000 at three different interest rates:

Interest Rate	Number of Months	Total Interest Paid
18%	222	$2,615.43
24%	403	$6,812.23
10%	145	$ 888.49

For example, the notebook computer would cost you over $8,000 if you make minimum payments at 24% interest. ($2,000 + $6,812.23 = $8,812.23)

It would also take you over 33 years to pay for it. (403/12=33.58) Do you really think your notebook computer would last that long?

What happens if you increase the monthly payment?

$2,000 Credit Card Balance @ 24% APR		
Payment	**Number of Months**	**Total Interest Paid**
Minimum monthly payment of $50	403	$6,812.23
Add $10 a month, $60 monthly payment	56	$1,328.23
Add $20 a month, $70 monthly payment	43	$ 995.22
Double the payment to $100 a month	26	$ 579.75

Which would you prefer? Explain your reasoning.

Before you buy that notebook, you probably want to determine if it is worth the extra cost in interest—especially if you plan to make minimum payments.

What did you learn from this lesson?

How will it influence your future choices when making credit card purchases?

Conclusion

Using credit cards is a great convenience for most consumers, but it can also be a very costly choice. If you are not paying off your credit card balance in full every month, then you are increasing the cost of your purchases and reducing the amount of money you could put in savings to meet your future goals. The cost and benefits of using credit cards depend on the interest rate charged by the credit card company and the amount of payments you are able to make on a monthly basis. Making minimum payments on credit card purchases means you end up paying for many years, and doubling or tripling the cost of the items purchased. In addition, it is important to review your monthly statement to ensure it is correct and to keep from paying unnecessary fees.

FREE RESOURCE

For classroom sets of The ABCs of Credit Cards, contact the Oklahoma Council of Economic Education at http://www.econisok.org.

Who made the best choice? If you said Wichita, then you are correct!

Austin will probably be very surprised to learn he will be paying 22% on his credit purchases, unless he pays the entire balance each month. And, unless he is transferring a balance on the second card, he will not have 1.5% interest on it either.

By just throwing away the credit card applications, Norman is at risk to become a victim of identity theft.

Wichita showed she was a savvy credit user. She read the terms for both cards, decided the costs were greater than the benefits, and shredded the applications before throwing them away to prevent possible identity theft.

Name: _____ Class Period: _____

Credit Cards: More Than Plastic
Review Lesson 8.1

Answer the following questions and give the completed lesson to your teacher to review.

1. Discuss the costs and benefits of using credit cards.

2. Identify and explain three items on your monthly credit card statement.

3. All credit cards charge interest. What can you do to reduce the costs of paying interest?

4. What factors should you consider when selecting a credit card?

Name: _____ Class Period: _____

Comparing Credit Cards – Activity 8.1.1

Use three credit card offers mailed to you, your parents, or your teacher. Complete the following comparison of credit cards. You may also contact three banks or credit unions in your area or go online to find information on three cards you can use to compare terms.

	Credit Card #1	**Credit Card #2**	**Credit Card #3**
Issuer			
Introductory Interest Rate/ No. of Months			
Interest Rate			
Annual Fee			
Transaction Fees or Other Fees?			
Days in Grace Period			
Credit Limit			
Incentives			
Will you use these incentives?			

Which of the three credit cards would you prefer to have? Explain your answer.

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