KATRINA'S CLASSROOM:

FINANCIAL LESSONS FROM A HURRICANE

LESSON 3: A FRESH START

Students learn about the wise use of credit cards. Through demonstrations and activities, they analyze different strategies for paying off credit card balances. They learn about the value of having emergency savings.

Jump$tart National Standards, Knowledge Statements, and Benchmarks for This Lesson

FINANCIAL RESPONSIBILITY AND DECISION MAKING

Knowledge Statement: A key to financial well-being is to spend less than you earn	Grade 8

INCOME AND CAREERS

Knowledge Statement: People can earn income from rent and interest	Grade 8

PLANNING AND MONEY MANAGEMENT

Knowledge Statement: Some payment methods are more expensive than others	Grade 8
Standard 3: Describe how to use different payment methods	Grades 8, 12
Standard 4: Apply consumer skills to purchase decisions	Grade 8

CREDIT AND DEBT

Knowledge Statement: For any given loan amount and interest rate, the longer the loan period, the smaller the monthly payment and the larger the total cost of credit	Grade 8
Knowledge Statement: Making minimum payments on credit card balances increases the total cost and repayment time	Grade 12
Knowledge Statement: Understanding credit card disclosure information is key to controlling borrowing costs	Grade 12
Standard 1: Identify the costs and benefits of various types of credit	Grades 8, 12

SAVING AND INVESTING

Knowledge Statement: Saving means setting income aside for emergencies and immediate needs. Investing means putting money to work earning more money for the future. Funds for investing often come from current income not spent	Grade 8
Knowledge Statement: Compound interest is money earned on both principal and previously earned income	Grade 8
Standard 1: Discuss how saving contributes to financial well-being	Grade 8, 12
Standard 2: Explain how investing builds wealth and helps meet financial goals	Grade 8

LEARNING OBJECTIVES

At the end of the lesson, students will be able to

- Describe guidelines for the wise use of credit cards.
- Create an effective strategy for paying off credit card debt.
- Describe how to set aside funds to create an emergency fund.
- Apply the principles of compounding to predict interest payments on a deposit.

TOOLS AND CONCEPTS

In the video, students will learn about

- Credit cards.
- Emergency funds.

PREPARATION

Make transparencies of Visual 3-1—Credit Card Statement, Visual 3-2—That Big Coffee Drink, and Visual 3-3—Simple vs. Compound Interest. If you choose to do the optional activity, make a transparency Visual 3-4—Making the Minimum Payment.

Photocopy Activity 3-1—Discussion Questions for *A Fresh Start* and Activity 3-2—Evaluation for *A Fresh Start*.

KEY MESSAGES

- Wise use of credit and credit cards
- Having emergency savings

PROCEDURE

1. **Introduce the video**.

   Explain to the class that they are going to watch the story of Jacquelyn, a young woman whose family left Biloxi, Mississippi, during Hurricane Katrina. Ask them to pay attention to how Jacquelyn's family paid for necessities while they were gone and what they are doing now to get back on track financially.

2. **Play *A Fresh Start***.

   Relate the story to any personal emergency experiences in the class.

3. **Distribute Activity 3-1—Discussion Questions for *A Fresh Start*. Discuss the video**.

   How did Jacquelyn and her family manage when they were staying with Jacquelyn's aunt?

   - What were some of the things Jacquelyn's family needed during and immediately after Hurricane Katrina? (they needed to buy food and clothes; they needed a place to stay)
   - How did Jacquelyn's family buy groceries and other necessities? (they brought cash and used credit cards)
   - What do you think would have happened to them if they did not have any savings in the bank, weren't creditworthy, and didn't have any credit cards? (they couldn't have covered day-to-day expenses)
   - What did her family need when they were forced to leave their home? (shelter, food)
   - There is a difference between needs and wants. Sometimes it seems that we need things that we can actually live without.
   - What did some of the people in this story have to live without? (power, computers, cell phones, phones, air conditioning)

   What is Jacquelyn's family doing now to get on track financially?

   - What is the family doing about their credit card debt? (trying to pay it back as quickly as they can)
   - What does Jacquelyn want now that her life is getting back on track? (a dress so she can be in the school pageant.)
   - How is Jacquelyn managing her money so she can get what she wants? (earning money by doing chores and babysitting, saving money for a goal)

4. **Discuss the need for emergency funds**.

   In the video, Jacquelyn's friends talked about the importance of saving money for an emergency. Hurricane Katrina was a major natural disaster, but emergency funds are important for all kinds of unexpected events.

   - Have you ever been in any kind of situation in which you needed money for an emergency? (car broke down, had to travel to see a sick relative)
   - How would/did it feel not to have money when you needed it? (bad, scary)
   - How would/did it feel to have money when you needed it? (good, in control, being able to help someone, feeling relieved)

5. **Using credit cards**.

   Jacquelyn's family took some money out of the bank, but it didn't last long. Soon they had to rely on credit cards to pay for the things they needed, like food and clothes.

   Ask students the following questions and discuss answers.

   - What is a **credit card**? How does it work? (A credit card is type of loan called a line of credit. It is accessed with a plastic card containing a secure number that allows the holder to borrow money to make a purchase. The bank that issues the credit card pays for the purchase, and the holder must then pay back the bank. If the customer does not pay the credit card bill within a certain period of time, the bank charges interest on the loan. In addition to interest on the unpaid balance, some credit card companies charge an annual fee just to have the credit card.)

- What is the value of having a credit card? (A credit card is a convenient way to pay for things. It is especially good to have in an emergency.)
- What are the risks of using credit cards? (When you use a credit card, you are borrowing money. Some people use - credit cards to pay for things they don't need or can't afford. Then they have a hard time paying the balance each month, and they end up paying a lot of interest in addition to the amount of the original purchases. If you pay off your credit card by the due date shown on the statement, no cost is incurred except for a possible annual fee.)
- What is the best way to use credit cards? (Use credit cards if you can pay off the balance each month or need it for an emergency. Shop carefully for credit card interest rates, fees, and terms. Generally, do not use a credit card to get a cash advance. The interest rate for a cash advance is high.)

6. **Paying a credit card statement**.

Project Visual 3-1—Credit Card Statement. Examine the credit card statement with students, explaining that this is a monthly "bill."

Discuss terminology in the questions below. Check with your class to be sure they understand critical terms. Point out each element on the credit card statement as you define the terms.

- What is a **credit line**? (A credit line is a type of short-term loan. The credit line on this statement is $1,200.)
- What is a **balance**? (A balance is the total amount of money owed on a credit card. On this billing statement the new balance is $125.24.)
- What is **interest**? (Interest is money paid for the use of borrowed funds. It is also called a finance charge, as on this statement.)
- What is an **interest rate**? (An interest rate is the percentage rate of the interest paid; for example, this credit card provider charges 19.80% a year to its customers on their balances.)
- What is the **minimum payment**? (The minimum payment is the amount you must pay to avoid additional penalties and fees. The minimum payment for this statement is $20.)

Ask: Why is Jacquelyn's family paying off their credit card debt quickly? (Jacquelyn's family is trying to pay off their credit card debt as quickly as they can because they would pay interest on the debt. The sooner they can pay off the balance, the less interest they will have to pay.)

Discuss credit card debt with students as stated below.

- Credit card companies can charge a lot of interest. It would be unusual to earn an interest rate on savings that is as high as what a credit card company charges, so the smartest thing to do is avoid credit card debt and pay it off as quickly as you can.
- When you don't have debt, you can use your money to earn interest by investing it in a savings account, money market account, or certificate of deposit (CD). You can also earn income on other types of investments like mutual funds and buying property, although these investments are riskier. They can go up in value, but they can also go down.
- It is hard to save money to put into an account. One way to do that is to cut back on expenses.

7. **Identify and discuss savings goals**.

Jacquelyn had a savings goal: to buy a dress. Her family understands the importance of saving for an emergency fund. All of us have goals for the future. Some are small, like buying a dress. Others are bigger, like buying a car or going to college.

Ask: Why is it important to save for an emergency fund? (you have money when you need it, you can get through a crisis more easily, you won't go into debt)

Ask: What are some savings goals?

Brainstorm goals. Write them on the chalkboard in front of the class. Ask students to estimate a cost to each goal; for example, an emergency fund for a student might be $100; a dress might be $50. Tickets to a ball game for four people might be $100. A flat screen television might be $2,000. A computer might be $500.

8. **Cutting expenses**.

Project Visual 3-2—That Big Coffee Drink

Tell Students: Some coffee drinks can cost around $4 each. Many people buy one every day without even thinking. That $4 can really add up. Let's see how. (Note: You might need to change this to another drink that is more popular with students in your area.)

Discuss each question below with the class. Ask them to provide the numbers. Point out the numbers on the visual as you go.

- If you bought a coffee drink five times a week, how much is that? ($20)
- How much is that per month? ($80)
- How much is that per year? ($960)

Tell students: That is almost $1,000! If you don't drink the coffee drinks that regularly, you probably drink something else just as expensive. Now let's look at what that $1,000 would do if you didn't buy the coffee drinks but instead put it into an interest-bearing savings account at 5% interest.

9. **Simple versus compound interest.**

Project Visual 3-3—Simple versus Compound Interest

Tell students: Let's see what happens if you gave up the coffee drink for one year and saved the money instead.

Explain that a savings account can offer simple interest or compound interest. Walk the class through the difference. Ask the class to provide you with the numbers as you fill them in on the visuals with the figures listed in the chart below.

SIMPLE VERSUS COMPOUND INTEREST

Simple Interest (Interest Rate = 5%)

Year	Principal	Amount used to calculate interest	Interest	Balance
1	$ 1,000.00	$ 1,000.00	$ 50.00	$ 1,050.00
2	0	$ 1,000.00	$ 50.00	$ 1,100.00
3	0	$ 1,000.00	$ 50.00	$ 1,150.00
4	0	$ 1,000.00	$ 50.00	$ 1,200.00

Total amount your money earned with simple interest: $200.00

Compound Interest (Interest Rate = 5%)

Year	Principal	Amount used to calculate interest	Interest	Balance
1	$ 1,000.00	$ 1,000.00	$ 50.00	$ 1,050.00
2	0	$ 1,050.00	$ 52.50	$ 1,102.50
3	0	$ 1,102.50	$ 55.13	$ 1,157.63
4	0	$ 1,157.63	$ 57.88	$ 1,215.51

Total amount your money earned with compound interest: $215.51

Discuss:

- What was the difference in interest earned between simple and compound interest? ($15.51) Explain that this difference could be quite a bit more if more money were saved or if the interest percentage were higher.
- What was the total amount you saved by not drinking the coffee for a year? ($1,215.51)
- What could you do with $1,215? Return to the goals you created during the brainstorming session on the chalkboard. How could this savings help reach any of these goals? About how long would it take to reach some of these goals?

There were three things that helped you save:

(1) You didn't drink coffee for a year and saved the money.

(2) You received interest on the money you saved.

(3) Your interest was compounded.

10. **Optional Activity—Doing the minimum**.

Everyone knows what it means to "do the minimum." It means doing just enough to get by. When it comes to paying off credit card debt, doing the minimum can really end up being the maximum. Here's how.

Project Visual 3-4—Making the Minimum Payment

(Note: Cover each column of the table with a separate sheet of paper.)

Discuss:

- The balance on this bill is $1,000. This is the total amount the credit card holder owes. The annual interest rate is 10%. The minimum payment on this bill is $20.
- If you paid $20 a month (the minimum payment) without making any additional charges, how much would you pay toward principal, and how much would you pay towards the interest? *(Reveal the rows in this column that show how much of the payment goes to the principal and how much goes to the interest. If they paid $20 this month, $8.33 goes towards the interest and the other $11.67 goes towards the principal balance.)*
- How long do you think it would take to pay off the balance? *(Reveal the row that shows how long it would take to pay off the balance.)* By paying $20 a month, it would take more than five years to pay off this balance!
- How much do you think it would cost in interest payments? *(Reveal the row that shows the total cost of borrowing.)* The total cost of borrowing the $1,000 would be $299.
- Let's see what happens if you could afford to pay 10% of the original balance each month. If you paid $100 each month, without making any additional charges, how much would you pay each month towards interest, and how much would you pay towards the principal? *(Reveal the rows that indicate what happens by paying off 10% of the balance each month, and show how much of the payment goes to the interest and how much goes to the principal.)* The interest payment will be $8.33 a month, and the principal payment will be $91.67 a month.
- How long do you think it would take to pay off the balance? *(Reveal the row that shows how long it would take to pay off the balance.)* By paying $100 a month, the credit card holder can pay off the debt in 11 months.

- How much do you think it would cost in interest payments? *(Reveal the row that shows the total cost of borrowing.)*
  The total cost of borrowing the $1,000 would be $48.
- It would be best to pay the balance off as quickly as possible.

11. **Jacquelyn's Needs, Wants, and Goals**.
    Project Visual 1-1 from Lesson 1.
    - Ask the class what needs, wants, and goals Jacquelyn and her family have. Fill in the actual information about Jacquelyn.
      Jacquelyn's Needs: Shelter, food, clothes.
      Jacquelyn's Wants: To be in a beauty pageant; a new dress.
      Jacquelyn's Goals: To pay off credit card debt; to save for an emergency fund; a new dress.
    - Compare predictions with actual answers.

CLOSURE

Ask students the following:

- Why is it wise to pay back credit cards as quickly as possible? (you reduce your debt and avoid paying large amounts of interest)
- What is the difference between simple and compound interest? (simple interest is added only to the original principal; compound interest is paid on both the principal and the accumulating interest)

EVALUATION

Distribute Activity 3-2—Evaluation for *A Fresh Start*. Ask students to complete the handout during class or for homework. Review the answers with students.

You Decide. Have students write a story about a character who faces a situation in which an emergency fund would be helpful. Write two endings for the story. The first ending shows what happens to the character when he or she has the emergency fund; the second ending shows what happens to the character without an emergency fund.

Y **Your Credit Card's Information**

ACCOUNT NUMBER	
1234 5678 9100 1234	
PAYMENT DUE DATE	NEW BALANCE TOTAL
09 / 10 / 07	$ 125.24
TOTAL MINIMUM PAYMENT DUE	AMOUNT ENCLOSED
$ 20.00	

DETACH TOP PORTION AND RETURN WITH PAYMENT

Make check payable to:

YOUR CREDIT CARD SERVICES
P.O. BOX 12345
ANYTOWN, ST 12345-6789

JANE DOE
123 MAIN STREET
ANYTOWN ST 12345-6789

Account Number	Credit Line	Cash or Credit Available	Days in Billing Cycle	Closing Date	Total Minimum Payment Due	Payment Due Date
1234 5678 9100 1234	$ 1,200.00	$ 1,074.76	31	08 / 15 / 07	$ 20.00	09 / 10 / 07

Posting Date	Transaction Date	Reference Number	Card Type	Category	Transactions AUGUST 2007 STATEMENT			Charges	Credits (CR)
PURCHASES AND ADJUSTMENTS									
07 / 18	07 / 16	0063	MC	C	KARA'S GARDEN	ANYTOWN	ST	14.83	
07 / 18	07 / 16	2884	MC	C	SHUN LING RESTAURANT	ANYWHERE	ST	30.55	
07 / 18	07 / 17	0798	MC	C	GOLDEN DRAGON RESTAURANT	ANYTOWN	ST	27.50	
07 / 19	07 / 17	6706	MC	C	OFFICES LAND	ANYTOWN	ST	12.26	
07 / 25	07 / 22	7465	MC	C	VALUE MORE CLOTHING	ANYTOWN	ST	40.10	
TOTAL FOR BILLING CYCLE FROM 07 / 16 / 2007 THROUGH 08 / 15 / 2007								**$ 125.24**	**$ 0.00**

IMPORTANT NEWS

YOU ARE A VALUED CUSTOMER. WE WANT TO MAKE SURE YOU ARE AWARE THAT WE HAVE RECEIVED YOUR LAST PAYMENT IN THE AMOUNT OF **$168.80**. THANK YOU!

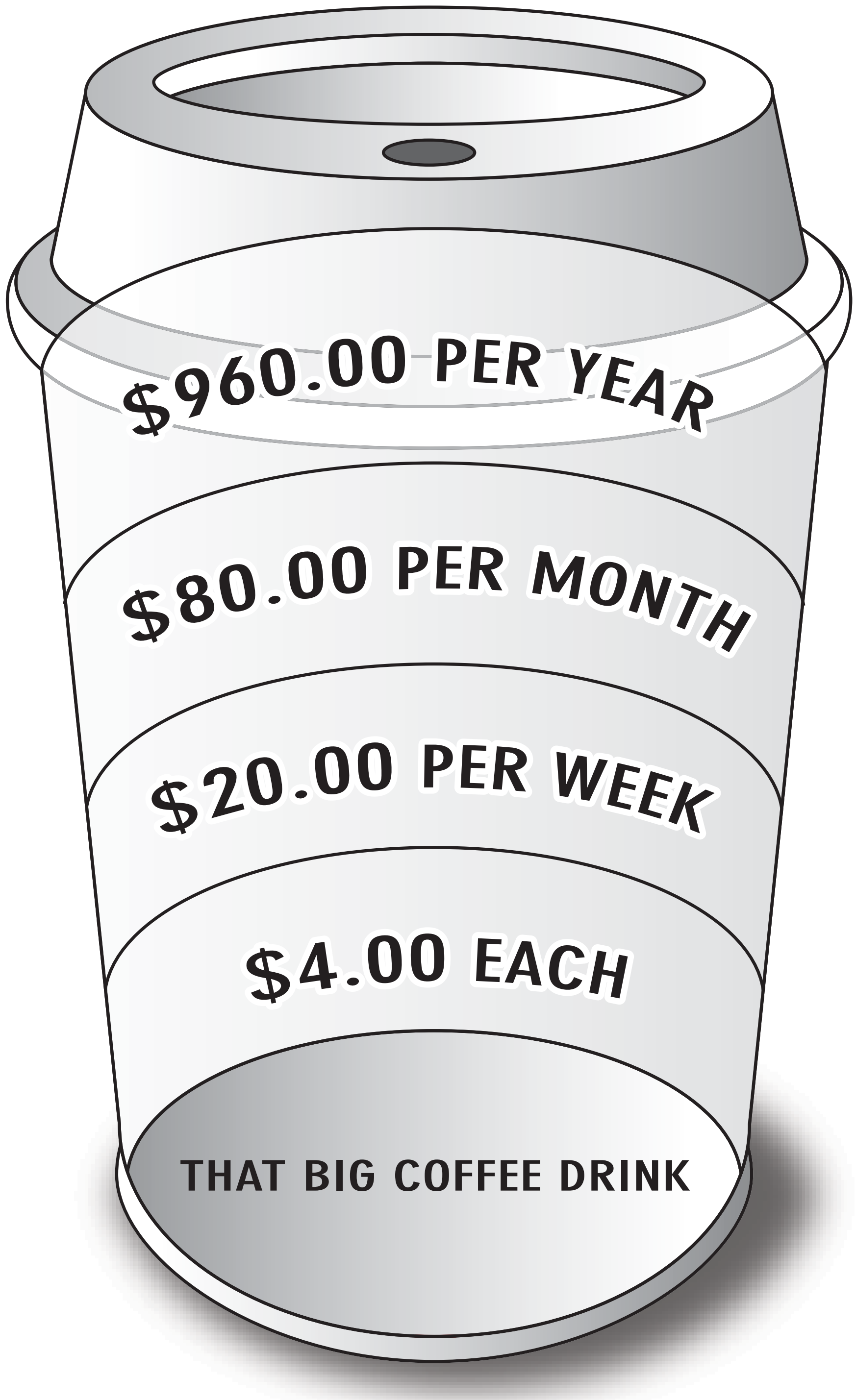
SUMMARY OF TRANSACTIONS

Previous Balance	(-) Payments and Credits	(+) Cash Advances	(+) Purchases and Adjustments	(+) Periodic Rate FINANCE CHARGES	(+) Transaction Fee FINANCE CHARGES	(=) New Balance Total
$ 168.80	$ 168.80	$ 0.00	$ 125.24	$ 0.00	$ 0.00	$ 125.24

TOTAL MINIMUM PAYMENT DUE

Past Due Amount	$ 0.00
Current Payment	$ 0.00
Total Minimum Payment Due	$20.00

FOR THIS BILLING PERIOD:
ANNUAL PERCENTAGE RATE............ 19.80%


$960.00 PER YEAR
$80.00 PER MONTH
$20.00 PER WEEK
$4.00 EACH
THAT BIG COFFEE DRINK

SIMPLE INTEREST (INTEREST RATE = 5%)

Year	Principal	Amount used to calculate interest	Interest	Balance
1	$ 1,000.00	$ 1,000.00	$ 50.00	$ 1,050.00
2	0	$ 1,000.00		
3	0			
4	0			

Total amount your money earned with simple interest:

COMPOUND INTEREST (INTEREST RATE = 5%)

Year	Principal	Amount used to calculate interest	Interest	Balance
1	$ 1,000.00	$ 1,000.00	$ 50.00	$ 1,050.00
2	0	$ 1,050.00		
3	0			
4	0			

Total amount your money earned with compound interest:

How long will it take to pay off this credit card if no additional purchases are made?

Principal Balance = $1,000

Interest Rate per year = 10%

	Paying only the minimum payment each month (fixed payment of $20.00)*	**Paying 10% of the original balance each month** (fixed payment of $100.00)
Monthly payment	$20.00	$100.00
Amount applied to the principal	$11.67	$91.67
Amount applied to interest	$8.33	$8.33
Total time to pay it off	5.4 years (65 months)	11 months
Total cost of borrowing	$299.00	$48.00

* Assuming minimum = 2% of principal

Minimum payment requirements can usually be found on your credit card statement as part of the terms and conditions. This is not the amount shown as the minimum payment due for that month but rather is the basis for calculating all minimum monthly payments in percentage and dollar terms.

How did Jacquelyn and her family manage when they were staying with Jacquelyn's aunt?

1. What were some of the things Jacquelyn's family needed during and immediately after Hurricane Katrina?

2. How did Jacquelyn's family buy groceries and other necessities?

3. What do you think would have happened to them if they did not have any savings in the bank, weren't creditworthy, and didn't have any credit cards?

4. What did her family need when they were forced to leave their home?

5. What did some of the people in this story have to live without?

What is Jacquelyn's family doing now to get on track financially?

6. What is the family doing about their credit card debt?

7. What does Jacquelyn want now that her life is getting back on track?

8. How is Jacquelyn managing her money so she can get what she wants?

ACTIVITY 3 - 2 — EVALUATION FOR *A FRESH START*

Directions: Match the following vocabulary words with their definitions. Write the corresponding letter of the word in the appropriate blank space.

A. Interest rate	B. Interest	C. Balance
D. Minimum payment	E. Credit line	F. Credit card

1. __________ Allows access to a type of loan with a specified line of credit; can be a convenient way to pay for things.
2. __________ A type of short-term loan; is an amount negotiated with the credit card company.
3. __________ Money paid for the use of borrowed funds; is also called a finance charge
4. __________ A percentage rate of the interest paid on a loan.
5. __________ The amount you must pay to avoid additional penalties and fees.
6. __________ Total amount of money owed on a credit card.

Directions: Answer the following questions.

7. In the video, Jacquelyn's friends talked abut the importance of saving money for an emergency. Give one example of a time when you or someone you know needed money for an emergency.

8. Explain how interest charges influence the rate at which someone should pay off credit card debt.

9. Identify one item that you regularly spend money on. If you gave it up, approximately how much money would you save? Show how you arrived at your answer.

10. A savings account can offer simple interest or compound interest. Suppose you have an initial savings account balance of $2,000. Assume that you make no additional deposits over the next three years.

    a. What would you expect the balance to be after three years, assuming a simple interest rate of 5%?
    b. What would you expect the balance to be after three years, assuming a compound interest rate of 5%?
    c. What is the difference between your answer in part a and your answer in part b?

ACTIVITY 3 - 2 — ANSWER KEY FOR *A FRESH START* EVALUATION

Directions: Match the following vocabulary words with their definitions. Write the corresponding letter of the word in the appropriate blank space.

A. Interest rate	B. Interest	C. Balance
D. Minimum payment	E. Credit line	F. Credit card

1. **F** Allows access to a type of loan with a specified line of credit; can be a convenient way to pay for things.

2. **E** A type of short-term loan; is an amount negotiated with the credit card company.

3. **B** Money paid for the use of borrowed funds; is also called a finance charge

4. **A** A percentage rate of the interest paid on a loan.

5. **D** The amount you must pay to avoid additional penalties and fees.

6. **C** Total amount of money owed on a credit card.

Directions: Answer the following questions

7. In the video, Jacquelyn's friends talked abut the importance of saving money for an emergency. Give one example of a time when you or someone you know needed money for an emergency.

   (Answers will vary.)

8. Explain how interest charges influence the rate at which someone should pay off credit card debt.

   (It is wise to pay off credit card debt as quickly as possible because interest charges add to the total amount the debtor must pay back. The more quickly a debtor pays off a credit card balance, the less total amount he or she must pay back.)

9. Identify one item that you regularly spend money on. If you gave it up, approximately how much money would you save? Show how you arrived at your answer.

   (Answers will vary.)

10. A savings account can offer simple interest or compound interest. Suppose you have an initial savings account balance of $2,000. Assume that you make no additional deposits over the next three years.

    a. What would you expect the balance to be after three years, assuming a simple interest rate of 5%?

    ($2,000 x .05 = $100 per year for three years.
    $2,000 + ($100 x 3) = $2,300)

    b. What would you expect the balance to be after three years, assuming a compound interest rate of 5%?

    Year 1: $2,000 x 1.05 = $2,100
    Year 2: $2,100 x 1.05 = $2,205
    Year 3: $2,205 x 1.05 = $2,315.25

    c. What is the difference between your answer in part a and your answer in part b?

    $2,315.25 – $2,300 = $15.25

LESSON 3a: A FRESH START EXTENSION ACTIVITY

Students learn how financial decisions are reflected in a credit history and about the impact of poor decisions on a credit report and credit score. Using a WebQuest of selected credit education Internet sites, students define key terms, identify the components of a credit score, identify the three main credit reporting agencies, and explore the process for obtaining a credit report and reporting errors or concerns.

Jump$tart National Standards, Knowledge Statements, and Benchmarks for This Lesson

CREDIT AND DEBT

Knowledge Statement: Consumers can choose from a variety of credit sources	Grade 8
Knowledge Statement: Credit bureaus maintain credit reports, which record borrowers' histories of repaying loans	Grade 8
Knowledge Statement: Sometimes people borrow more money than they can repay, which can have consequences such as repossession and garnishment	Grade 8
Knowledge Statement: Bankruptcy provides debt relieft, but has serious negative consequences	Grade 12
Knowledge Statement: Negative information on credit reports can affect your financial future	Grade 12
Knowledge Statement: Laws and regulations offer specific protection for borrowers	Grade 12
Standard 1: Identify the costs and benefits of various types of credit	Grade 12
Standard 2: Explain the purpose of a credit record and identify borrowers' credit report rights	Grade 12
Standard 3: Describe ways to avoid or correct debt problems	Grade 12

LEARNING OBJECTIVES

At the end of the lesson, students will be able to

- Define key terms.
- Identify the components of a credit score.
- Identify the three main credit reporting agencies and explain how to order a credit report.
- Highlight key facts about credit reports.

TOOLS AND CONCEPTS

Through this activity, students will learn about credit reports, credit scores, credit reporting agencies, default, delinquency, credit inquiries, installment credit, revolving credit, secured credit, unsecured credit, FICO, Fair Credit Reporting Act, and the Equal Credit Opportunity Act.

PREPARATION

Review background narrative for lesson introduction lecture and demonstration.

Prepare Visuals 3a-1—National Credit Scores, Visual 3a-2—Types of Credit, Visual 3a-3—Credit Conditions, and Visual 3a-4—Credit Review as PowerPoint slides or overhead transparencies.

Coordinate student Internet access to www.myfico.com and www.philadelphiafed.org.

Photocopy Handout 3a-1—Guided Exploration for each student.

Students will produce a quick reference "Credit Report Card." Have available cardstock, markers, construction paper, scissors, pencils, glue sticks, tape, stapler, etc. Stude nts may also create the card with word processing, desktop publishing, or presentation applications such as Microsoft Word, Publisher, or PowerPoint.

Optional: This activity can be done individually or as a group assignment. If using groups, determine the optimum group size in advance and/or assign students to a group. A group size of four to five students is suggested.

KEY MESSAGES

- Building and maintaining a good credit history takes time.
- A credit report is a reflection of one's financial decisions and behavior.
- A credit report affects more than just borrowing. It can influence the cost of insurance or the outcome of a job search, an apartment rental, or a cell phone service application.

TIME REQUIRED

90 minutes or two 50-minute class periods

PROCEDURE

1. **Introduce the topic of credit, credit reports, and credit scores by presenting the background information lecture and demonstration**.

   Background Information:

   What is "credit"? A quick check of "credit" in the dictionary yields definitions such as trust, a reputation for sound character, and a source of honor or distinction. Financially speaking, credit is both a reputation for solvency (being able to meet financial obligations) and integrity (honesty) and a financial tool that is available to help us purchase the things we need or want. Using credit (the tool) is neither good nor bad; however, the way we manage our use of credit tips the scales of our credit reputation in one direction or the other.

As in all things, trustworthiness and a sound reputation are earned. Good credit is earned through sound financial decision making about controlling debt and managing credit. Credit is the ability to borrow money. Good credit allows us to borrow money to finance larger purchases—such as cars, homes, school tuition, furniture, etc.—that would otherwise take a long time to accumulate enough cash to pay for all at once. Debt is the amount of money owed as a result of our credit worthiness. The balance between our income and our debt level, along with how we manage that debt, makes up our credit history and determines our credit score.

2. **Display Visual 3a-1—National Credit Scores**.

Your credit score is the measure of how you handle your financial obligations. Think of it as your financial GPA. It is a three-digit number that lenders and other creditors use to make an informed decision about your creditworthiness, which can help them determine an appropriate interest rate. The number is generated by assigning points to the various activities on your credit report, much like the grades you earn in school.

A credit score can range from 300 to 900, and the higher, the better. Nationally, consumers credit scores are distributed as follows:

800+	13%
750–799	27%
700–749	18%
650–699	15%
600–649	12%
550–599	8%
500–549	5%
up to 499	2%

A poor credit history can hurt your chances of getting a cell phone, a car, an apartment, or a house. It can cause your insurance rates to rise, and it can hurt your chances with a prospective employer. Your credit history reflects more than just your financial management skill; it also reflects your character and your level of preparedness to address or adapt to changing circumstances.

Our economy thrives on credit. In order to understand the impact of credit behavior on our credit report or credit score, we must understand the different types of credit and the conditions under which credit is granted.

3. **Display Visual 1a-2 — Types of Credit.**

   Types of Credit

   Revolving credit – For example, credit cards. Credit cards allow you to borrow at any time up to a limit set by the creditor. As you borrow against your credit limit, the amount available to borrow is reduced. As you repay your debt, the difference between your credit limit and the amount that you owe is available for you to borrow again. You are allowed to pay back the loan in lump sums or over an extended period of time. If you choose to pay over time, you will be charged interest on the full amount that you owe.

   Installment credit – For example, car loans, mortgages, student loans, etc. A lender allows you to borrow an amount for a specific purpose for a specific amount of time at a given interest rate. The total amount of interest to be paid is calculated up front, and payments are spread out equally over the length of the loan.

   Noninstallment or service credit – For example, cell phone plan, utilities, etc. With this arrangement, you are paying for a service that has already been used. Payment in full is required by a specified date. While interest is not charged, failure to pay within the specified time may result in service fees and/or discontinuation of service.

4. **Display Visual 3a-3 — Credit Conditions**.

   Credit Conditions

   Secured credit – Secured loans are those that require collateral (something of value) to guarantee repayment of the debt. For example, car loans and home mortgages require the lender to hold the title of the car or property as collateral until it is paid in full. In the event the loan is not paid, the lender repossesses the car or home.

   Unsecured credit – Loans that do not require a guarantee—for example, credit cards, service credit, and some installment credit.

5. **Students conduct a WebQuest.**

   Tell students that they will explore several Web sites to research terms and facts about credit reports and credit scoringr.

   - Divide the class into groups of four or five students.
   - Distribute a copy of Handout 3a-1—Guided Exploration to each student. Depending upon your preference, you may (1) assign each member of the group preselected questions to complete, (2) assign the group all the questions to complete, or (3) preselect several questions for the group to complete.
   - Direct the students to www.myfico.com. Give general directions for accessing the following sections to be used in the activity.
     - From the main page, scroll down to the bottom and demonstrate how to use the “Fico Credit Score” table.
     - Point out the “Good credit scores save you money” tab and the “About FICO scores” tab.
     - Explain to the students that the interest charged on a loan depends upon the amount borrowed, the reason borrowed, and the borrower’s credit score.

- Using the “Good credit scores save you money” tab, point out to the students the three loan types illustrated: 30 Yr fixed mortgage, 15 Yr home equity loan, 36 month auto loan.
- Select your home state (or any state) and show the students how the cost of credit changes by state, loan type, and credit score.
- From the main page, click “Credit Education” from the topic bar. Answers to many of the questions on the WebQuest can be found by manuevering through this page.
- From the “Credit Education Center” page, click “Credit Basics” and /or “Credit Q&A” from the topic bar. Answers to many questions on the WebQuest can be found by manuevering through these pages.

- Have the students or groups explore the sites and find the answers to the questions on the handout.

6. **Debrief student findings.**

Reconvene the group and have each student contribute his or her findings to the group so that each group has a fully completed results page or has all assigned questions completed.

CLOSURE

7. **Display Visual 3a-4 — Credit Review.**

As a wrap-up of the credit discussion, ask the students the following:

- What is “credit”?
- Is all debt bad? Why or why not?
- Should we be concerned about having bad credit? Why or why not?
- What does our credit report say about us to a potential employer?
- Besides borrowing money, what are some other activities affected by our credit report?

EVALUATION

8. **“Credit Report Card.”**

Tell the students that each group will examine the results of the WebQuest acitivity and develop a visual display of key facts about credit reports. The visual display, called a “Credit Report Card” is an 8 1/2" x 11" poster that serves as a visual reminder of the importance of developing and maintaining good credit. This activity may take a full 50-minute class period to complete, or, alternatively, it can be assigned as a take-home activity.

- Each group will use the questions they were assigned in the WebQuest activity as the topic for its poster. If the groups were required to complete the entire WebQuest, evenly distribute a category of questions (Credit Report, Credit Score, Know Your Rights) between the class groups so that all the categories are addressed.
- Instruct the group to review the results of their WebQuest and identify as a group what they perceive to be the four most important or interesting facts or lessons revealed in the answers and list the facts in ascending rank order with the highest priority item LAST. The facts or information can be suggestions, cautions, facts, procedures, statistics, etc. Creativity counts.

- Distribute the paper or cardstock and make available the necessary supplies (markers, construction paper, scissors, pencils, glue sticks, tape, stapler, etc.) If computer access is readily available, students may use word processing, desktop publishing, presentation applications such as Word, Publisher, PowerPoint, or other graphic applications to produce the "Credit Report Card."
- Allow time for the groups to discuss, plan, and create their cards. The cards can be text, graphic, drawings, images, rhyme, mnemonic devices, slogans, etc., designed to improve recall of the selected facts.
- Reconvene the group and review the activity results by asking each group to display its quick-reference "Credit Report Card" and present a summary of the four facts that they selected as the most important. Encourage the students to explain the meaning or relationship of the imagery or verse they used on their "Credit Report Card." Provide feedback or solicit feedback from the group if preferred. As an ongoing reminder of the results of the exploration, display the "Credit Report Cards" around the room or on the bulletin board.

The purpose of this exercise is to help you better understand how a credit score and credit report are derived and their impact on consumer purchasing power. Use the Web site links below to answer the questions on the following pages.

My Fico
http://www.myfico.com/Default.aspx

Understanding Your Fico Score
http://www.myfico.com/Downloads/Files/myFICO_UYFS_Booklet.pdf

FRB Philadelphia Consumer Resources
http://www.philadelphiafed.org/consumer-resources/

What Your Credit Report Says About You
http://www.philadelphiafed.org/consumer-resources/publications/what-your-credit-report-says.cfm

Your Credit Rating
http://www.philadelphiafed.org/consumer-resources/publications/your-credit-rating.cfm

Your Credit Rights
http://www.philadelphiafed.org/consumer-resources/publications/your-credit-rights.cfm

Credit Report

1. What is a credit report?

2. Where does the information contained in a credit report come from?

3. What are the three main credit reporting agencies?

4. What is the official Web site for the free annual credit report allowed by law?

5. How often should you review your credit report?

6. When can your credit report be reviewed by a lender or other entity?

7. What are the conditions under which a consumer can get a free copy of his or her credit report?

8. How long will negative information remain on your credit report?

9. What is a “healthy mix” of types of credit use on your credit report?

10. On average, how many credit obligations do consumers have on their credit report?

11. Give examples of the most common credit obligations.

Credit Score

12. What is the difference between a credit report and a credit score (FICO score)?

13. What credit information categories make up the FICO score?

14. Which category has the largest impact?

15. List the credit type components of the largest category.

16. What kind of information is not included in your FICO score?

17. What is a credit inquiry, and how does it affect your credit score?

18. List five tips for improving your FICO score.

19. Besides applying for credit, what might your credit score be used for?

20. How does my FICO score change?

21. How will a bankruptcy affect my FICO score?

22. Can accounts that aren't on my credit report affect my score?

23. How will closing old accounts impact my credit score?

Know Your Rights

24. How are mistakes made on a credit report?

25. What should you do if you find an error in your credit report?

26. What does the Fair Credit Reporting Act (FCRA) provide?

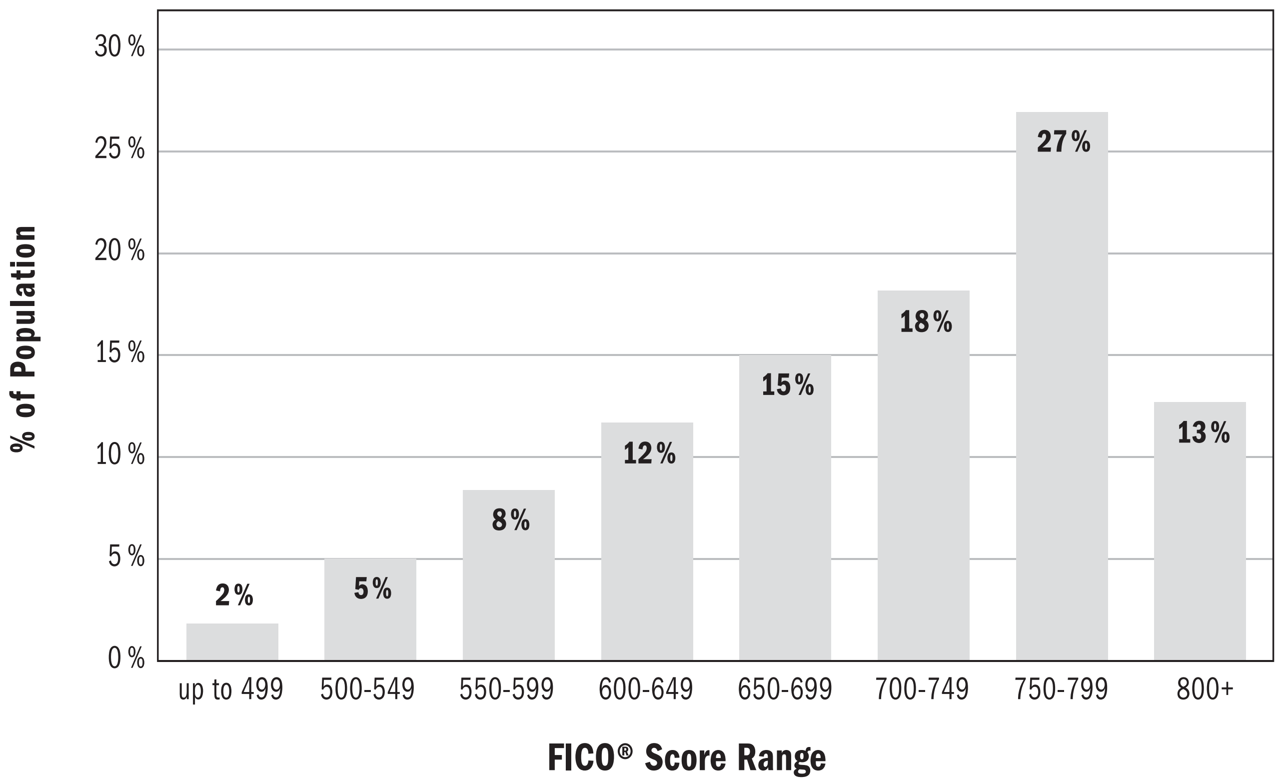
27. What does the Equal Credit Opportunity Act (ECOA) provide?

28. What does the Fair and Accurate Credit Transactions Act provide?

29. What should I do if I am denied credit because of something in my credit report?

30. If negative information is true, can I have it removed from my credit report?

VISUAL 3a- 1 — NATIONAL CREDIT SCORES



Source: "Understanding Your FICO Score" http://www.myfico.com/Downloads/Files/myFICO_UYFS_Booklet.pdf

Revolving credit (example: credit cards)

- Borrow at any time up to a limit set by the creditor.
- The difference between your credit limit and the amount that you owe is available to borrow.
- Pay back the loan in lump sums or over an extended period of time.
- Interest is charged on the full amount owed (principal, interest, and fees).

Installment credit (examples: car loans, mortgages, student loans)

- Borrow a specific amount for a specific purpose for a specific amount of time at a given interest rate.
- Total amount of interest to be paid is calculated up front.
- Payments are spread out equally over the length of the loan.

Noninstallment or service credit (examples: cell phone plan, utilities)

- Pay for a service that has already been used.
- Payment in full is required by a specified date.
- Failure to pay within the specified time may result in service fees and/or discontinuation of service.

Secured credit

- Requires collateral (something of value, e.g., home or car) to guarantee repayment of the debt.
- If the loan is not repaid, the lender repossesses the collateral.

Unsecured credit

- Loans that do not require a guarantee, e.g., credit cards, service credit, and some installment credit.

- What is credit?
- Is all debt bad?
- Should you be concerned about having bad credit?
- What does your credit report say about you to a potential employer?
- Besides borrowing money, what are some other activities affected by your credit report?