

Understanding Credit

The **BIG** Idea

- What is credit and why does it matter to me?

AGENDA

Approx. 45 minutes

- I. Warm Up: What Do You Know About Credit? (10 minutes)
- II. Credit: The Good, The Bad, The Bottom Line (10 minutes)
- III. What Your Credit Rating Means to You (15 minutes)
- IV. Finding Out Your Credit Rating (5 minutes)
- V. Wrap Up (5 minutes)

MATERIALS

STUDENT HANDBOOK PAGES:

- Student Handbook page 154, Your Car, Your Credit
- Student Handbook page 155, How Much Will You Pay?
- Student Handbook page 156, What's Behind Your Credit Rating?
- Student Handbook page 157, Credit Rating Quiz

FACILITATOR PAGES:

- Facilitator Resource 1, Credit Rating Scores
- Facilitator Resource 2, Credit Rating Quiz Answer Key

- Overhead projector
- Chart paper and markers
- Calculators (one per student)

OBJECTIVES

During this lesson, the student(s) will:

- Understand credit, as well as its advantages and risks.
- Understand credit ratings and the advantages of having a good credit rating.
- Understand what actions lead to a good credit rating and a poor credit rating.

OVERVIEW

In this lesson, students read a scenario about making their first car purchase and reflect on what they know about credit and credit ratings. Next, they define credit and discuss its advantages and disadvantages. Then they discuss credit ratings, and complete an activity in which they compare car loans based on different credit ratings. Finally, they talk about what's on a credit report, how to access their own reports, and what to do if there are mistakes.

PREPARATION

- The following handouts can be made into overhead transparencies or copied onto chart paper:
 - **Student Handbook page 155, How Much Will You Pay?**
 - **Student Handbook page 156, What's Behind Your Credit Rating?**
- Print a copy of **Facilitator Resource 1, Credit Rating Scores** and cut out the individual scores to hand out to students in **Activity III**. You may wish to reproduce this on heavy paper so cards are reusable.
- List the day's **BIG IDEA** and activities on the board.
- Write the day's vocabulary words and definitions on the board.

VOCABULARY

Credit: Money you borrow, for example, from a bank, with the promise to pay it back at a later date or over time.

Interest: The fee paid for borrowing money; usually a percentage of the money borrowed.

Credit report: A record of all the money you've borrowed, including credit cards, and your payment history.

IMPLEMENTATION OPTIONS

If time is an issue, you may choose to omit the quiz in the **Wrap Up, Student Handbook page 157, Credit Rating Quiz**.

In **Activity III, Student Handbook page 155, How Much Will You Pay?**, if your students struggle with math, you may wish to calculate several examples as a class.

ACTIVITY STEPS

I. Warm Up: What Do You Know About Credit? (10 minutes)

1. To begin this lesson, as students enter the classroom, refer them to **Student Handbook page 154, Your Car, Your Credit**. Give students a few minutes to read the scenario and answer the questions.
2. **SAY SOMETHING LIKE:** Welcome, everybody. Before we look at your answers, I'd like to see a show of hands. Who thinks they might apply for a credit card in the next few years? Who here is thinking about buying a car or a house in your future? And if you're not going to buy a house, you'll need to rent, right? And who thinks they just might apply for a job at some point in their lives? Wow, that's everyone! Well, if you think you might do any of these things, then you need to understand and take care of your credit rating.
3. **SAY SOMETHING LIKE:** Today we're launching into a six-week unit that covers money and finances. This unit is called "Money Matters" because it's all about money and how it matters to you as you think about life on your own. We'll be spending this week and next on credit and credit cards, followed by two lessons about buying and maintaining a car, and two lessons about renting an apartment. Today, we're going to review what we mean by "credit," the benefits and dangers of credit, what a credit rating is, and why it matters to your future.
4. **SAY SOMETHING LIKE:** Now let's take a look at the first question from **Your Car, Your Credit**. [Take a few minutes to let students share their answers. The second question is addressed during **Activity III**.]

II. Credit: The Good, The Bad, The Bottom Line (10 Minutes)

1. **SAY SOMETHING LIKE:** Let's start with the term **credit**. Can someone tell me, in your own words, what credit is? [Let one or two students respond.] In short, *credit is money that you borrow and pay back at a later date or over time*. When you use a credit card, you're borrowing money from the bank or financial institution that issued the credit card. When you apply for a credit card, you're making a promise that you'll pay back the money.

Besides credit cards, what other times do we use credit? [Let students answer and write them on the board. Make sure the list includes "Buying a house" (house loans or mortgages), "Buying a car" (car loans), and "Applying for financial aid for college" (school loans).]

2. **SAY SOMETHING LIKE:** As you can see, credit is an important tool that you'll probably use throughout your life. For example, people may not have the money up front to pay for college, but school loans allow them to go to college and pay back the loans when they begin their careers. And very few people have enough money in the bank to purchase a house without credit. Home mortgages allow them to own homes by paying back the loan over time.
3. **SAY SOMETHING LIKE:** But credit has its downside, too. For starters, some people may borrow more money than they can afford to pay back. This is especially true with credit cards, because they're easy to use and you can quickly lose track of how much money you owe.
4. **SAY SOMETHING LIKE:** But there's another big disadvantage of using credit. [You may want to write this on the board.] *Credit can cost a lot of money!* In other words, the amount you pay back in the end is much more than the amount you borrowed to begin with. Does anyone know why this is? [Take answers.]

The answer is **interest**. Any loan comes with interest, an amount you pay in addition to the money you borrow. Interest is usually a percentage of the money you borrow. The higher the interest, the more money you pay for a loan.

Usually long-term loans, like those for homes, cars, and colleges, carry a lower interest rate. You might pay 18% annual interest (expressed as an Annual Percentage Rate) on a credit card loan, while a home loan might have an annual interest rate of closer to 6%. On the other hand, long-term loans are just that – *long term*. So even though that house loan has a lower interest rate, you're paying off the loan for over 30 years. And that means every year, your interest is adding up – and adding to the total amount you owe.

5. **SAY SOMETHING LIKE:** So, let's look at the bottom line. Anytime you apply for a loan or decide to use credit, it's important to determine how much you're going to pay in the end. This depends on three factors:
 - The amount of money you borrow.
 - The interest rate charged by the lending institution.
 - The length of the loan – or how long it takes to pay back the loan.

III. What Your Credit Rating Means to You (15 minutes)

1. **SAY SOMETHING LIKE:** We started this lesson with an activity about credit rating. Does anyone know what this is? [Take answers.]

Your **credit rating**, also called a credit score, is an estimate of your ability to repay money you borrow. It's based on your **credit report**, a record of all the money you've borrowed – including credit cards – and your payment history. We'll take a closer look at what you'll find in your credit report in a few minutes.

Your credit rating depends on several different factors. Here are just a few:

- Your payment history: Do you pay off credit cards and other bills on time? A history of missed or late payments could hurt your credit rating.
- Your debt: How much money do you owe now? Having credit cards with high balances close to the limit could hurt your credit rating.
- Length of your credit history: How long have you had credit? The longer you've had credit (and used it wisely), the better your credit rating.
- The number of times you ask for credit: Have you applied for lots of cards in a short period of time? If so, this could be a red flag to a creditor.

All of these factors are considered to determine an individual's credit rating. People are assigned a number between 300 and 850 based on their past behavior using credit. The higher the number, the better the rating.

2. **SAY SOMETHING LIKE:** Now you might be wondering what the big deal is. Who really cares about your credit rating and credit report? Well, a lot of people will. After all, your credit rating says a lot about your judgment and trustworthiness. Insurance companies, landlords, and even potential employers can check your credit report. But most of the people who review your credit report will be lenders, like loan and credit card issuers. Anytime you apply for a loan or a credit card, the lender will automatically check your credit report.
3. **SAY SOMETHING LIKE:** Now, let's think back to that quiz we started the class with. Does anyone remember how your credit rating can affect a loan? [Take answers from the class.] In a nutshell, *your credit rating determines if you get a loan and the interest you pay on that loan.*
 - **The higher your credit rating, the lower your interest rate.** If you have a high credit rating, it means a lender will feel safer lending you money because you've proven your ability to repay loans in the past.

- **The lower your credit rating, the higher your interest rate.** If your credit rating is low, a lender might doubt your ability to repay the loan. After all, if you didn't make payments or often paid late in the past, it's likely you could do so again. To safeguard the loan, they'll set a higher interest rate.
 - **If your credit rating is very low, you could get turned down for the loan.** If you've failed to make payments in the past, a lender won't want to lend you money now.
4. **SAY SOMETHING LIKE:** Now, remember that car loan from the first activity? I'm going to assign each of you a credit rating and we're going to find out what effect it has on your car loan.

Hand out the strips you cut from **Facilitator Resource 1, Credit Rating Scores**, so that every student is assigned a credit rating. Then have students turn to **Student Handbook page 155, How Much Will You Pay?** Have students circle their assigned credit score on the chart.

5. **SAY SOMETHING LIKE:** To purchase the car you found, you need a loan for \$10,000. You've decided you need a 36-month loan, so it's paid off in full in three years. Take a minute to look at the chart and answer the questions. When you're done with questions 1-4, please find someone near you with a credit rating that falls in a different category. Work together quietly to answer questions 5 and 6.
6. Have students share information as a class to confirm that good credit provides significant savings over the life of a loan.

IV. Finding Out Your Credit Rating (5 minutes)

1. **SAY SOMETHING LIKE:** After that activity, you might be getting curious about these credit reports that determine your credit rating. As we discussed earlier, a credit report is basically a snapshot of your credit history. This history is collected and kept on file by credit bureaus. A credit report includes the following information:

Use chart paper or an overhead transparency of **Student Handbook page 156, What's Behind Your Credit Rating?** to present this information, as students take notes on their own Student Handbook page.

- **Personal Identification Information:** Name, address, social security number, telephone number, and spouse's name; past and present employer names and addresses.

- **Public Record Information:** Legal files, such as bankruptcies.
 - **Collection Agency Account Information:** Details if a collection agency has contacted you about an outstanding debt.
 - **Credit Account Information:** Information on every account or loan in your name, such as: when it opened, the highest balance, present balance and payment history (including if any payments are past due and by how much).
 - **Inquiries:** Companies that have requested your credit report, for a credit-card offer or application.
2. **SAY SOMETHING LIKE:** You might think you'll always know what's on your credit report, but it's a good idea to check it about once a year. You want to make sure the information is up-to-date and accurate. You can do this by contacting one of the three credit bureaus:
- Equifax (www.equifax.com)
 - Experian (www.experian.com)
 - Trans Union (www.transunion.com)

These credit bureaus provide free reports once a year. You can access your credit report immediately if you request one online. If you call or write, it takes about 15 days to receive one in the mail.

3. **SAY SOMETHING LIKE:** If you find a mistake on your credit report, you can write the credit bureau and it should be corrected within 60 days. But remember, you cannot remove correct information from your report, even if it has a negative impact on your credit rating. However, it won't be there forever: account information remains on your credit report for seven years from the date it occurs.

Of course, many of you won't have a credit report yet. If you've never had a credit card, or taken out a car loan, then there's nothing to report. This is a great situation to be in because you can start off with a blank slate.

V. Wrap Up (5 minutes)

1. As a final activity, have students turn to the **Student Handbook page 157, Credit Rating Quiz**. Give students a few minutes to answer the questions. When they're done, review the answers together. See **Facilitator Resource 2, Credit Rating Quiz Answer Key**.

2. **SAY SOMETHING LIKE:** In this lesson, you've learned about credit and why it's important to use it wisely. [Have a class discussion to review what you learned. Some questions to spark discussion include:
 - What surprised you most about what you learned today?
 - When we did the activity on car loans, who was assigned a credit rating under 620? How did that feel to know you were paying so much money to the bank – and so much more than other students?
 - What are two things you can do to make sure you have a good credit rating?]

3. **SAY SOMETHING LIKE:** Next week, we're going to talk about something that gets lots of people into credit trouble — credit cards. As you've learned today, the way you use your credit cards has a big impact on your credit rating, so it's important to use them wisely. We'll learn more about using credit cards next week.

Credit Rating Scores

Cut out the strips below and hand out one to each student when you assign credit ratings.

757	840	800	730
708	696	700	704
682	665	670	674
648	625	635	642
604	594	601	612
526	513	535	547
830	717	683	657

Credit Rating Quiz Answer Key

What have you learned about credit? Take this quick quiz to find out!

1. Your credit rating is most influenced by:
 - a) Your payment history on loans (*including credit cards*)
 - b) The number of credit cards you own
 - c) Your past and present income
2. If you have poor credit rating, you could:
 - a) Be turned down for a car loan
 - b) Have to pay a higher interest rate, meaning higher payments
 - c) Both
3. If you've never had a credit card, then you probably have:
 - a) A perfect credit rating
 - b) A poor credit rating
 - c) No credit rating
4. Your credit rating is:
 - a) Kept confidential, even from you, unless you apply for a loan
 - b) Private information, and cannot be accessed unless you give written permission
 - c) Public information, and can be accessed by anyone from potential lenders to future employers (*Future employers need written permission to access credit reports.*)
5. Information stays on your credit report:
 - a) For one year from the date it occurred
 - b) For seven years from the date it occurred (*Bankruptcies remain on your report for 10 years.*)
 - c) Forever
6. Which of these credit rating scores would give you the *lowest* interest rate?
 - a) 820
 - b) 620
 - c) 520
7. Your credit report includes your payment history for all your credit card accounts. It also shows:
 - a) Past and present employers
 - b) Where you've lived
 - c) Both of these

Your Car, Your Credit

It is the year after graduation, and you've been saving your money to buy a car. You have a steady job, so you assume you'll have plenty for monthly payments. If you don't, you figure you'll just cover extra expenses with your credit card. On the day you go to check out cars, it doesn't take long to find the one you want. Your heart is pounding with excitement. You're thinking, this is the day I drive off with my own car! You picture yourself gripping the leather steering wheel, the sun roof open, the windows down, your favorite song blaring from the radio....

But as you walk into the dealership to start paperwork, the salesman says, "I think I can get you a great deal on this baby, today. And we offer great financing, too – it all depends on your credit rating." Suddenly, the image of you and your car is getting blurry and a queasy feeling is rising in your stomach as the words "credit rating" echo in your ears. Credit rating?! What's that? Is it going to come between you and your dream car?

Is your strategy to cover extra expenses with your credit card a good one? Why or why not?

What do you know about credit ratings? How could your credit rating affect your car purchase?

How Much Will You Pay?

You are applying for a three-year (36-month) car loan for \$10,000. Check the credit rating you were assigned with the chart below and answer the questions.

Credit Score	APR (annual percentage rate)	Monthly Payment	Overall Payment	Total Interest
720–850	6.583%	\$307		
690–719	7.476%	\$311		
660–689	8.978%	\$318		
620–659	10.685%	\$326		
590–619	14.118%	\$342		
500–589	15.149%	\$347		
Below 500	LOAN DENIED			

1. What is the APR on your car loan? _____
2. What is the monthly payment? _____
3. Determine your overall payment and write it in the chart. (Hint: Multiply your monthly payment X 36 months.)
4. Determine the total amount of interest you will pay over the life of the loan and write it in the chart. (Hint: Subtract \$10,000 from your overall payment.)
5. Find a partner with a different credit rating. What is the difference between your monthly payments and theirs? _____
6. What is the difference between the total interest you pay and what your partner pays?

What's Behind Your Credit Rating?

Use the space below to list information included on a credit report.

1. Personal identification information such as _____

2. Public record information such as _____

3. Collection agency account information (explain) _____

4. Credit account information such as _____

5. Inquiries (explain) _____

The following companies provide credit reports:

- Equifax (www.equifax.com)
- Experian (www.experian.com)
- Trans Union (www.transunion.com)

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