The Centsables®

GRADES 6-8 LESSON PLAN

Lesson topic

What is a credit card and how does it work?

Instructional Objectives

Students will be able to:

1. Explain the concept of credit
2. Explain what a credit card is
3. Describe the difference between buying with cash and with a credit card

Essential Question

What does it really mean to use a credit card to buy something?

Financial Literacy Standards

National Standards for Financial Literacy, Council for Economic Education:

• **Standard IV, Using Credit, Benchmarks: Grade 4, (2) When people use credit, they receive something of value now and agree to repay the lender over time, or at some date in the future, with interest. (3) By using credit to buy durable goods-such as cars, houses, and appliances-people are able to use the goods while paying for them.**

• **Standard II, Buying Goods and Services, Benchmarks: Grade 8, (3) People choose from a variety of payment methods in order to buy goods and services. (4) Choosing a payment method entails weighing the costs and benefits of the different payment options.**

National Standards in K-12 Personal Finance Education, Jump$tart Coalition for Personal Financial Literacy:

• **Planning and Money Management, Standard 3: Describe how to use different payment methods.**

• **Credit and Debit, Standard 1: Identify the costs and benefits of various types of credit.**

Materials
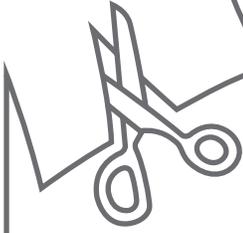
- A large display of the Credit Card Calculator table
- Copies of the Credit Cost worksheet for the students
- Credit Cost worksheet for the teachers
- Pencils for each student

Motivation

Say:

– Were you ever in a situation with a friend where you both wanted to buy an ice cream (or a snack at school, etc.) and you discovered that you didn't have enough money? Did your friend lend you the money and did you agree to pay him/her back the next day? Did you keep your promise to pay your friend back?

– If this, or something like it, sounds familiar, that's very much like using credit to make a purchase

– Using a credit card to buy something is like having someone who will lend you money whenever you need it! It is also an agreement or a promise that you will repay that loan. Just as you would do with your friend

– But, there is one BIG difference between borrowing money from your friend and buying something with a credit card, though. Who can tell us what that difference is?

– If you said, or were thinking, that the difference is that my friend would just expect me to pay back only the cost of the ice cream, but the credit card company or the bank would charge me a fee for lending me money, you're right! (A fee is a cost for something)

Learning Activity

Say:

– Let's say you saw an amazing bike that you would love to own. Your friends would flip to see you riding it down the street, because nobody has anything as cool. The bike is on sale for $400.00, but you don't have $400.00!

– Now let's pretend that you have a credit card. So you have the choice of using it to make your purchase. But you must promise to repay the entire amount over time (not the next day, but someday)

– You are now faced with an important decision, but before you make up your mind, you should understand how credit cards work

Key points to discuss

- When you use a credit card to pay for something, the bank is really lending you money. It uses its own money to pay for your purchase. Then the bank sends you a bill, and allows you to pay back the money to them over time.

- When the bank sends you a credit card bill each month, you have the choice of paying the entire amount at once, or of paying a portion of what you owe. That's pretty convenient, right? You get to enjoy what you bought – like that cool bike – right away without spending all that money to buy it!

Say:

– By slowly paying back the bank, you get to send them small payments each month that are probably a lot easier for you to handle than the full price of the bike

– The money that you send the bank each month includes a fee (or a cost) for borrowing the money called interest

– Each month, the bank will charge you interest for the convenience of using their money

– The longer you take to pay off your credit card bill, the more interest you will be paying. So you might end up paying a lot more for that $400 bike than you would if you paid in cash

– Any questions so far?

– Okay, let's get back to your important decision. You want to buy the bike but you don't have enough money

– Today we are going to explore together what buying the bike "on credit" really means to you

– We know the price of the bicycle is $400.00

– The bank is going to charge a fee for lending the $400.00 (not like your friend who lent you money for free)

– What is the fee we have to pay called? (Elicit: interest)

Do: Distribute copies of the Credit Cost worksheet. Display a large copy of the Credit Card Calculator table in front of the room

Say:

– Let's look at the Credit Cost Worksheet, and let's see what happens as you pay your credit card bill

– Your credit card balance is the total amount you borrowed for the bike. So write $400.00 on that first line

– The interest we have to pay is always given as a percent (%). We are going to pretend that the interest (or interest rate) is ten percent (10%). Write that on your sheet

– Ten percent (10%) is how much the bank will charge us each month on the amount of the $400 loan that we still owe them

– Each time we make a payment, part of that money goes toward paying the credit we owe, and what's left over goes toward paying back the original $400

– You decide that you can afford to pay more than the minimum and so you will make a payment of $30.00 each month. Fill that on your sheet

Do:

Display your large Credit Card Calculator table

Say:

– Look carefully at the Calculator table at the bottom of your sheet. Find month 1, and let's read across the table: what is your payment? ($30.00) How much of that payment is interest? It tells you in the next column ($3.33)

– Look at the fourth column with the heading "Principal Paid." This does not mean that you paid your school principal $26.67! Who can tell us what it means? (It is the amount of money from your payment that is subtracted from the original $400 you borrowed to make your purchase)

– How do we calculate this amount? We start with $30.00 payment, subtract the $3.33 in interest, and that equals $26.67

– Now look at the last column, "Remaining Balance." How much do you still owe the bank for the $400.00 bike after your make your first month's payment? (Elicit: $373.33)

Challenge

• How was the amount $373.33 calculated? (Elicit: $400.00-$26.67=$373.33)

Do:

Use the Credit Card Calculator table as the basis for exploring the answers to further questions. The following are suggestions:

Say:

– According to the table, how many months will it take to pay your bill in full? (15 months) Let's write 15 on your sheet

– Now here's a tricky question: What is the total amount of interest you will have paid? Who can tell us how to compute that? (add up all the "Interest Paid" amounts) Let's do that right now. (give them some time to do the addition, then elicit the answer: $25.80) Write that amount on your sheet

– Who can tell us the total cost of the bike after 15 months at the fixed rate of $30.00 each month? ($400.00+$25.80=$425.80) That goes on the last line of your sheet

– As you make your payments each month, what happens to the amount of interest you are charged? (It decreases) Why? (As the balance decreases, so does the amount of interest owed)

– What happens to the amount of principal being paid each month? (It gets larger) Why? (Less of the payment is needed to pay interest)

Challenge

• As an independent seat activity (or as part of the lesson Closure) you may make a T-Chart with Benefits on one side and Costs on the other and elicit lists of both from the students. For example...

• Benefits: Ability to make the purchase immediately; use of the product while paying for it; ability to buy something you might not otherwise be able to afford.

• Costs: You are promising to pay for the purchase, which might limit other purchase opportunities; you may not be able to pay back as quickly as you thought, which could result in increased interest costs.
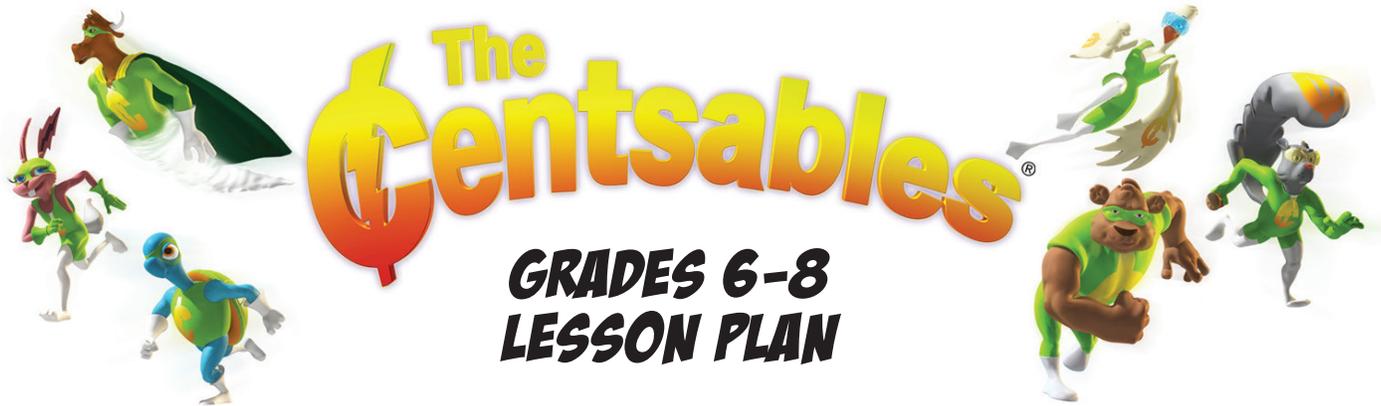
Closure/Summary

Elicit from students:

• Who would decide to buy the bike on credit? [ask for a show of hands] Who would wait until you saved up enough to pay for it in cash? [hands] Have several "credit" students and several "cash" students explain their answers.

• Who can give us a definition of credit without using the word? (It's a way to buy things, without using cash.)

• Why is buying with a credit card like making a promise? (Because you promise to pay the money back.)

• What happens if you do not pay the full amount of what you owe each month? (You will be charged interest.)

• By a show of hands, who thinks they will definitely get credit cards when they are older?
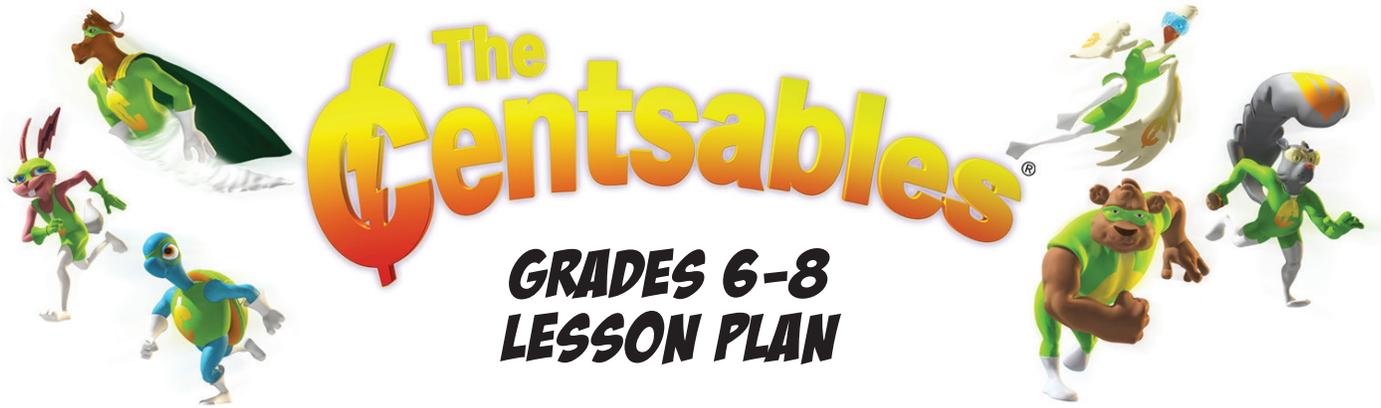
Credit Card Calculator

Month	Fixed Payment	Interest Paid	Principal Paid	Remaining Balance
1	$30.00	$3.33	$26.67	$373.33
2	$30.00	$3.11	$26.89	$346.44
3	$30.00	$2.89	$27.11	$319.33
4	$30.00	$2.66	$27.34	$291.99
5	$30.00	$2.43	$27.57	$264.43
6	$30.00	$2.20	$27.80	$236.63
7	$30.00	$1.97	$28.03	$208.60
8	$30.00	$1.74	$28.26	$180.34
9	$30.00	$1.50	$28.50	$151.84
10	$30.00	$1.27	$28.73	$123.11
11	$30.00	$1.03	$28.97	$94.13
12	$30.00	$0.78	$29.22	$64.92
13	$30.00	$0.54	$29.46	$35.46
14	$30.00	$0.30	$29.70	$5.75
15	$5.80	$0.05	$5.75	$0.00

Credit Cost student worksheet

What is your credit card balance? _____
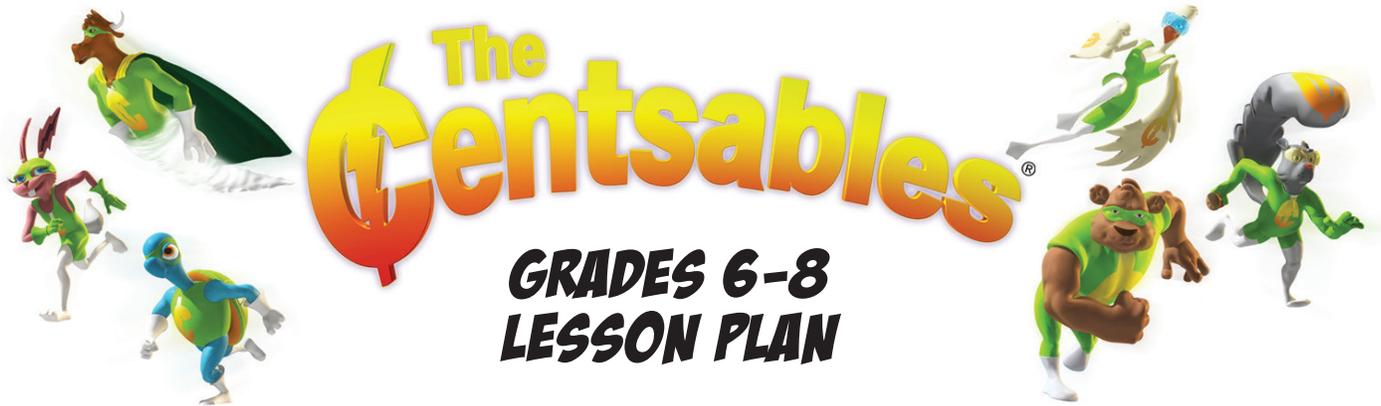
What is the interest rate on your credit card? ___

What payment will you make each month? _____

It will take you ___ months to be rid of your debt.

You will pay _____ in interest.

Your total cost for the bike is _____

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Credit Cost teacher worksheet

What is your credit card balance? $400.00

What is the interest rate on your credit card? 10%

What payment will you make each month? $30.00

It will take you 15 months to be rid of your debt.

You will pay $25.80 in interest.

Your total cost for the bike is $425.80

Month	Fixed Payment	Interest Paid	Principal Paid	Remaining Balance
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