

LESSON: Cost of borrowing

Financial Literacy Outcome

At the end of this lesson, students will:

- analyze the role and importance of credit in personal finance.

Curriculum Expectations

Grades 9 and 10, Business Studies (2006)

Introduction to Business (BBI1O/2O)

Finance

- Analyze the role and importance of credit in personal and business finance.
- Explain the advantages and disadvantages of both consumer credit and business credit.

Grades 11 and 12, Social Science and Humanities (2000)

Managing Personal Resources (HIP3E)

Social Structures

- Evaluate the cost and implications of buying on credit (e.g., credit cards, bank loans, mortgages) and assess the benefits of alternative approaches.
- Demonstrate an understanding of how to complete banking transactions (e.g., by completing forms to open accounts and to deposit withdraw funds; writing cheques; using a cheque register; applying for credit cards and loans).

Grades 11 and 12, Mathematics (2007)

Mathematics for Work and Everyday life (MEL3E)

Comparing Financial Services

- Gather, interpret and compare information about the costs (e.g. user fees, annual fees, services charges, interest charges on overdue balances) and incentives (e.g. loyalty rewards; philanthropic incentives such as support for Olympic athletes or a Red Cross disaster relief fund) associated with various credit cards and debit cards.

- What You Need**
- Lab (optional)
 - How do credit cards work (Appendix 5.1)
 - Creating public awareness (Appendix 5.2)
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- Minds On**
- Class: Video**
- Get it on Credit
[http://www.getsmarteraboutmoney.ca/en/managing-your-money/planning/managing-debt/Pages/video-get-it-on-credit.aspx?group=Funny Money&page=1](http://www.getsmarteraboutmoney.ca/en/managing-your-money/planning/managing-debt/Pages/video-get-it-on-credit.aspx?group=Funny%20Money&page=1)
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- Action**
- Individual: Handout**
- Distribute handout How do credit cards work (Appendix 5.1)
 - Take up or assess student answers – you may want to clarify the assessment task
- Individual: Internet Discovery**
- Using online credit card calculators, see effect of different rates and payments options – use example lesson, What is credit?
<http://getsmarteraboutmoney.ca/tools-and-calculators/credit-cards/default.aspx>
Try different amounts – have students compare adding \$5 or \$10 above minimum payment amount to see difference it makes
Have students examine college or university debt
<http://getsmarteraboutmoney.ca/tools-and-calculators/student-loan/default.aspx>
 - Using the Internet, develop 10 tips to use credit cards wisely
<http://www.cbc.ca/news/canada/story/2011/10/25/credit-card-tips.html>
<http://www.fcac-acfc.gc.ca/eng/resources/publications/paymentoptions/tscreditshop-eng.asp>
- Individual: Assessment (Optional)**
- Have students create a brochure or primer for selecting a credit card and tips for its use -- Creating public awareness (Appendix 5.2).
- You could also have them create a youtube or animoto video that shows tips for selecting and using their credit cards.*

Consolidation/ Debrief

Choose one activity

Individual/Class: Quiz about selecting credit cards

- Wrap up with a quiz

See sample credit card quiz (Appendix 5.3)

OR

<http://www.fcac-acfc.gc.ca/eng/resources/toolCalculator/CreditCard/quiz/CreditCardQuiz-eng.asp?sn=0>

<http://www.themoneybelt.ca/tools-atelier/quiz-teste/card-carte-eng.asp?q=1>

There are sample quizzes available online. Take care that you select Canadian sites as there are some differences between US and Canadian legal obligations for credit cards.

Can be done individually or as an entire class exercise using whiteboard or clickers.

- Wrap up with online activity

<http://getsmarteraboutmoney.ca/en/education-programs/for-teachers/curriculum-tools/multimedia-resources/Documents/CreditScores/index.html>

Appendix 5.1: How do credit cards work?

1. You present your credit card to the cashier (depending on the card, you may be asked to enter a PIN).
2. The merchant gets electronic authorization for the purchase and records your transaction on a purchase statement.
3. You receive a copy of the statement (depending on the credit card you have, you may be asked to sign the purchase statement).
4. The financial institution or retailer sends you an invoice or statement listing your purchases, the amount owed, and the due date.
5. You pay the financial institution or retailer on time.

Review the Buy Now & Pay Later statement and answer the questions on the next page.

Buy Now & Pay Later First National Bank of Ontario		Credit Card Statement		
Name: Raj Smith	Previous balance	\$124.32	Credit Limit	\$500.00
Account #: 6230 0100 0156 8219	Less: Payments & credits	\$124.32	Available credit limit	\$307.70
Statement Date: January 13, 2011	Plus: New charges / adjustments, interest etc.	\$192.30	Payment period remaining	
	Equals: New balance	\$192.30	If each month you pay the minimum amount due only	1 year and 11 months
	Minimum payment due on February 3, 2011	\$10.00		
Date of purchase	Description	Amount		
Dec. 14, 2010	AA Fashion Store, Bontown	\$84.75		
Dec. 24, 2010	Electronics & Accessories, Bytown	\$75.00		
Jan. 1, 2011	World Downloads, Newtown	\$23.99		
Jan. 10, 2011	Fast Food Kiosk, Folksview	\$8.56		
Interest rate: 18%				

1. What was the period during which the purchases were made?

a) How many days are in this payment period?

b) What was the total amount of purchases made during the statement period?

c) What is the minimum amount that must be paid by the due date?

2. If interest rate was calculated using the following formula:

$$\text{Interest charges for month on overdue balances} = \frac{\text{Interest rate per year}}{12} \times \text{Balance owed}$$

a) What is the yearly interest rate charged on overdue balances?

b) What is the monthly interest rate charged on overdue balances?

c) How much interest would you be charged if you forgot to make the payment owed to the credit card issuer?

3. How long would it take to pay off this debt if you make only the minimum monthly payments?

Appendix 5.1: How do credit cards work? - Answers

1. What was the period during which the purchases were made? **Dec 14 – Jan 13**
 - a) How many days are in this payment period? **30**
 - b) What was the total amount of purchases made during the statement period? **\$192.30**
 - c) What is the minimum amount that must be paid by the due date? **\$10**
2. If interest rate was calculated using the following formula:

$$\begin{array}{l} \text{Interest charges for month} \\ \text{on overdue balances} \end{array} = \frac{\text{Interest rate per year}}{12} \times \text{Balance owed}$$

- a) What is the yearly interest rate charged on overdue balances? **18%**
 - b) What is the monthly interest rate charged on overdue balances? **1.5%**
 - c) How much interest would you be charged if you forgot to make the payment owed to the credit card? **\$2.88**
3. How long would it take to pay off this debt if you make only the minimum monthly payments?
23 months

Appendix 5.2: Creating Public Awareness

Background

Student debt in Canada now totals \$20 billion and continues to grow. The average varies widely by province, from \$15,000 in Quebec to an estimated \$35,000 in Nova Scotia.

The high cost of post-secondary education means that many students are borrowing more and falling deeper into debt in order to get a post-secondary education.

Many students find themselves turning to credit cards and lines of credit because they aren't eligible for student aid, which is determined by using a formula that takes into account how much their parents should be able to contribute.

Six out of 10 young Canadians, aged 18 to 29, are in debt of some kind, with credit card debt being the most common, followed by student loans, according to a 2008 EnviroNics survey. One in five had debts totaling more than \$20,000. Half of those with debt felt that their debt level was as much or more than they could handle. These numbers are conservative. As the study notes, three in 10 surveyed either did not know their debt level or would not divulge that information.

Introduction

You have been hired to prepare a student brochure or video on how to appropriately deal with credit. Your public awareness project should include considerations when selecting a credit card and tips for its use.

What to Include

- Glossary of Terms
- Credit, debt, statement, interest, principle, annual percentage rate (APR), credit rating, grace period, cash advance fee, currency exchange
- Things to consider when selecting a credit card
- Tips for using a credit card



Appendix 5.3: Credit card quiz

True/False

Indicate whether the statement is true or false.

- _____ 1. Last month, your credit card balance was zero. This month, your statement shows that you made a \$500 purchase. If you can pay off only \$450 by the due date indicated on your statement, you will be charged interest only on the \$50 left to pay.
- _____ 2. You are carrying a \$1,000 balance on your credit card: \$800 for purchases you made two months ago, and \$200 for cash advances you took this month. Your credit card agreement says your annual interest rate is 16% for purchases, and 20% for cash advances. When you make a \$300 payment, the issuer will apply it to your purchases, because they occurred first.
- _____ 3. You won't pay interest on a cash advance as long as you pay your credit card bill in full by the due date indicated on your statement.
- _____ 4. If you frequently pay your credit card just a couple of days after the due date, this won't affect your credit rating.
- _____ 5. Credit rating agencies will charge you a fee for sending you a copy of your credit report by mail.

Multiple Choice

Identify the choice that best completes the statement or answers the question.

- _____ 6. Getting the lowest rate possible when borrowing money could be a function of one or more of the following factors.
 - a. Borrowing record
 - b. Loan history
 - c. Credit risk
 - d. All of the above
- _____ 7. A credit report is...?
 - a. A list of your financial assets and liabilities
 - b. A monthly credit card statement
 - c. A loan and bill payment history
 - d. A credit line with a financial institution

- _____ 8. When we're talking about credit cards, what do the letters APR stand for?
- a. Accelerated percentage rate.
 - b. Average percentage rate
 - c. Annual percentage rate.
 - d. Anticipated performance rate
- _____ 9. Which of the following can hurt your credit rating?
- a. Making late payments on loans and debts
 - b. Staying in one job too long
 - c. Living in the same location too long
 - d. Using your credit card frequently for purchases
- _____ 10. Jack is having trouble paying his credit card bill this month. What should he do?
- a. Ignore it and wait until he has the money.
 - b. Get another credit card and use that one to pay the first card.
 - c. Call his credit card company to discuss his options.
 - d. Screen his calls to avoid bill collectors.