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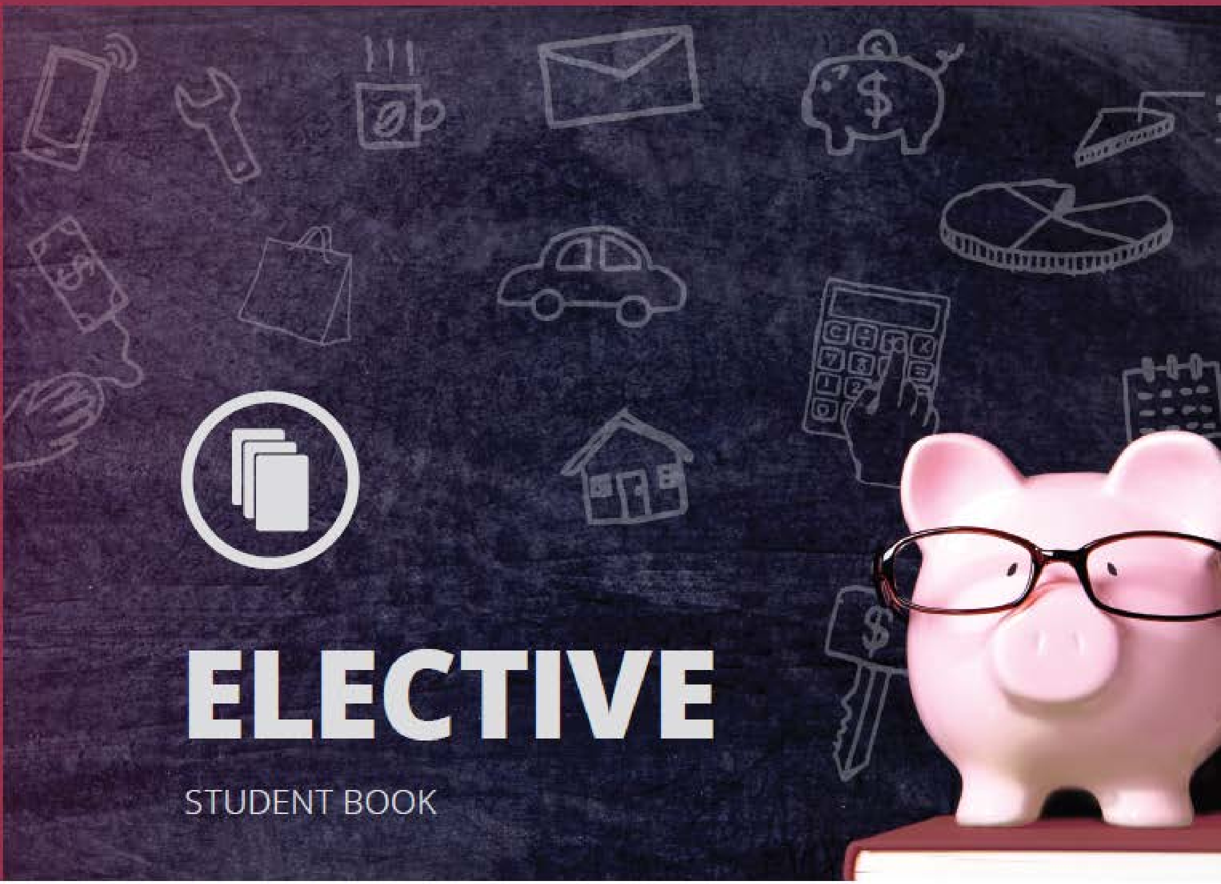

ELECTIVE

STUDENT BOOK

Consumer Math | Unit 10

AOP

1. INCOMES, BANKING, AND BUDGETING

Income is the foundation of all financial planning. In this section, you'll review different sources of income and paycheck calculations and deductions. With an income comes the need to find a banking solution. You'll review different types of financial institutions, tools and resources typically offered by banks, and strategies to consider when choosing a bank. You'll also review strategies for creating a budget and being a smart shopper so you can make the most of the money you earn and save!

Section Objectives

Review these objectives. When you have completed this section, you should be able to:

1. Identify sources of income.
2. Define key terms related to income.
3. Identify tools that will help manage money.
4. Identify the major types of financial institutions.
5. Identify banking services, tools, and resources that will help you.
6. List resources available to research career options.
7. Describe a strategy for organizing personal finances.
8. Describe a budget and the benefits of having one.
9. Identify examples of spending wisely.

Vocabulary

Study these words to enhance your learning success in this section.

asset	**ATM**	**bank**	**budget**
capital gains	**commission**	**credit union**	**debit card**
deduction	**direct deposit**	**discount**	**dividends**
employee benefits	**FDIC**	**financial**	**fixed expenses**
gross pay	**impulse purchases**	**income**	**interest**
statement period	**taxable income**	**variable expenses**	

Note: All vocabulary words in this unit appear in **boldface** print the first time they are used. If you are unsure of the meaning when you are reading, study the definitions given.

SOURCES OF INCOME

Income is the foundation of **financial** planning. Without income, how would plan a **budget** to spend, save, and grow your money? So, when considering financial planning, income is a good place to start. While a job will likely be your main source of income, it's important to understand employment isn't the only source of income. There are many different ways people earn money, or income.

A few sources of income include:

- **Capital gains**—income earned by the sale of **assets**
- **Commission**—a percentage of a sales price paid to a sales employee for their sale or service
- **Dividends**—money paid to people who own stock in a company from the company earnings
- **Rent**—money paid to a property owner
- **Tips**—money given to service workers for their service
- **Interest**—money a bank pays you for keeping your funds in an account

Most income is taxed by state and federal governments, meaning you must pay a certain percentage of the income to the governments. **Taxable income** includes:

- salary
- interest on any bank accounts
- interest on all bonds except municipal (tax-free) bonds
- dividends
- bonuses
- unemployment compensation
- tips
- capital gains
- gambling and lottery winnings
- most withdrawals from a retirement account

The more sources of income you are able to acquire, the more income you'll be able to make. But since employment is the primary source of income for most people, let's review paycheck basics.

Complete these activites

1.1 Wages from an employer are the only source of income.

a. true b. false

1.2 Tips are considered __________.

a. a bonus b. gains c. taxable income d. dividends

1.3 Susan bought some land. She sold it for $3,000 more than she paid for it. The $3,000 is an example of __________.

a. interest b. dividends c. capital gains d. rent

1.4 Rick works off commission. He earns 10 percent of all manufacturing equipment he sells. If he made a sale of $9,000, how much was his commission?

a. $900 b. $100 c. 90 d. $9,000

1.5 When a company makes earnings or a profit, and they share this profit with the stockholders, it's called __________.

a. dividends b. interest c. gains d. tips

Paychecks. Most people today have pay directly deposited into their bank account and receive a pay statement either in the mail or through email. Whether you receive a physical check or choose **direct deposit**, the pay statement has important information that should be reviewed to ensure your pay and **deductions** are correct.

Deductions are amounts subtracted from your pay, and they typically include Social Security tax, Medicare tax, state or local taxes, and health insurance. It's a good practice to keep pay statements for your records. This can help with budgeting, reviewing your earnings, and potential applications for credit, which sometimes require proof of income.

A pay statement will typically include:

- your hourly pay rate and hours (if you are paid by the hour)
- the pay period and year-to-date pay
- **gross pay** (before deductions)
- net pay (after all deductions)
- each deduction

If you are an hourly employee and work overtime, you'll also see your overtime pay and hours listed on the pay statement. Some employees are paid salary, which means they have a set annual income. Salaried employees cannot earn overtime pay, but some positions earn bonuses or stipends, which are funds paid for extra duties or meeting specified goals.

Not all pay statements look the same. Some may also include accrued sick and vacation time. Some employers offer paid sick and vacation days that can be accrued or earned after certain periods of time. Your personal information, such as your name, address, and employee number, will appear on the pay statement.

Some employers also offer certain benefits in addition to pay. While the benefits may not be income, they do have monetary value that can reduce other spending, making them valuable.

Some **employee benefits** may include:

- **health insurance plans**—typically medical, dental, and vision
- **retirement plans**—typically a 401(k) or defined-benefit plan
- **tuition reimbursement**—used for schooling
- **stock purchase plan**—the opportunity to buy stock in the company at a discount

Career Choices. You may already know what career you plan to pursue, or you may still be considering different options. Either way, the career you choose will impact your income. Researching things like job descriptions, education and skills requirements, future job outlook, advancement opportunities, and average salary will help you identify a career you enjoy that meets the income standards you hope to achieve.

The Bureau of Labor Statistics (BLS) website is a great place to gather information on many different job industries, including salary and hiring trends. The BLS publishes the Occupational Outlook Handbook, which provides detailed breakdowns on occupations, including median pay, required education, training, projected number of jobs, and job growth rate data.

Some career choices will include additional options for income streams. For example, sales jobs may have opportunities for commission and bonuses. Employee benefits like health insurance plans, retirement plans, and stock purchase plans can also save you money and earn additional income.

Complete these activities.

1.6 Diana's gross pay was $890, and her total deductions were $89. What is her net pay?

a. $89 b. $979 c. $890 d. $801

1.7 In one to two sentences, list some deductions you may see on your pay statement.

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1.8 In one to two sentences, explain where you could find the average or median salary for an occupation you're interested in.

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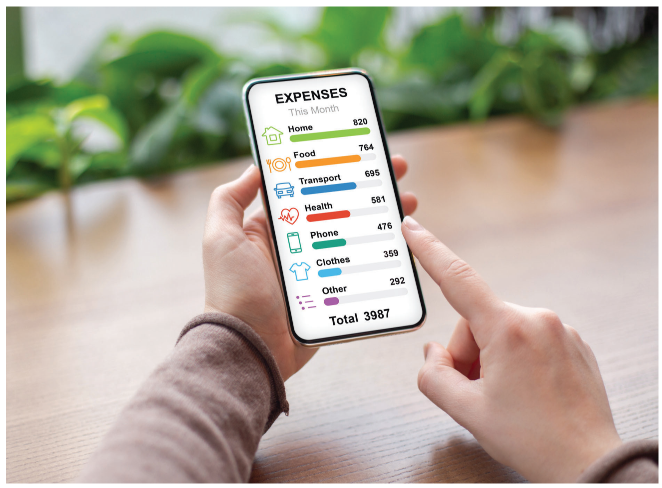
SMART SHOPPING

Spending less than you make is a most important habit to reach your financial goals. Spending wisely keeps you from owing banks and credit card companies large amounts of money. So how do you spend money wisely? Some great tips include:

- avoiding **impulse purchases**
- looking for bargains
- buying high quality
- using credit cards infrequently
- thinking about what's most important
- tracking your spending

We're all vulnerable to impulse buying. You're hungry and drive by a fast-food place that looks delicious. Or you walk through a store and see clothing you know you'd love. Or you see an advertisement for the latest smart phone, and you suddenly realize you really want to upgrade. As tempting as impulse spending is, doing it regularly can lead to overspending and increased debt. Creating and sticking to a budget will help you avoid impulse buying. And when shopping, be sure to create a list and stick to that as well. A set budget and shopping lists will help you plan your purchases and live within your means.



Bargain shopping can be fun. When you plan your purchases ahead of time, that also gives you time to search for good deals, search for **discounts** or coupons and read product reviews. Bargain shopping doesn't mean buying low quality items, which may break or fail and end up costing you more money. But if you check product reviews, you'll be able to identify good deals and discounts that are also high-quality products.

Paying cash (or using a debit card that is the same as cash) for the majority of your purchases will also help you spend wisely. Using credit cards infrequently will reduce the amount of interest you spend. The best way to use credit is to pay the full statement amount each month so you don't way any interest, but at least keeping the balances very low will keep any interest that accrues to a minimum.

Considering whether purchases are *wants* or *needs* will also help you prioritize any spending. A need will be something like gas in your car to get to work or groceries for the week. A want will be something like a music streaming service or trendy new shoes. Prioritizing purchases that are most important will help you ensure you take care of your needs before you spend money on wants.

Tracking your spending is another tool for the wise spender. Sometimes we don't realize how much we're spending or patterns of irresponsible spending. Keeping a spending diary that's handwritten or saving receipts and updating an online budget with each expense and purchase will provide you with great information to analyze any patterns in spending.

For example, perhaps you find you're spending too much right after you receive each paycheck. You're excited to get paid and so you always do some impulse buying. Or maybe you realize you're spending too much money on fast food, and you need to better plan grocery shopping and start eating at home. Tracking your spending will help you identify any irresponsible habits and better manage your spending.

Write *T* for True or *F* for False.

1.25 ____________ Avoiding impulse spending is a good tip for spending wisely.

1.26 ____________ Avoiding buying gifts is a good tip for spending wisely.

1.27 ____________ Borrowing money from your friends is a good tip for spending wisely.

1.28 ____________ Looking for bargains is a good tip for spending wisely.

1.29 ____________ Tracking your spending is a good tip for spending wisely.

1.30 ____________ Using credit cards infrequently is a good tip for spending wisely.

Complete these activities

1.31 In one to two sentences, describe how you can spend wisely or improve your spending habits.

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CHECK ____________ ____________
Teacher Date

Review the material in this section in preparation for the Self Test. The Self Test will check your mastery of this particular section. The items missed on this Self Test will indicate specific areas where restudy is needed for mastery.

SELF TEST 1

Write the letter of the vocabulary word that matches the correct definition (each answer, 2 points).

1.01	____________	portion of income subject to taxes	a. budget
1.02	____________	item that is owned and has value	b. debit card
1.03	____________	plan for how you will spend and save your money	c. deduction
1.04	____________	money paid to people who own stock in a company	d. gross pay
1.05	____________	purchase that is not planned	e. taxable income
1.06	____________	used like a credit card, but money is deducted from checking account	f. variable expenses
1.07	____________	anything to do with money and investments	g. dividends
1.08	____________	earnings before deductions from work or other sources	h. commission
1.09	____________	government corporation that supplies deposit insurance to protect money in American banks	i. asset
1.010	____________	amount that is subtracted	j. FDIC
1.011	____________	costs that change in amount	k. impulse purchase
1.012	____________	Fee paid to an employee for transacting business or performing a service	l. financial

Write *T* for True or *F* for False (each answer, 3 points).

1.013 ____________ When choosing a bank, you should compare their services.

1.014 ____________ You can pay your bills online from your bank's website or app.

1.015 ____________ Gross pay is income before deductions.

1.016 ____________ Very few banks are FDIC members.

1.017 ____________ Banks provide all services for free.

1.018 ____________ Tracking your spending is a way to become a smart spender.

1.019 ____________ Earning interest from shares in a company is a source of income.

1.020 ____________ Some banks charge fees for certain tools and services.

1.021 ____________ All banks offer the same services.

List the four steps in creating a budget (each answer, 2 points).

1.022 ______________________________

1.023 ______________________________

1.024 ______________________________

1.025 ______________________________

Write five tips for spending your money wisely (each answer, 2 points).

1.026 ______________________________

1.027 ______________________________

1.028 ______________________________

1.029 ______________________________

1.030 ______________________________

Circle the correct answer (this answer, 2 points).

1.031 On the __________ website, you can find median salaries for job industries.

a. Bureau of Labor Statistics b. Bureau of Jobs c. Better Business Bureau

1.032 __________ may sometimes include health insurance, retirement plans, tuition reimbursement, and stock purchase plan.

a. Employee plans b. Employee benefits c. Employee rights

1.033 Kevin bought some land. He later sold it for $2,500 more than he paid for it. The $2,500 is an example of __________.

a. interest b. dividends c. capital gains d. rent

1.034 Carrie works off commission. She earns 5 percent for the products she sells. If she made sold $9,000 of product for one month, how much was her commission for the month?

a. $450 b. $90 c. $900 d. $45

1.035 When a company makes earnings or a profit, and they share this profit with the stockholders, it's called __________.

a. dividends b. interest c. gains d. tips

1.036 Income that is taxed by the state and federal governments is __________ income.

a. federal b. state c. additional d. taxable

INVESTMENTS

Insurance helps protect your money and investments help increase your money. There are many different types of investment accounts, some available through your bank or credit union, and some available as separate accounts. Start with a savings plan. Think about short-term savings goals like a trip or a car, as well as long-term savings goals like buying a home and retirement.

Planning for short and long-term savings goals will help you identify the types of investment accounts that are appropriate.

Beyond the traditional savings account—which also earns interest—there are several types of savings accounts banks offer, each with different rules and interest rates, that earn higher interest. When considering savings accounts, keep in mind the annual percentage yield (APY), any interest thresholds, and variable interest rates. APY is the amount of interest you can earn in one year from a savings account. The higher the APY, the higher your **rate of return** will be. The interest threshold is the balance amount you need before a bank will behind paying interest. Variable interest rates are different interest rates paid for different size balances, with higher balances earning higher rates.

Special savings accounts and savings products include:

- savings bonds
- CDs
- money market accounts
- 529 plans
- IDA
- club accounts
- treasury securities

Savings bonds are issued by the U.S. government. You are essentially providing a loan to the government and earning interest on the loan and the government pays you interest. CDs or certificates of deposit are a type of savings account that offers the highest interest of any savings options at banks. If you deposit money in a CD, you can't make deposits or withdrawals during the term or period of time set by the bank. A money market is similar to a traditional savings account, but they offer a higher rate of interest. A 529 plan is a college savings plan designated for future college expenses.

An IDA, or individual development account, is a special type of savings account designated to help low-income individuals start a business, pay for education, or buy a home. In an IDA savings account, an organization matches the money you deposit. A club account is a savings account used for special activities such as a holiday or vacation. These accounts have higher interest rates, but there are restrictions for withdrawals and you're required to make regular deposits.

Remember the PACED decision-making model!

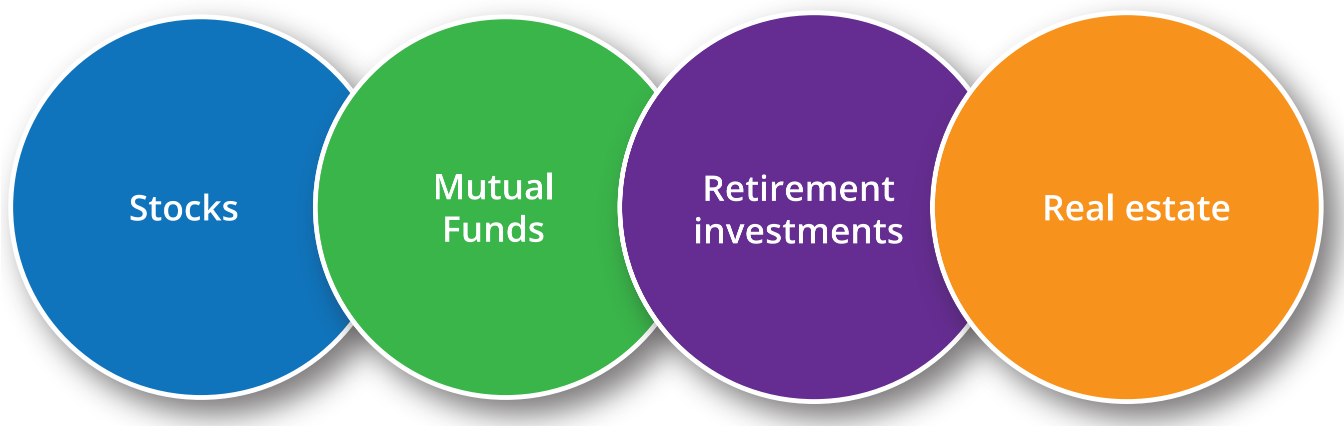
Lastly, treasury securities are sold by the U.S. Department of Treasury. This U.S. government division sells treasury securities such as savings bonds, treasury bills, treasury notes, and treasury inflation-protected securities.

Remember the PACED decision-making model? This is a good tool for making savings and investment choices.

The time to consider **investing** will be here before you know it! You'll likely start with savings accounts, but for longterm goals, investing may grow your money at a faster rate. Investing is often higher-risk, but the rate of returns or earnings from your investments will likely be higher than savings accounts. The major differences between investing and saving include:

Investing	Saving
risky	safe
potentially earns more money	earns a lower amount in interest
not federally insured	federally insured
sometimes earns money through dividends	no dividends; earns interest
necessary to sell an investment to use the money	no need to sell; withdrawals permitted

Some common types of investments include:



A **stock** is a **share** of ownership in a company; so, when you buy stock, you actually become part owner of the company. Owning stock makes you a shareholder. If the company does well, the value of your stock increases and you make money. But if the company does poorly, your stock can lose value and you may lose money. People buy and sell stocks through the stock market, also called the stock exchange.

The New York Stock Exchange (NYSE) and NASDAQ are the biggest stock markets, or exchanges, in the United States. Let's review the process.

First, a company that's publicly owned sells shares of stock to raise money to operate or expand its business. Or an individual might decide to sell shares of stock they own. Once shares of stock are available for purchase, and an individual decides to buy some of those shares, the individual puts in an order to buy stock with a stockbroker.

Next, a broker notifies the person that trades the stock for their firm. Trade is just another way of saying to buy or sell. The trade is executed either electronically or on the exchange floor. So, if the trade is made at the NYSE on the exchange floor, the person who is buying the stock for their firm finds another person on the floor who is willing to sell the stock. The two people agree on a price. If it's sold electronically, the sale is made online. The broker keeps track of the trade and notifies the individual when the stock has been purchased and the price for which it was purchased.

Then, the person who purchased the stock waits and watches how the stock is doing by looking at stock quotes. Finally, when the individual is ready to sell his stock, they submit an order with a broker to sell the stock. Again, the broker makes sure the trade is executed electronically or on the exchange floor. The money from the sale is either sent to the seller as a check or deposited into the seller's account.

Complete these activities.

2.23 The stock market is __________.

a. the same as a brokerage firm
b. an organized way for people to buy and sell stocks
c. a place where you buy and sell stock
d. the section of the newspaper where you look up how much a stock is worth

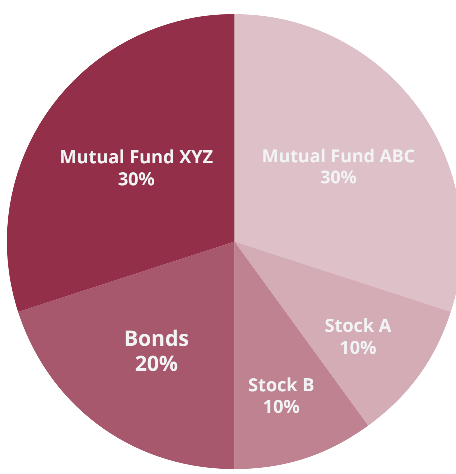
2.24 Julian would like to buy stock. What should he do?

a. He should visit the stock market, open an account, and purchase stock.
b. He should choose a broker, open an account, and deposit money, or buy stock directly from the company.
c. He should go online to the NYSE site and buy stock.
d. He should go to her bank and fill out the necessary documents.

2.25 A stockbroker __________.

a. manages a mutual fund
b. buys and sells stock
c. works on the trading floor at the NYSE

Mutual funds are a lower risk investment. A mutual fund is a professionally managed collection of money from a group of investors. The money in a mutual fund is invested in many different stocks and bonds. A **fund manager** decides where to invest the money and you pay a small percentage of the investment to pay this expert to manage the fund.



Retirement Investments. Retirement investments vary, but most allow you to invest money pre-tax, or before taxes are taken out. For example, for a 401(k), you can have a certain amount of your paycheck deposited in the account before taxes are withdrawn. Oftentimes you can choose different types of investments for a 401(k), such as stocks, bonds, and mutual funds, allocating a certain percent to go to each type of investment. For example, you may choose to have 30 percent go into one mutual fund, 30 percent to a different mutual fund, 20 percent to bonds, 10 percent to a certain stock, and 10 percent to another stock.

Three types of common retirement investments are the 401(k) plan, a 403(b) plan, and an IRA.

- A 401(k) is a retirement plan that some private corporations offer their employees.
- A 403(b) plan is similar to a 401(k), but is offered to employees of some nonprofit organizations, such as schools and hospitals.
- An IRA is a retirement plan for individuals who earn under a certain amount per year or who do not have the opportunity to invest in a 401(k) or a 403(b).

A Roth IRA is similar to, but has some differences from a traditional IRA. A traditional IRA allows you to invest money before taxes, and you cannot access your account without paying penalties until you reach retirement age. At that point, you can begin making withdrawals, but they will be subject to state and federal taxes. You pay taxes before depositing into a Roth IRA account, but when you reach retirement, the funds can be withdrawn tax free. And once you've made regular deposits for at least five years, you can access your funds without penalty, even before reaching retirement age.

Some employers offer pension plans, or defined-benefit plans, in which the employers contributes to a pool of funds set aside for the worker's future benefits. Some defined-benefit plans allow employees to contribute to the plan and some match a percentage of contributions. Most pensions today are offered by government or state institutions and organizations. For example, For example, the California Public Employees' Retirement System (CalPERS), an agency in the California executive branch that manages pension and health benefits, is the largest public pension fund for California public employees.

With most employer-sponsored retirement plans, an employee must be vested before an employer will begin matching contributions. Common vesting periods are three to five years.

Write *T* for True or *F* for False.

2.26 ____________ A 401(k) is a workplace retirement savings account.

2.27 ____________ Funds contributed to a 401(k) are taken from your paycheck before taxes.

2.28 ____________ 401(k) plans have a Roth IRA option.

2.29 ____________ Roth IRA contributions are taxed, but funds withdrawn after retirement are not taxed.

2.30 ____________ The IRS limits the amount of money you can contribute to an IRA.

2.31 ____________ Pensions are also called defined-benefit plans.

2.32 ____________ Pensions are very common workplace retirement plans today.

Fill in the blanks

2.33 A(n) ________________________ is a type of investment that involves buying a share of a company

2.34 _________ or _________ are types of retirement investments offered to employees.

2.35 A(n) __________________ is a type of retirement investment offered to employees of some non-profit organizations.

2.36 A(n) ________________________ is a professionally managed collection of money from a group of investors.

2.37 A(n) ________________________is a person who decides where to invest money in a mutual fund.

2.38 A(n) ________________________ investment lets you save and invest money tax-free until you withdraw it when you retire.

CHECK _______________ _______________
Teacher Date

Real estate may also be considered a type of investment because real estate may grow in value over time, just like investment accounts. Like some other types of investments, it can be risky. Land, residential homes, and commercial homes may increase in value or they may decrease in value over time. The real estate market also changes over time with average interest rates for loans increasing and decreasing, so there are times when many people are buying and selling and times when not many people are buying or selling.

Review the material in this section in preparation for the Self Test. The Self Test will check your mastery of this particular section. The items missed on this Self Test will indicate specific areas where restudy is needed for mastery.

3. CREDIT SCORES, CREDIT CARDS, AND CONSUMER LOANS

Most people use credit, taking out credit cards and different loans, and understanding how they work, how to find the least expensive options, and smart strategies to use them wisely will help you reduce expenses and save money. In this section, you'll review how credit scores are calculated and what to consider when choosing a credit card. You'll also review common options for mortgages, home equity loans, auto loans, and college education loans.

Section Objectives

Review these objectives. When you have completed this section, you should be able to:

20. Identify types of credit.
21. Understand what is reported to credit bureaus.
22. Identify the factors lenders consider when making credit decisions.
23. Explain how a credit score affects creditworthiness and the cost of credit.
24. Define key financial terms associated with credit cards.
25. Define key terms associated with mortgages.
26. Identify various types of mortgages.
27. Identify costs associated with mortgages.
28. Identify various types of loans, including student loans, home equity loans, and auto loans.

Vocabulary

Study these words to enhance your learning success in this section.

APR	**cosigner**	**credit limit**	**credit report**
credit score	**creditworthy**	**debt**	**FASFA**
finance charges	**fixed rate**	**grace period**	**grant**
inquiry	**installment loan**	**lender**	**minimum payment**
periodic rate	**principal**	**scholarship**	**secured loan**
Truth in Lending Disclosure	**unsecured loan**	**variable rate**	

Note: All vocabulary words in this unit appear in **boldface** print the first time they are used. If you are unsure of the meaning when you are reading, study the definitions given.

BEING CREDITWORTHY

Showing you can be trusted to make payments on time and repay **debt** makes you creditworthy. Practicing responsible borrowing habits will improve your **credit score**, which makes you more likely to be approved for loans and credit cards at lower interest rates. **Lenders** use tools to help them decide who can borrow money and how much money they can borrow. These tools are a **credit report** and **credit score**.

Types of Credit and a Credit Report. Credit allows you to buy now with the promise to pay later. Credit cards are one type of credit, but there are other types as well. For instance, loans are another type of credit. The four basic types of credit are credit cards, service credits, loans, and installment credit.

- Credit cards are issued by individual stores, banks, or credit card companies.
- **Service credit** is a promise to pay for services, such as telephone, gas, electricity, and water. Since you don't pay for the water before you use it, it's considered credit.
- Loans allow borrowers to obtain money with the promise to pay it back. Loans can be for small or large amounts, and the amount may be loaned to you for a few days or several years. The money can be repaid at one time or in regular payments.
- Installment credit allows the borrower to take a product home with a promise to pay later. The product may be a large appliance or furniture. You usually sign a contract, make a down payment, and make regular payments, called installments.

A credit report is a little like a report card that shows how **creditworthy** you are. A credit report includes some basic personal information, such as your name, current and previous addresses, telephone number, Social Security number, date of birth, and current and previous employers. It contains a credit history for each credit account you've owned, including the date it was opened, **credit limit** or loan amount, balance, monthly payment, and your payment pattern over the past several years, including any bankruptcies or unpaid balances. Your credit report also shows your job history, if you own your own home, and if you've been sued or arrested.

It's best to know what's on your credit report before you try to obtain credit. Experts recommend that you obtain a copy of your credit report at least once per year.

There are three main credit bureaus: Equifax, Experian, and TransUnion. You're allowed to get one free credit report from each credit reporting agency per year. If there's an error, you can dispute it either by submitting a dispute on the credit bureau website or by writing to the credit bureau. To order a credit report, you'll want to use the official site created by the three reporting companies: www.annualcreditreport.com. Avoid the other sites that claim to offer free reports because they charge a fee.

When you apply for a loan or credit card, lenders will request a copy of your credit report from a credit bureau, which will report an **inquiry** on your credit report. The lender will evaluate how responsible you are based on your credit report and decide whether they'll approve or deny you. If payments on any loans or credit cards have been late or missed, the lenders report the information to the credit bureau, and it shows on the report and lowers your credit score.

Credit Score. Lenders don't always look at a complete credit report. Sometimes they rely on one number called a credit score, which is also called a FICO score. FICO is an acronym for Fair Isaac Corporation, which created the score. It's based on information taken from the full credit report. Think of your credit score as a number that predicts the likelihood that a debt will be repaid on time.

About thirty factors from the credit report are used to determine a credit score. Some of these factors include the following:

» **Payment history**—Does the record show many late payments? Or does it show bankruptcy, or an account turned over to a collection agency?

» **Outstanding debt**—How much does an individual owe on credit cards and to banks?

» **Credit history**—How long has an individual had his oldest account?

» **Application for new credit**—How many new accounts has the individual tried to open? How long has it been since the individual tried to open a new account?

» **Types of credit in use**—How many credit accounts are already open?

A credit score is generated by a computer using a formula and the above information. This number ranges from 300 points to 850 points. In general, you are likely to obtain credit easily if your FICO score is high. Some lenders consider a score of 650 or above high. Scores between 620 and 650 are considered average and indicate basically good credit. Scores below 620 are considered low.

Credit Score	Rating	Impact
300-579	Very Poor	These individuals often have difficulty being approved for new credit.
580-669	Fair	These individuals are often considered subprime borrowers. They may have trouble qualifying for new credit or will pay high interest rates if approved.
670-739	Good	These individuals are generally viewed by lenders as acceptable or low-risk borrowers.
740-799	Very Good	These individuals have demonstrated a history of positive credit behavior and will easily be approved for credit at lower interest rates.
800-850	Excellent	These individuals are viewed as very low-risk and will be approved for credit at the lowest interest rates.

Complete these activities.

3.1 A credit score of 590 is considered __________.

a. good b. very poor c. fair

3.2 A person with a good credit rating is viewed by lenders as __________.

a. low-risk b. subprime c. very low-risk

3.3 A higher credit score predicts you'll be __________.

a. risky b. dependable c. accessible

3.4 Different lenders and credit reporting agencies use __________.

a. different scoring models b. the same scoring models c. FICO scores

3.5 In a few sentences, explain how a credit score affects creditworthiness and the cost of credit.

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Using Credit Responsibly. How do you act responsibly so that you have a good credit score and credit report? Here are some tips for using credit responsibly and maintaining creditworthiness.

- Protect your credit card and account numbers to prevent unauthorized use.
- Quickly report lost or stolen credit cards.
- Open only a few credit cards. Too many credit cards can make overspending tempting.
- Pay cash when you can and pay full credit card balances or at least more than **minimum payments** each month.
- Look for credit cards that have no annual fees and lower interest rates.
- Read the terms of the credit carefully and make informed decisions.
- Don't spend more than your credit limit.

Write *R* for responsible credit use or *I* for irresponsible credit use.

3.6 ____________ Jillian has a credit card bill of $2,000. She makes only the minimum payment and is always close to the limit on her credit card. Is Jillian using credit responsibly?

3.7 ____________ Cher isn't able to pay her larger credit card bill so she takes a cash advance from a smaller credit card to make the payment.

3.8 ____________ Phoebe has several credit cards, but the balances are low and she checks her budget each month to make sure her debt-to-income ratio stays below 20 percent.

3.9 ____________ Marc gets a $500 bonus from work. He has credit card debt, so he uses $400 to pay toward his debt and saves $100 for a trip he's saving for.

3.10 ____________ Xavier uses his credit card for gas all month, but he pays off the balance of the card at the end of each month.

UNDERSTANDING CREDIT CARDS

Credit cards can be wonderfully convenient. However, if you overuse a credit card, it can lead to heavy debt and hurt your credit score. Understanding how credit cards work can help you avoid this. Some credit card companies charge high interest rates, and high interest rates make your purchases even more expensive.

Finance charges are the interest and fees you pay for making purchases using a credit card. Something that originally cost $1,000 at the store, for instance, could end up costing you twice as much if you're being charged a high interest rate and you take a long time to pay the balance off.

There are two interest rates you should be familiar with. One is the **APR**, or annual percentage rate, and the other is the periodic interest rate. The APR is the annual percentage you're charged for borrowing money. Notice it's a yearly interest rate. However, credit card companies don't charge interest just once per year. Interest will be charged to your account every payment period, which is usually monthly. If you divide the APR by twelve (because there are twelve months in one year), you will get the **periodic rate**. So, the periodic rate is used to calculate the interest you pay in one payment period. For example, if the credit card has an APR of 18 percent, you can divide the 18 percent by 12 to calculate the periodic rate.

$$18\% \div 12 = 1.5\%$$

When you buy something with a credit card and pay the entire balance, you pay only the purchase price—nothing extra. Credit card companies typically have a **grace period**—typically about 21 days—before interest starts accruing. If you pay any purchases off during the grace period, you won't have to pay interest.

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