***Lesson 6.3: Credit Cards***

**Read this page on your own before we begin the lesson.**

Your credit card is tied to a credit account — which is a borrowing tool and a form of debt. But unlike an installment loan, like the car loan we did in lesson 6.2, a credit card is a form of revolving credit. This means that instead of borrowing all the money at once like you do with a loan, you borrow as you spend with a credit card. Every time you make a purchase with your credit card, you are doing it with the issuer’s money, not your own. A credit card account will have a limit. This is the maximum amount the credit card company will let you borrow on the account. Any transactions charged to a credit card are added to your credit card balance. This is the amount of money you’ve borrowed by charging purchases to your credit card but have yet to repay. You add to your credit card balance every time you swipe your credit card, and you lower it every time you make a credit card payment. The minimum payment is the amount you must pay each month to keep your credit card accounts in good standing. Your minimum payment will be due on your credit card due date each month. A minimum payment is calculated based on your credit card balance. *It is usually two to three percent of your credit card balance, or the outstanding interest you owe plus one percent of the balance*. Most credit card issuers also have a flat amount that is the smallest they’ll charge on a credit card each month, typically $15 to $35. The minimum payment on a credit card is small compared to your overall balance. It’s also recalculated each month. This means that the [average credit card balance](http://www.marketwatch.com/story/how-long-does-it-take-to-clear-a-2000-credit-card-with-minimum-payments-2015-07-07) can take over a decade to repay with minimum payments alone — and you’ll pay hundreds in credit card interest during that time. Credit card interest, also called a credit card finance charge, is the cost you pay to have a balance. This is set by your [credit card annual percentage rate (APR)](https://studentloanhero.com/featured/credit-card-apr-effects/), which is the rate at which your balance accrues interest. You will usually have a 25-day grace period to repay a balance with your credit card issuer before it charges interest on the borrowed money. Pay off your credit card in full each month and you won’t pay credit card interest. But if you charge, say, $100 this month and only pay $50 back, you’ll accrue interest on the remaining $50 until you repay it. Therefore, you should always pay more than the credit card minimum to keep balances low. It will also help you avoid credit card interest and serious credit card debt. Credit card companies also change your APR when you fail to make a minimum payment.

1. Watch this video to see how interest accrues. <https://www.youtube.com/watch?v=SnlHbMIWJak>

2. What is a typical interest rate for a credit card if you have “good” credit? Research here. <https://wallethub.com/edu/average-credit-card-interest-rate/50841/>

3. What is the average credit card debt held by the average American household? Research here. <https://www.valuepenguin.com/average-credit-card-debt>

References Elyssa Kirkham https://studentloanhero.com/featured/how-do-credit-cards-work/

**Problem 1: BRITNEY**

1. Britney Pender is a 17 year old high school junior. Her grandparents gave her a car last summer when she got her driver’s license, but last week when she went to drive home from her part time job it wouldn’t start. Her parents had it taken to a dealership and they have reported that the car needs a new transmission. It will cost $4788 to fix the car. Britney certainly doesn’t have that kind of money and neither do her parents, so her parents put it on one of their credit cards. Britney’s parents know they won’t be able to pay this off quickly, so they will pay the minimum payment each month until it is paid off. They have pretty good credit so their interest rate is 20.31%. The credit card charges a minimum payment of 3% of the balance or $25, whichever is highest each month. How long will it take Britney’s parents to pay off this credit card?

**Problem 2: WILMA**

2. Wilma has gotten herself into a little bit of a pickle. As a new college graduate, she got a good job with a decent salary, but she didn’t set a budget and has been using a credit card for the past year whenever she didn’t have enough money at the end of each month to pay all of her expenses. After one year her credit card balance is $2420 (yikes). Since she doesn’t have a solid credit score her interest rate is 33.85%. She realizes she has to get some help and pay this debt off as soon as possible. She seeks advice from a financial adviser who helps her decide what monthly payment she should use to pay off this debt in 24 total months. What is the monthly payment that Wilma should pay?