Qualifying for loans

Students apply their understanding of secured or unsecured loans as they write a description of an individual who may or may not qualify for each type of credit.

Learning goals

Big idea

Borrowers may qualify for different types of loans based on their credit history.

Essential questions

- How might a person's credit habits and decisions influence their ability to borrow money?
- What are some facts about credit scores that could influence lenders when a person wants to borrow money?

Objectives

- Understand the characteristics of secured and unsecured loans
- Identify credit habits and choices that could help or hurt a person's credit history

KEY INFORMATION

Building block:

Financial knowledge and decision-making skills

Grade level: High school (9–12)

Age range: 13–19

Topic: Borrow (Getting loans, Managing credit)

School subject: CTE (Career and technical education), English or language arts, Social studies or history

Teaching strategy: Cooperative learning, Personalized instruction

Bloom's Taxonomy level: Understand, Apply

Activity duration: 45–60 minutes

National Standards for Personal Financial Education, 2021

Managing credit: 12-2, 12-8, 12-9, 12-10, 12-12

These standards are cumulative, and topics are not repeated in each grade level. This activity may include information students need to understand before exploring this topic in more detail.

NOTE

Please remember to consider your students' accommodations and special needs to ensure that all students are able to participate in a meaningful way.

What students will do

- Review the characteristics of secured and unsecured loans.
- Write a description of individuals who do or don't qualify for a secured loan or an unsecured loan based on their credit history.

Preparing for this activity

- ☐ While it's not necessary, completing the "Differentiating between secured and unsecured loans" activity first may make this one more meaningful.
- ☐ Print copies of all student materials for each student, or prepare for students to access them electronically.

What you'll need

THIS TEACHER GUIDE

- **Qualifying for loans** (guide)
  cfpb_building_block_activities_qualifying-loans_guide.pdf

STUDENT MATERIALS

- **Qualifying for loans** (worksheet)
  cfpb_building_block_activities_qualifying-loans_worksheet.pdf

Exploring key financial concepts

Credit offers seem to be everywhere, but not everyone who applies for a loan qualifies for it. Creditors often evaluate a person's credit history to determine whether they will lend to that person.

Secured loans require the borrower to provide collateral (something of value like a car, a boat, a home, etc.) that the bank or lending institution can take if the borrower can't pay back the loan. If a person cannot pay back a secured loan, the lender can take steps to take the collateral and sell it. (If the lender sells the collateral for more than the person owes – including the lender's expenses – the lender may have to give the person the rest of the money.) The person can also face debt collection, can have negative information filed on their credit report, and may be sued.

TIP

Because financial products, terms, and laws change, students should be encouraged to always look for the most up-to-date information.

In contrast, unsecured loans require no collateral, so the bank or lending institution is trusting that these borrowers will pay them back. This trust is based on their credit history—what borrowers have done in the past that gives them a good credit rating. Because unsecured loans put lenders at higher risk, they may have a higher interest rate than secured loans. If a person cannot pay back an unsecured loan, they can face debt collection, can have negative information filed on their credit report, and may be sued.

Teaching this activity

Whole-class introduction

- Ask students if they or someone they know has ever borrowed money.
- Ask students what kinds of things people might consider before borrowing money.
  - Examples may include whether and when the borrower can pay the money back or how much the lender would be willing to lend.
- Read the "Exploring key financial concepts" section to students to explain the differences between secured and unsecured loans
- Be sure students understand key vocabulary:
  - **Credit report:** A summary of your credit activity and current credit situation such as loan paying history and the status of your credit accounts. Lenders use these reports to help them decide if they will loan you money and what interest rates they will offer you. Other businesses might use your credit reports to determine whether to offer you insurance; rent a house or apartment to you; or provide you with cable TV, Internet, utility, or cell phone service. If you agree to let an employer look at your credit report, it may also be used to make employment decisions about you.
  - **Lender:** An organization or person that lends money with the expectation that it will be repaid, generally with interest.
  - **Loan:** Money that needs to be repaid by the borrower, generally with interest.
  - **Secured loans:** Loans in which your property (a thing you own) is used as collateral; if you cannot pay back the loan, the lender takes your collateral to get their money back. The lender can also engage in debt collection, can file negative information on your credit report, and might sue you.

TIP

Visit CFPB's financial education glossary at consumerfinance.gov/financial-education-glossary/.

- **Unsecured loan:** A loan (such as most types of credit cards) that does not use property as collateral; lenders consider these loans to be more risky than secured loans, so they may charge a higher rate of interest for them. If the loan is not paid back as agreed, the lender can also start debt collection, file negative information on your credit report, and might sue you.

Individual and group work

- Create groups of three to four students.
- Distribute the "Qualifying for loans" worksheet to each student.
- Explain that each student will write a description (using one of four scenarios on the worksheet) of a person whose credit history either allowed or didn't allow them to get a specific kind of loan.
- Have groups decide who will write the description of each type of potential borrower listed on the worksheet.
    - If any group has fewer than four students, group members can choose which scenarios they'll focus on.
- After students have finished, have them share their descriptions with the class.

Wrap-up

If time allows, ask students to share what differences they noticed between people who did or didn't qualify for the loan.

Suggested next steps

Consider searching for other CFPB activities that address the topic of borrowing, including getting loans and managing credit. Suggested activities include "Calculating loan payments" and "Determining how down payments affect loans".

You also may consider having students get an estimated credit score at the FICO Score Estimator[1] at https://www.myfico.com/fico-credit-score-estimator/estimator.

Measuring student learning

Students' answers on their worksheets and during discussion can give you a sense of their understanding. **Keep in mind that students' answers may vary, as there may not be only one right answer.** The important thing is for students to have reasonable justification for their answers.

1 The CFPB does not endorse this third party or guarantee the accuracy of this third-party information.