

PFL Academy

Chapter 60: Understanding Financial Contracts — Student Activity Packet

The Challenge: What Are You Really Agreeing To?

Only 7% of people read end-user agreements before clicking "I agree." Yet these contracts can cost you thousands of dollars in unexpected fees, lock you into unfavorable obligations, and give up important rights.

A student who didn't read her apartment lease discovered she owed **\$3,800** in termination penalties when she got a job offer in another city. A man who signed a "free" phone contract found he'd owe **\$1,150** to cancel early.

Your Goal: Develop contract literacy to identify essential elements, spot red flags, and protect your financial interests before signing.

Learning Objectives

- Identify the five essential elements that make a contract legally binding
- Interpret common legal terminology and contract clauses
- Analyze contract terms to understand rights, obligations, and potential risks
- Evaluate the financial implications of different contract types
- Apply contract literacy skills to protect personal interests

CORE CONCEPTS

Term	Definition
Contract	Legally enforceable agreement requiring: offer, acceptance, consideration, capacity, and legality
Consideration	Something of value exchanged between parties (money, services, goods, or promises)
Capacity	Legal ability to contract: 18+ years old, mentally competent, not under duress
Breach of Contract	Failure to fulfill contract obligations; can result in legal remedies and penalties
Fine Print	Often-overlooked clauses containing important fees, penalties, and limitations
Arbitration Clause	Requires disputes be resolved through private arbitration, not courts
Automatic Renewal	Contract continues unless you actively cancel, often requiring advance notice

The Five Essential Elements of a Valid Contract

- 1. Offer:** A clear proposal to do or provide something specific
- 2. Acceptance:** Unconditional agreement to the offer's terms
- 3. Consideration:** Each party exchanges something of value
- 4. Capacity:** Parties are legally able to contract (age, mental competence, no duress)

5. Legality: The contract's purpose must be legal

Part A: Identifying Contract Elements (12 minutes)

Instructions: Read each contract excerpt and identify the essential elements present.

Contract Excerpt 1: Gym Membership Agreement

"I, the undersigned member, agree to pay FitLife Gym \$49.95 per month for a 12-month membership period beginning on the date of enrollment. In exchange, FitLife Gym agrees to provide access to all gym facilities during operating hours. Member must be at least 18 years of age. This agreement may be cancelled within 72 hours of signing without penalty."

Element	Present? (Y/N)	Evidence from Contract
Offer		
Acceptance		
Consideration		
Capacity		
Legality		

Is this a valid, enforceable contract? Why or why not?

Contract Excerpt 2: Car Sale Between Friends

"I promise to sell my 2018 Honda Civic to Mike for \$12,000. Mike promises to pay me in full within 30 days. Vehicle will be transferred upon receipt of payment."

Element	Present? (Y/N)	Evidence from Contract
Offer		
Acceptance		
Consideration		
Capacity		
Legality		

What's missing from this contract that could cause problems?

Part B: Red Flag Identification (15 minutes)

Instructions: Read each contract clause and identify potential red flags. Rate each from 1 (minor concern) to 5 (major red flag).

Clause 1: Automatic Renewal

"This agreement shall automatically renew for successive one-year terms unless Member provides written notice of cancellation at least 60 days prior to the renewal date. Renewal will occur at the then-current membership rate."

Red flag rating (1-5): ____

Potential problems with this clause:

Clause 2: Arbitration Requirement

"Any dispute arising from this agreement shall be resolved through binding arbitration. Customer waives all rights to participate in class action lawsuits and agrees that disputes will be arbitrated on an individual basis only."

Red flag rating (1-5): ____

What rights are you giving up?

Clause 3: Unilateral Modification

"Provider reserves the right to modify these terms at any time. Continued use of services after modifications are posted constitutes acceptance of new terms."

Red flag rating (1-5): ____

Why is this problematic?

Clause 4: Early Termination Penalty

"Tenant may terminate this lease early upon 60 days written notice and payment of an early termination fee equal to two (2) months' rent plus forfeiture of security deposit."

Red flag rating (1-5): ____

If rent is \$1,200/month and deposit is \$1,200, what's the total early termination cost?

Two months' rent: $\$1,200 \times 2 = \$$ ____ Plus forfeited deposit: $\$$ ____ Total early termination cost: $\$$ ____

Red Flag Summary: Common contract red flags include: automatic renewal, arbitration requirements, unilateral modification rights, excessive penalties, liability waivers, and vague termination procedures. Always calculate the WORST-CASE cost before signing!

Part C: Contract Comparison Challenge (15 minutes)

Scenario: You need a cell phone plan. Compare these three options and determine which is best for your situation.

	Plan A	Plan B	Plan C
Monthly cost	\$80	\$55	\$70
Contract length	2 years (24 months)	No contract	1 year (12 months)
Phone included?	"Free" \$950 phone (financed)	No, bring your own	\$200 subsidy on phone
Early termination fee	\$350 + remaining phone balance	\$0	\$150
Auto-renewal?	Yes, to 2-year term	No	Converts to month-to-month

Calculate Total 24-Month Cost (if you stay full term):

Plan A: $\$80 \times 24 = \$$ _____ (phone "included") Plan B: $\$55 \times 24 = \$$ _____ + \$400 phone purchase = \$_____ Plan C: $\$70 \times 12 = \$840 + \$70 \times 12$ (month-to-month) = \$_____ + (\$600 phone - \$200 subsidy) = \$_____

Calculate Cost If You Leave After 10 Months:

Plan A: $\$80 \times 10 = \$800 + \$350$ ETF + \$_____ remaining phone balance = \$_____ Plan B: $\$55 \times 10 = \$550 + \$400$ phone = \$_____ Plan C: $\$70 \times 10 = \$700 + \$150$ ETF + \$400 phone cost = \$_____

Analysis Questions:

Which plan is cheapest over 24 months?

Which plan is cheapest if you might leave after 10 months?

Which plan would you choose and why?

Key Insight: "Free" usually isn't free. The \$950 phone in Plan A is financed into your payments and owed if you leave early. Plan B's flexibility costs more monthly but gives maximum freedom.

CHECK YOUR UNDERSTANDING

1. Which element is NOT required for a valid contract?

- A Consideration (exchange of value)
- B Notarization (notary signature)
- C Capacity (legal ability to contract)

D Acceptance (agreement to terms)

2. An arbitration clause in a contract typically:

A Increases your legal remedies if something goes wrong

B Requires disputes to be settled privately, not in court

C Allows you to sue for unlimited damages

D Has no effect on your legal rights

3. "Unilateral modification rights" in a contract means:

A Both parties must agree to any changes

B One party can change the terms without the other's consent

C The contract cannot be modified once signed

D Modifications require court approval

4. A 16-year-old signs a gym membership contract. This contract is:

A Fully valid and enforceable

B Voidable by the minor (they can cancel it)

C Automatically void from the start

D Only valid if a parent co-signs

5. Short Answer: You find a great apartment and the landlord wants you to sign the lease immediately, saying "another applicant is very interested." What should you do, and why?