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by brette sember

WHAT TO TEACH YOUR KIDS ABOUT CREDIT

MOST OF US probably headed out into the world without a very good understanding of how credit really works and how to use it responsibly. If the recent credit crunch is any indication, this country has a real problem with credit. The average household carries \$8000 in debt on their credit cards, and has 12.71 credit cards. There are 1.3 billion credit cards in use in the U.S. at this time. 43% of households spend more than they earn each year. We spend a lot of time on religious education, instrument lessons, sports practice, dance lessons, not to mention SAT prep course and possibly tutors in specific subjects to help our kids learn and grow, yet not many parents spend a lot of time helping kids learn about money and credit.

Start Young

Your five year old doesn't need to know a lot about credit. At this age, he's still trying to learn to count money and is finding out how to spend it. Help your preschooler learn to save money. If he gets \$20 for his birthday, suggest he save half and spend half. Start a piggy bank or even a real savings account for your child. Learning to save is an important skill and one that does not come naturally to many kids. Saving, is after all, a kind of impulse control. Just as

you probably don't let your child eat all his Halloween candy in one sitting, you shouldn't let him spend all his money at once either.

Young children can start to understand the concept of credit. After all, your child has seen you use credit cards, so it's a good idea to explain what it is. Tell your child that the credit card allows you to buy things all month long and then pay for them all at once at the end of the month. Tell her if she bought a piece of gum from you every day of the week for ten cents but you let her use credit, she would have to pay you seventy cents at the end of the week. It's the same concept – buy now and pay later.

Encourage Kids to Think about Money

When your child is of elementary and middle school age, you know he understands how money works, but he still needs to be taught how to think about money. Explain to your child what a budget it – you as an adult have to create a budget for the household and can't run out and spend every paycheck on clothes, video games, or candy because otherwise there wouldn't be money to pay for electricity, gas or food. Encourage your child to make thoughtful purchases (avoiding impulse purchases when

possible). Savings should be something that your child is expected to create and maintain. Encourage her to watch her savings grow and praise her for doing so.

If your child wants to purchase something she doesn't have the money for, allowing her to borrow it from you is fine, as long as you set up and enforce a repayment schedule. This is a great way to help kids learn credit in a hands on way. Help your child understand what purchases are beyond her means. If she wants to buy a \$100 item, but only earns \$5 a week in allowance, it will take her 20 weeks (almost five months) to pay that back.

Moving Toward More Responsibility

By the time your child has become a teen he will hopefully have learned a lot of financial lessons from you. However, these are the years during which you can have the most impact on how he will manage money as an adult. Encourage your teen to set up a budget that includes expenses such as school lunches, entertainment, gifts for friends and family, and savings. Give your teen an allowance or require him to use money from a job to cover these expenses. Help her understand how to use the money carefully so all expenses can be met (he will need a budget). Give your teen the register from her savings account and teach him how to balance it against bank statements and keep it up to date.

Once your teen is driving (and is even more independent) you might want to consider having a card issued to her from one of your credit card accounts. You will remain the account holder, but she can be listed as an authorized user. Sit her down and talk about how

you use credit. Explain that credit cards are a convenience that allow people to pay for things with one bill at the end of the month (and yes, you should be paying that balance off each month and teaching your teen to do the same). Tell her what expenses she is authorized to put on the card (maybe you will want to limit it to gas or school supplies). Expect her to retain the receipts and be prepared to provide an accounting of exactly how he used it. If you will allow her to use the card for personal discretionary spending (like movies or eating out), you can expect her to pay you back for all items charged to the card by the date the monthly bill is due.

Doing this gives her the power to use a credit card, but with your close oversight and guidance. Many teens get their first individual credit card in their own name when they go off to college, so this allows him to try a credit card with training wheels before then.

Explain That There is Oversight

Teens also need to understand what credit reports and credit scores are. A credit report is like a report card for how well you pay back your loans and credit cards. It shows late payments or missed payments. A credit score is like an overall grade for how well you manage your credit. This is real life though and not school and every mistake you make with credit will haunt you for at least seven years (the length of time an item remains on a credit report). If you have bad credit, you won't be able to get a car loan or a mortgage when you want it. Teach your teen to get his free credit report every year from all three major credit reporting agencies at www.annualcreditreport.com. Show him your own credit report and explain how to read it.

Ten Rules to Teach Your Teens about Credit and Debt

1. Credit is not evil or bad, it is just a useful tool adults can take advantage of.
2. Using a credit card is a real loan. It is not "free money" or a license to spend.

3. Credit cards can be very convenient and helpful if you use them correctly.

4. The balance on a credit card should be paid off every single month. If you don't pay off the balance on a credit card, you will pay a very high interest rate.

5. You should never buy something on a credit card if you don't have the money to pay for it.

6. It is OK to take out other kinds of credit – such as car loans or mortgages – without paying them off immediately, but you must be sure you can make the monthly payments for the entire length of the loan.

7. If you pay a credit card late, it will damage your credit rating and make it harder for you to get other credit.

8. Make sure your teen understands that student loans are not forgivable in bankruptcy – any school loan your child

takes out will have to be repaid. The same is true of tax debt.

9. Any time you spend beyond your means you are guaranteed to end up with debt you cannot pay. Teens need to be reminded to think about the future and how a big purchase today will leave them strapped for cash a month from now.

10. Store cards that offer "no interest and no payments" for six months or a year are a great deal – but only if your teen divides the amount charged by the number of months the offer is in effect and pays that sum each month, so the whole debt is paid before interest kicks in. If any debt remains after the free period, interest is charged on the entire purchase.

*Brette Sember is a former attorney, mom of two children and author of *The Everything Kids' Money Book* and *The Complete Credit Repair Kit* and has taught a course about credit and debt for Barnes and Noble University. Her web site is www.BretteSember.com*

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