Money and You: Subjects your kids won't be studying

by Carrie_Schwab_Pomerantz

"Back to school." Time for new clothes, new notebooks and pencils. And for teens who don't have one, a savings account.

Why a savings account? Because one of the topics your teens should be learning about is personal finance, and the chances are good that your child isn't going to find "Money 101" on the curriculum this fall. Just seven states require students to learn about personal finance, which is particularly troubling given how little today's teens know about the subject.

According to a recent survey Schwab conducted on teens and money:

- More teens have cell phones (74 percent) than savings accounts (60 percent).

- Just 41 percent know how to budget their money.

- Nearly a third of teens are in debt, and only 26 percent understand credit cards fees and interest.

- Only 22 percent know how to invest money to build wealth and a mere 13 percent know what a 401(k) plan is.

Of course I realize that building wealth and 401(k) plans are hardly top of mind for teenagers. But the fact is that teens do need to know about personal finance now. They are already active consumers and borrowers, and some are even savers and investors. It should be equally obvious that knowing about spending and saving, understanding and using credit, and investing for the future are vital to their futures. Today's teens, after all, are tomorrow's adults.

Which begs the question: How are you going to teach tomorrow's adults how to manage their money responsibly and effectively? You're going to give them some practice, that's how. And in this column and the next, I'll provide some specifics. This week it's saving, budgeting and learning how to handle credit responsibly. Next week we'll move on to investing.

The importance of budgeting: The most fundamental concept of money management is budgeting, and there's no better time to start teaching this concept than when your kids are teenagers. Start with an exercise to help them understand the basics. Have them write down everything they spend in a week. Then review the list together (a good time to talk about the difference between necessities and luxuries, between needs and wants) and use it to determine a reasonable allowance. I suggest giving your older kids a monthly as opposed to weekly allowance that will cover all their expenses - everything from bus fare and lunch money to funds for clothes and a cell phone - and make them responsible for using it wisely. It only takes a couple of experiences of being broke on the 25th of the month to teach them a little prudence. When they realize you're not going to buy them that new cell phone they've been eyeing, it might prompt them to save or get a job.

Starting early when it comes to saving is valuable. When my own children were quite small, I opened savings accounts in their names and encouraged them to put aside at least a third of their allowances and any monetary gifts they might receive. The goal was to make saving second nature in order to instill the habit of saving for the future. And when they were barely teenagers, I opened custodial accounts to get them started, in a small way, with the markets and investing.

Even if your teens aren't savers yet, encourage them to put something away. As an incentive, you might agree to match any savings they voluntarily make. You should explain to them the power of compound growth. If your 16-year-old could put $1,000 into a Roth IRA from her summer job and it grew an average of 8 percent a year until the first year she could make a withdrawal at age 59, that would turn into almost $35,000; if she could maintain the $1,000/year savings rate (at the same average annual return), she would end up with about $450,000.

The savings habit is particularly valuable for the young because if they start early, they'll have to save a lot less for long-term goals like retirement. If they start saving 10 percent of their income when they enter the workforce in a few years, they'll probably never need to save a larger percentage. Someone who waits until he or she is in his or her 30s will need to save about 20 percent of his income - and the percentage just keeps rising the older he or she gets.

The true cost of credit cards and debt: Some 29 percent of the teens we surveyed owed money, an average of close to $300. It may seem surprising that I'm a proponent of credit cards for teens; however, my endorsement only holds when there is proper supervision. Credit cards are useful in emergency situations and essential for certain purchases, but - and this is a huge but - if you decide to get your teen a credit card, you also have to teach him or her the rules of the road. After all, high-cost debt with non-deductible interest is an enormous problem for millions of Americans.

That's why I'm teaching my children to think of the credit card as a financial tool, not a substitute for cash. I do not want them to use a card to pay for a cup of coffee or their favorite energy drink, and I do expect them to pay the balance in full and on time every month to avoid interest charges and penalties. Make sure your kids understand the fine print so they know how expensive it can be to carry a balance or to be late with a payment. And review their monthly statement to see how they're using them.

If you've been waiting to hear some good news, there actually is some. Our survey revealed that the overwhelming majority of teens want to learn about money and personal finance. And they want to learn it from their parents. So start by teaching your kids how to be smart about their own money today; it's the best way for them to learn to be smart about their money when it really counts.

Next week: Tips for teaching them about the markets and investing.

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