



NATIONAL ENDOWMENT FOR
FINANCIAL EDUCATION

MAKE SURE THAT YOUR CHILD'S FIRST CREDIT CARD EXPERIENCE ISN'T A DISASTER

Help Your Teenager Learn to Manage Credit Under Your Watch

ENGLEWOOD, COLORADO—First date, first job, first car...life is full of new experiences for teenagers, and each one brings its own risks, rewards and responsibilities. Many of these "firsts" are accompanied by the advice and guidance of parents. But, when it comes to a teenager's first credit card, some parents are afraid that their child may be courting fiscal disaster, so they simply avoid the issue altogether.

However, like it or not, credit cards are part of American life, and parents would do well to teach their teens how to manage credit wisely before they head into the world.

"Until they turn 18, teenagers can't obtain a credit card without their parents' permission, but as soon as they reach their 18th birthday, the credit card offers start pouring in," says William L. Anthes, Ph.D., president and CEO of the Colorado-based National Endowment for Financial Education® (NEFE®). NEFE is a nonprofit foundation that promotes financial well-being for all Americans.

Anthes says, "If parents wait until their children enter college or are ready to leave home to teach them about smart credit management, it could be too late."

The facts back up Anthes' concern. According to Nellie Mae, a leading originator of student loans, more than 80 percent of college undergraduate students have at least one credit card, and they reported an average credit card balance of \$2,327 in 2001. Graduate school students surveyed by Nellie Mae in 2003 had racked up an average credit card debt of \$7,831. They also reported holding an average of six credit cards each. This heavy reliance on credit by young people is beginning to have extremely negative consequences. Young Americans aged 25-34 have the second-highest rate of bankruptcy (just after those aged 35-44), according to a report released in 2004 by Demos, a nonpartisan research group.

Anthes says, "The best way to help your teenager avoid financial disaster when it comes to credit cards is to demonstrate how to use credit before the stakes are too high. Just as you wouldn't teach your child how to drive on the highway before he or she learned to brake, you shouldn't expect that your teen automatically will understand how to use credit responsibly. Start slowly, and you can be sure that your child will become a savvy credit

user."

To help teens make a successful transition to their first credit card, Anthes offers the following suggestions.

- **Learn to manage cash first.** Before handing over a credit card, give your child plenty of practice with cash. If the teen has a part-time job or you provide an allowance, expect the child to pay for certain expenses, such as clothes or movies, out of these funds. Help your child set up a savings account, and insist that he or she contribute to it on a regular basis. Open a checking account so the teenager can practice writing checks and balancing a checkbook. Show your child how to make a budget, stick to it and save for what he or she wants. "The goal is to instill in teens the values of saving and careful spending. If teens get into trouble by overspending, parents shouldn't bail them out. For example, if your child spends too much on clothes and then can't afford lunch for two weeks, help him or her establish a plan for payment, but don't just hand over the cash," Anthes says.
- **Start with a debit card.** One way to give your teen experience with plastic while protecting him or her from debt is to provide a debit card. Because the money instantly comes out of the teen's savings or checking account, this type of card reinforces the importance of limiting spending. "Be sure to remind your teenager to save receipts for purchases and deduct the amount from his or her bank balance immediately," Anthes says.
- **Consider a secured credit card.** A bank can set up this type of credit card for your teen, with the card's credit limit generally equal to the amount of money in the young person's savings account. If the teen fails to make the monthly payments, the bank taps into the savings account for reimbursement. A secured credit card can help your teen get used to handling credit and build a credit history, without incurring debt. As an alternative to a secured credit card, consider a card with a low credit ceiling, such as \$500.
- **Get a joint card with your teen.** Apply for a card together (which has the advantage of helping your child establish a credit history), or authorize your teen to use your credit card. Either way, you can monitor the teenager's use of the card every month when the statement arrives or daily by going online. You also have the power to put the brakes on the card if spending gets out of control. "Set rules for using the credit card," Anthes recommends. "For example, you might stipulate that your teen must get your OK before charging anything. You could set a limit on the amount that can be charged or agree that the teen is expected to pay the balance in full each month from his or her job earnings." Keep in mind, however, that if your name is on the account, you legally are responsible for paying it.

- **Set consequences.** Discuss what will happen if your teenager's credit card experience goes bad. Will you expect the teen to get a part-time job to pay off the card? Will you loan your child money, charging interest, to pay the balance? If so, how much will you be willing to loan?
- **Keep talking.** "Parents sometimes feel as though their teenagers don't listen to them, but teens report that they learn more about money management at home than anywhere else," Anthes says. Without lecturing, discuss the following credit card fundamentals:

1. Teens (and adults) only need one credit card.

2. When shopping for a card, look for one that has no annual fee, a low interest rate and a 20- to 30-day grace period (the amount of time you have to pay for new purchases before interest is charged). Avoid cards that charge a processing fee or have low introductory interest rates that shoot up after a few months. You can shop for credit card deals on the Internet or at your local financial institution.

3. Pay the balance in full every month to avoid interest charges. The only exception to this rule is for a real emergency. Discuss with your teen what constitutes an emergency. In some cases, you may prefer that your child ask you for money instead of using credit. If not, talk about what would be an appropriate amount of time for paying off emergency charges.

4. To ensure that money will be available to pay off the card, encourage your teen to subtract credit card purchases from his or her checking account balance immediately.

5. If it's impossible to pay the full balance, emphasize the importance of at least paying more than the minimum due. Show your teen how long it can take to pay off credit card debt if you only pay the minimum by running the numbers using various balances. Online calculators are available at <http://www.bankrate.com/> or <http://www.cardweb.com/>.

6. Mail the payment at least a week before the due date to avoid late fees.

7. Do not use a cash advance from a credit card unless there's a serious emergency. Explain to your teen that he or she will be charged interest immediately and also may be charged a fee for the money.

8. Your credit history will follow you. Help your teenager understand that falling into debt and paying bills late will negatively impact his or her ability

to get a car loan or home mortgage in the future. Even employers and landlords can look at credit records to decide if they want to hire or rent to someone. Show your teen what a credit report looks like by ordering yours from Equifax (<http://www.equifax.com/>), Experian (<http://www.experian.com/>) or TransUnion (<http://www.transunion.com/>). (Depending on where you live, you may be able to order one credit report a year for free from <http://www.annualcreditreport.com/>).

"Teach your teen to think of a credit card as a loan," Anthes says. "Before he or she pulls out the credit card, ask your child to answer this question: 'Would I really go to the bank and take out a loan for this?' If the answer is no, and your teen puts away the card, you'll know that you've done a good job of teaching your child how to handle credit."

By helping your child learn how to use credit responsibly, you have done him or her a great service and, potentially, saved your teen from carrying the burden of credit card debt for years to come.

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