

## Educating teens about credit

By [Caren Weiner Campbell](#) • Bankrate.com

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We're living on a plastic planet, where even vending machines, parking meters and Starbucks branches are now accepting credit and debit cards for everyday transactions. Small wonder that high schoolers -- who were expected to spend \$195 billion in 2006, according to a study by the Harrison Group -- hanker for their own charge cards.

"Getting a credit card is a rite of passage," says Todd Mark, director of consumer relations for Consumer Credit Counseling Service of Greater Atlanta.

In fact, a 2005 study by the Jump\$tart Coalition for Financial Literacy reveals that 31.8 percent of high school seniors use a credit card. About half of these students have a card in their own names and the rest use cards issued in a parent's name. And of course, college freshmen get bombarded with credit card come-ons as soon as they set foot on campus.

Facing this prospect, plenty of debt-dubious parents wonder how best to introduce kids to the temptations of swipe-and-sign. As with most child-rearing decisions, the best course of action depends on the individual child. But thanks to an ever-increasing number of credit and debit options, savvy grown-ups can choose the card best suited to a teen's temperament, financial sophistication and maturity level.

### Getting started with plastic:

- [Debit card](#)
- [Prepaid or stored-value card](#)
- [Joint credit card](#)
- [Secured credit card](#)
- [Authorized user](#)

### Starting out

Youngsters who already have a checking or savings account -- and that should be the first step in a kid's financial education -- are ready for a standard debit card because they're accustomed to keeping track of transactions, according to Marc Minker, a CPA and personal financial specialist at the New York City consulting firm Mahoney Cohen & Co.

Parents can rest fairly easy in this situation, since even the most acquisitive teen will find it self-limiting: Once the account balance drops to zero, theoretically, he or she has to stop spending.

And conveniently, many employers will deposit wages directly into a teen's account.

However, since a debit card is taking money from a checking or savings account, overdrafts and the resulting fees can happen. What's more, if Junior's money gets debited via fraud or error, or if there is a problem with a merchant, recouping the already-gone cash can be difficult.

The Fair Credit Billing Act has different rules for liability with debit card fraud or theft. If you report the card missing before the thief makes any transactions, the issuer can't hold you liable for any charges. If you report the loss within two business days, you will be responsible only for \$50 of charges. If you don't report the loss within 60 days, you can be liable for \$500 of transactions. These rules make it important to check the account regularly to be sure there are no problems.

[Next: "All of the prepaid cards have one major drawback. ..."](#)

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If this setup gives you nightmares of your teen debiting away his college funds, you (and he) might be better off with a prepaid card or stored-value card. Not linked to a bank account, this variation on the debit card -- [Visa Buxx](#) is a well-known example -- sets even firmer limitations on spending. Parents activate the card by loading it with an appropriate amount of money. Other authorized adults, such as Uncle Joe or Grandma, can also add funds for birthdays or Christmas or when they see fit. Then Mom, Dad and the teenager can keep an eye on expenditures via online statements. "Stored-value cards are basically cash," says Mark, "so they're easy for kids to understand."

As a result, it's no surprise that stored-value cards are marketed overwhelmingly toward the teen demographic, and each uses a slightly different marketing angle.

MasterCard's affinity-based [MYPlash](#) features images of pop musicians, rockers and athletes, while hip-hop mogul Russell Simmons' [RushCard](#) offers tie-ins with mobile phones and discounts on clothing from his Phat Farm line and his ex-wife's Baby Phat label. Paychecks can also be deposited onto the RushCard.

The [Allow Card](#), a MasterCard-branded prepaid card, aims to educate teen cardholders by e-mailing them a monthly "financial lesson." It also offers parents 35 controls, including the ability to block certain types of merchants so that teens can't shop at undesirable places.

MasterCard-branded [PAYjr](#) operates on the allowance principle: Parents deposit a teen's allowance onto a PAYjr card, and both parent and teen can monitor use online. For kids 12 and younger, PAYjr has a savings program tied to chores: Parents set up a list of chores and due dates; once the chores are completed, the payment is automatically deposited into a savings account. [UPside card](#), a Visa-allied card, is a prepaid card that can be used online, in stores and at ATMs. It also has a points program that allows users to get cash back.

All of these stored-value cards have one major drawback: Just about every action entails a fee. For example, U.S. Bank charges its Buxx customers for enrollment, balance inquiries, reloading or replacing the card and assistance from a bank teller. And here's the one-two punch: If you don't use your card for a few weeks or months, you'll get socked with an "inactivity fee."

Allow Card has a \$19.95 activation and "lifetime membership" fee, and fees for ATM withdrawals (\$1.50), monthly maintenance (\$3.50), balance inquiry at point of sale (\$0.25), and others. There are no fees for point-of-sale purchases.

With these examples in mind, be sure to check the terms of a card before you and your child sign up for one.

### Revolving credit

"The basic principles of spending money come long before the first credit card," says Mark. "There's a whole collection of related topics: the value of a dollar, the time value of money, interest, the idea of saving toward a purchase." Armed with that understanding, teens are ready to graduate to credit cards -- something they should do before graduating from high school, according to personal finance experts.

[Next: "If I bail her out every time, that sends the wrong message. ..."](#)Page | [1](#) | [2](#) | [3](#) | [4](#) | 

#### RESOURCES

- [Find the best card](#)
- [Teach your children about credit cards](#)
- [Card issuers target teens](#)

#### TOP CREDIT CARD STORIES

- [Fame & Fortune: Filmmaker Danny Schechter](#)
- [Educating teens about credit](#)
- [Deep in debt again 6 years after bankruptcy](#)

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"People have to learn this stuff sometime," says John Parfrey, director of the High School Financial Planning Program for the National Endowment for Financial Education, or NEFE. "Managing credit is all about establishing those healthy habits and patterns early."

Mark agrees.

"If you're letting your kid under 18 use a credit card, make sure you're teaching them the skills of spending and then [paying off in full](#) immediately," he says. "That's Credit 101."

There are three ways to go: You can get a joint credit card, which means you and your child are [jointly responsible for the debt](#); you can get a secured credit card, which is tied to the teen's savings account, or you can make your teen an authorized user, which means you, not your child, are responsible for the debt.

As a first foray into credit, Minker recommends a low-limit joint credit card in the teen's name, backed by a co-signing parent. A person younger than 18 cannot apply for a credit card without a parent's approval, so this is a good way for a parent to monitor a teen's card use while building a credit history for the teen.

Though the joint arrangement allows parents to keep a rein on the card's limit, Junior should be responsible for paying the bill in full. "That forces him to start thinking about having enough money set aside by the end of the month," Minker says.

Once the statement arrives, or whenever you track card activity online, he advises, "sit down with your kid for 10 minutes and go over what was spent." Ideally, he says, "the teen wouldn't be using the card for clothing or food; it'd be used in case of an emergency, or to finally buy something they've been saving up for."

Mark concurs: "They shouldn't be using it as a short-term loan or as a way to leverage their lifestyle."

All of this training is undercut, however, if parents "swoop in and save the kid" from the consequences of overspending, says Minker. "I'd much rather have my daughter fall on her face while she's under my roof -- but if I bail her out every time, that sends the wrong message."

Another option is a secured credit card tied to the teen's savings account. The card's limit is usually equal to the teen's savings account balance. If the teen misses a monthly payment, the bank takes it from the savings account. This type of card also helps build a credit history. The downside of a secured card is that the annual percentage rate, or APR of interest is high, between 13 percent and 24 percent. Credit unions often have lower APRs, so it's worth [shopping around](#).

Finally, there's the option of making your teen an authorized user of your credit card. It's convenient, it's easy, it's commonly done -- but it could result in a megasplurge, potentially putting your budget, and good credit score, at risk. Here again, "supervision is the key," says Minker.

[Next: "We emphasize ... good debt vs. bad debt."](#)

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As with the joint card, parents need to review and discuss monthly credit card statements with their teen, says CCCS's Mark, and all parties should be monitoring expenses. "The kid should be keeping track of all his or her spending, rather than waiting to be told at the end of the month what he owes."

Speaking of credit ratings, some parents authorize a teenage child to use their card believing the regular payments on it will help him or her establish a good [credit score](#). But the credit bureaus attribute the [management of that card](#) -- sensible or otherwise -- to the parent, the one who's legally responsible for the debt.

With a joint card, the teen's actions are more likely to accrue to her own nascent credit record. That's both the good news and the bad news. "There is a danger of a teen getting off on the wrong foot with their credit rating, if the kid is not well-trained and uses the card unwisely," says Minker.

To that end, jittery parents can also take heart from surveys showing that many kids understand the pitfalls of plastic. Teenage Research Unlimited's [2004 survey](#) found that 38 percent of youngsters between 12 and 19 feel that credit cards should be used only by adults, and only 5 percent of teens believe credit card debt is no problem.

"Teens are getting the message that credit has a down side," says Parfrey. "But since debt is inevitable, we emphasize the idea of creditworthiness: good debt versus bad debt. After all, it's important to have an established credit record and credit scores. When you buy a house, it's not as if you can just put down cash on the barrelhead."

### Which plastic is right for my teen?

Type of card	Pros	Cons
<b>Debit card</b>	Uses money in checking or savings account. Easy to set up.	Risk of overdrafting account and incurring fees. Does not build credit history. Must report lost or stolen card within two business days or may be liable for \$500 of unauthorized transactions.
<b>Prepaid or stored-value card</b>	Spending limited to amount loaded on card. Online checking of balances and spending. Authorized adults can load funds. Employers can load wages onto some cards. Major credit card branded cards can be used many places.	Fees are charged for activation, loading money, monthly maintenance, many more actions. Does not build credit history.
<b>Joint credit card</b>	Builds credit history.	Parent and teen responsible for debt.
<b>Secured card</b>	Credit limit set by savings account balance. Builds credit history.	May have high APR.
<b>Authorized user</b>	Easy to set up.	Doesn't build credit history. Parent solely responsible for debt. Potentially puts parent's credit score at risk.

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