Kurt Rosentreter
CA CFP

Children and Money

Give your kids the gift that keeps on giving: the know-how to deal responsibly with money

Money makes the world go round. We all need a good understanding of how the financial system — bank accounts, loans, credit cards, RRSPs, taxes and more — works. Often children learn more about finances from their parents than they do at school. As parents, we have about 20 years to impart financial knowledge to our kids before they head into the workforce, get mortgages, do their own tax returns and prepare wills. If you're a dentist, it's likely your children are growing up in an affluent household — and it's possible they could inherit large sums of money. Unless you always want to be supporting your kids financially, it is important to teach them smart money skills.

Pre-Teens and Younger

These formative years are a good time to introduce the concept of money and the role it plays in society. Until you do, kids may think that everything is free or that money just appears, but there are several steps you can take to start to teaching youngsters about our financial system:

- The traditional allowance. Avoid handing your children money every week or month. Trade the money for completion of a task such as making a bed, picking up clothes or setting a table. Explain that this aspect of barter (work for money) is the fundamental element of our society.
- Give your children piggy banks. Have them count the contents on a regular basis and explain what happens when they use money to buy something – including that there is a limited amount of money. If the piggy bank is empty, explain that they cannot afford to buy anything. Tell them how our financial institutions serve the same purpose for adults' money.
- Let children stand in front of you at the ATM machine at your bank. Let them push the buttons, pull out the cash and get the receipt; at the same time you can discuss what is happening. (Look at the ATM as an electronic piggy bank.)
- When your child was born, you may have opened a Registered Educational Savings Plan (RESP), the government-sponsored savings program where you get a 20 percent free grant for every dollar you deposit, up to defined limits. As children approach age 10, they are old enough for a discussion about what an RESP is, what post-secondary education is, how the money can grow and why you make more contributions. At this age they are at the very early stages of learning that there can be school after high school, and that some schools have a cost, for which the family must save.

Teenagers

Children this age may be earning money from babysitting or another part-time job. They likely want to buy music, clothes, games, etc., and since they are active consumers, their financial education should take on a greater level of sophistication:

- Set up a young teen's savings account at a local financial institution, obtain a debit card for the child, if possible, and set it up to receive a paper statement (at least at first). Take your child to deposit earnings and make withdrawals, using the opportunity to explain how the debit and credit system works.
- If you want your child to be aware of social causes and the importance of charity, an increasingly popular method to teach this is to hold birthday parties where guests are asked to donate money or toys to various causes in lieu of gifts — causes that can be championed by your child including delivering the toys to the charity after the party.
- If teens earn income from a job, you can file a tax return for them. They won't pay any tax unless they earn more than approximately $10,000 a year, but filing a return starts them earning RRSP-contribution room. An RRSP can be opened and a lump-sum contribution made each year. There are lots of good lessons here: The filing of a

tax return lets you discuss the concept of taxes and explain how a return is a once-a-year summary of how a portion of your earnings are sent away to provide a variety of services for society (I'm sure you will find your own personal way to say this!).

- The RRSP can be used to introduce the concept of saving for retirement and how starting to save at a young age can use the time-value of money (compound interest) to produce large savings amounts.
- Often children in affluent households get anything they want and may have little appreciation for the challenges facing those who have limited funds. To help your teenagers appreciate the value and privileges of money, incorporate some financial life lessons. For instance, don't buy your kids everything they want every day; rethink lavish and endless gifts. Do your children really need $600 phones and designer clothes? If they lose their iPod don't just buy them another one — consider having them work and earn enough money to buy a new one themselves. Encourage your teens to get a part-time job and remove or limit allowances at this age. Giving them this balanced experience will set them up well for their 20s and 30s, when they will be on their own.
- Absolutely no credit cards for kids up to this point. There is no value in teaching children to use other people's money and spend beyond their means. If you feel the need to give them a card, start with a debit card from a bank account funded by their earnings or gift money.
- When your kids are older teens, explain that sometimes adults seek advice from professionals, such as an accountant or financial advisor. You could even bring them to a meeting with an advisor.
- For older teens with some money, you can open an in-trust-for investment account that can teach them about stocks and bonds. They can buy a share or two in a company they can relate to. They should also be encouraged to buy a bond, a GIC, a mutual fund and other security to learn about different products and how they interact with the market place. They will get a paper statement and should be encouraged to interact with your advisors by email or other means to ask questions about their account, the products and how it all works. Often, because the financial advisor is not mom and dad, the child develops a healthy sense of independence, empowerment and confidence in making financial decisions.

Young Adults

Children in their late teens have typically gone in one of two directions: post-secondary education (university, community college, trade school or other) or directly into the workforce after high school. While some children at this age may still look to dad or mom for advice on money matters, they may also rebel against parental guidance. At this stage, more than most, as children gain their independence, having their own financial advisor can be helpful to defray family pressure while keeping them within a financial plan. For the parent, losing this control can be uncomfortable, but a good advisor will treat a young adult as an individual (not as the son or daughter of a client) and can continue the teaching of proper financial management well into the child's 20s.

- Many older teens or young adults will be offered credit cards. Parents or financial advisors can build on the debit-credit discussion from the early teen years by introducing cash-flow budgeting and explaining how a credit card works, interest charges and the importance of not carrying balances month to month. Getting involved early with kids' credit habits allows you to teach funda-

continued page 36

mentals that can prevent bad credit habits later on: bankruptcy can ruin people's finances for the rest of their lives.

- For the 20-year-old, whether a student or employed, the discussion can shift to financial goals later in life: will you want to own a car or a home, have a family, travel and so on. It helps to attach prices to goals.
- If children are from a wealthy family or will inherit a large sum someday, a skilled advisor can teach them what it means to have money, the perils of wealth, the complexity of various wealth strategies, and general money management skills.
- After a child reaches 18 it's possible that a parent's name will come off any in-trust-for accounts, which means children can take full control of their savings. Whether via a parent or an independent financial advisor, education could now move into asset allocation, investment return, different product types, fees and investment goals.
- For working children in their 20s, goal planning is different from that of the student child: perhaps they will buy a vehicle or home or both in the next five years, and they may be spending their own money for the first time in their life. They are also expected to know how to manage their earnings and, perhaps, a pension plan at their new job, an RRSP or debts from schooling. For people at this young age, long-term goals are often far from their minds. Try to instill balanced thinking with their pay cheque.

  Circumstances may force these young people to spend every dollar they earn, *but* if their level of income permits, encourage them to open several savings accounts and set up automatic transfers from their pay cheque account to these accounts for various amounts. One account may be savings for a car. Another account may be for a home purchase deposit. Another account as an emergency fund. And so on. Get them thinking about how to compartmentalize their money, even if the regular contributions are small in the beginning. Without this coaching, a child may end up getting it backwards – spending most of his or her pay cheque (even when it's more significant) on lifestyle and then struggling to find money for an RRSP, disability insurance and other important financial goals.
- Similarly, if young working adults have a little money left over for savings, encourage them to open two investment accounts: a Tax Free Savings Account (TFSA), to accrue $5,000 over a few years for emergencies, and a basic RRSP. Hold the TFSA money in a high-interest savings product for easy access. And if possible encourage them to make automated monthly contributions from their chequing account to an RRSP. If their investments have 40 years of compounding time inside an RRSP portfolio, they have a greater likelihood of achieving their retirement goals.
- Finally, it is time for parents to let mid-20s children take control over more of their financial planning. Preparing their own tax return each year is an effective way to teach them about taxes, tax deductions and tax credits. Getting a power of attorney prepared is an introduction to death and estate planning. Having a permanent job introduces the concepts of pension plans, health and dental insurance and even company stock and stock options. At this age your children may still turn to you for advice. Or they may head out on their own to find the answers, armed with the confidence and strong foundation of financial wisdom you have given them over the last 20 years.

Kurt Rosentreter, CA, CFP, CLU is a Senior Financial Advisor with Manulife Securities Incorporated in Toronto. Kurt is an author of seven books on personal finance and a past course instructor with the Toronto Institute of Dental Excellence. Kurt may be reached at 416-628-5761 Ext 230 or at Kurt.Rosentreter@ManulifeSecurities.ca.