3 Financial Tips For Parents Sending Students Off To College

Mark Avallone, CONTRIBUTOR
I help people on their path to Financial Freedom. FULL BIO

To paraphrase Jim Morrison, summer's almost gone. While it was hopefully fun filled and full of great memories, for many young people this summer was also a chance to earn a few dollars before heading back to college. During the summer, the labor force participation (LFP) rate among youth aged 16 to 24 generally increases. In 2016, the expected LFP rate is 60%, which is in line with the prior year level as reported by the Bureau of Labor Statistics.

If your child had the drive to get a summer job and earn some income, he or she is already demonstrating some financial savvy. Starting smart money habits as early in life as possible can make a big difference over the long run. So, here are three important tips to help your kids as they begin their financial journey.

Harvard University Jonathan Warsh sits in front of Widener Library at Harvard in Cambridge, Massachusetts on Friday, September 4, 2009. Bloomberg News/Michael

1. Use earned income to fund a Roth IRA—even if you have to write the check.

Roth IRA's are one of the best tools available for young people to invest and grow money on a tax-free basis. If your child has earned income (versus unearned income such as money you gift them), then they are eligible to open a Roth IRA. Even if your child has earmarked his or her earnings to cover some expenses (e.g., cost of books, food, or housing), you can still fund their Roth IRA in an amount up to their earned income.

Starting early can make a big difference. To get the maximum compounding interest benefit over time, take advantage of a ROTH IRA as early as possible. And, if your son or daughter has a promising career ahead of them, it may not be long until the benefits of a Roth IRA are no longer available (due to reaching the IRS earned income limits for eligibility).

While the maximum annual contribution for a Roth IRA in 2016 is $5,500, let's consider a more modest example. If you invest $4,000 into a Roth IRA, and it grows for 40 years at a compound rate of 7%, it will grow to about $60,000! If your family's situation can allow for this generosity, it might be one of the best steps you can take to help your child financially.

2. Have your child open a credit card—but have the bill sent to your house.

Many experts warn of the dangers of credit cards, and there are good reasons for that. But we also need to remember that most college students are adults who will be managing their own affairs in a few years. I find that encouraging prudent use of debt (e.g., a credit card) can help young people manage their daily cash flow expenditures while teaching them the importance of disciplined debt management. At the same time, we don't want our children running up enormous debt. You can help them by monitoring their credit card usage. Start with a low-limit card that can also earn them reward points and be sure to pay it off in full to avoid those high interest charges.

3. Complete a cash-flow worksheet—and don't call it a budget.

Having your child work with you to create their own cash-flow worksheet can be empowering for your child in that it gives them a framework and shines a light on daily decisions they will confront. But don't call it a "budget;" for obvious reasons, "budget" can sound limiting, while "cash-flow worksheet" sounds more flexible and helpful.

Start by writing down whatever monthly income your child will earn or receive from all sources (earned income, parental gifts, etc.). Then list all monthly expenses. Subtract the monthly expenses from income to determine if there is a monthly surplus or deficit. Stress the importance of managing expenses to avoid accumulating debt. To complete your worksheet, you can use a notebook or any basic Excel sheet. If it's easier for your Millennial, use an online tool such as the ones available from Quicken or Mint. Whatever method you use, it's important is to track monthly inflows and expenditures to avoid accumulating debt.

Of course there are other steps you can take to prepare your child for a sound financial life, but these take into account three main areas: saving, debt management, and cash-flow management.

Contributor's Bio

Mark Avallone is the author of Countdown To Financial Freedom, and founder and President of Potomac Wealth Advisors, LLC a financial advisory firm serving clients through holistic financial planning and wealth management. Avallone writes on a variety of financial topics, and his contributions have appeared in the Wall Street Journal as well as in Forbes where he is a regular contributor. He has appeared on CNBC and has been a repeat guest on the Fox Business Network. His insights have also appeared in USA Today, U.S. News & World Report, The Washington Post, and other leading publications.