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Federal Financial Education Grants

By Anne Kim and Tess Stovall

Today's kids need to learn much more than the simple math it takes to balance a checkbook or keep a budget. As the events of the past year have made clear, what happens on Wall Street matters on Main Street—for retirement accounts, college funds and other investments. Young people hoping to achieve middle-class success need the financial savvy to make good decisions about their money. Providing federal grants for state-mandated financial education can help students get the knowledge and money smarts they need to navigate today's complex world and become confident investors, rather than passive stewards, of their money.

THE PROBLEM

Personal financial decisions are more complex than they used to be

Financial decisions today require students to be well-informed and financially savvy.

Young people today are entering a world with many more opportunities for building wealth but also with more complexity and risk. In the past, it was enough to have only a checking and savings account, a traditional pension, and a simple home mortgage. But all of that has changed.

In 2006, only 20% of all workers in the private sector participated in a traditional pension[1] while 43% of private sector workers participated in a 401(k)-type plan,[2] shifting the burden of making good investment choices away from employers and toward individual workers. And as we've learned in the past year, home loans can be exceptionally complex. Traditional home mortgages were 30-year loans with fixed interest rates, but in the past few years, increasingly complex mortgages, such as interest-only loans or loans with adjustable-rate mortgages, have popped up. As the recent housing crisis has shown, these mortgages may contain hidden risks that can take ill-informed borrowers by surprise, with costly consequences.

The recent economic downturn has also had a dramatic impact on credit scores,[3] which can determine whether borrowers pay thousands more in interest or qualify for credit at all,[4] yet less than one-third of Americans understand what a credit score is and what it indicates about a consumer.[5] As the recession has demonstrated, it is increasingly important for individuals to be effective managers of their finances, particularly in turbulent economic times.

Young people are making poor financial choices that will have a long-term effect on their financial well-being.

Only one in eight employed individuals between the ages of 21 and 24 is putting any money away in IRA or 401(k) plan.[6] Even among those between the ages of 25 and 34, less than half of those who work are currently participating in one of these retirement plans.[7] Considering how critical it is to save even small amounts of money early in life to ensure a comfortable retirement, these figures are alarming.

Many young people also have to take on debt in order to pay for college or other necessities. Eighty-four percent of college students report that they have at least one credit card, and one-third have a balance of $3,000 or more.[8] Owing so much at such a young age requires students to be financially savvy and make well-informed financial decisions. Skipping just one student loan or credit card payment can have a devastating effect on a person's credit score and make it harder to get a loan or credit in the future.

Many students don't have the financial basics or know-how to succeed.

As teenagers approach adulthood, many feel they aren't equipped to make the best financial decisions. More than three out of four college students do not think that they are ready to cope with the financial challenges that await them in college and in the future, and eight out of ten of their parents agree.[9] Three-fourths of college students admit to making mistakes in managing their money, including by over-using credit cards.[10]

On a basic test of financial literacy administered by the Jump$tart Coalition, the average high school senior answered fewer than half of the questions correctly.[11] For example, only 40% of seniors knew that they could lose their health insurance if a parent lost a job.[12] Fewer than half knew that just paying the minimum balance on a credit card bill was more expensive than paying off a credit card in full.[13] And only about one in six understood that, over the long-term, owning stocks will yield better returns than parking cash in a checking account.[14]

One survey found that only 5% of adults say they learned the basics of financial education in school, while many more people (41%) said they were self-taught or "learned the hard way."[15] Although more states are beginning to offer a formal financial education curriculum in schools, only three states—Utah, Missouri and Tennessee—go so far as to offer a one-semester class. All told, just 21 states have a financial education requirement for high school students.[16]

THE SOLUTION

Federal financial education grants

Third Way proposes the creation of a grant program administered by the federal government to reward and encourage states that offer mandatory financial education for high school students. This proposed five year, $100 million per year grant program in the Department of Education would provide states that require financial education in high schools with funding to develop materials, train teachers and pay for other incidental costs associated with establishing a new curriculum.

Grant funding would be formula-based, depending on the number of children in a state, and states may receive funding to implement mandatory financial education programs that are either integrated into existing curricula or are stand-alone classes. To be eligible for funding, proposed programs must cover certain topic areas, such as budgeting and credit and debt management, that are to be determined by the Department of Education in consultation with the Financial Literacy and Education Commission, which coordinates the efforts of the federal agencies that currently operate adult financial education programs.

In addition, this proposal would also establish a clearinghouse, which can be operated by a private non-profit organization, to provide states curriculum development assistance, collect research on best practices and program effectiveness, and help coordinate disparate ongoing financial education efforts run by other federal agencies.

Financial education works.

A growing body of research shows that financial education can help people make better money management decisions. Studies have found direct links between the level of financial knowledge a person has and the decisions they make, such as the amount they save or whether they pay bills on time.[17] Students in states with mandatory financial education have higher savings rates five years after completing their mandatory education than students in states without such a requirement.[18]

Students who've had financial education also report feeling much more confident about making the right choices. High school students who went through one financial education course not only felt that they knew more, but they also scored better on financial literacy tests and even changed their spending and saving behavior.[19]

Students, parents and teachers overwhelmingly support financial education.

A 2007 survey by Visa found that 91% of Americans support requiring financial education in high school.[20] Moreover, the majority of teenagers say they would like to learn more about money management, even though only about one in seven has ever taken a class on the topic.[21] Large majorities of teenagers say they wish they knew more about such basic skills as how to buy a car or a house, making investments, protecting themselves from identity theft, saving more money, managing credit card debt and budgeting.[22]

Meanwhile, eight in ten teachers say they think financial education is important to teach in schools, and three-fourths believe their state should have academic standards for this subject.[23] These teachers say that lack of time and state requirements are the top barriers to offering more financial education in schools.[24] Making federal funding available for state curricula could help overcome those obstacles.

Financial education at school can fill in the gaps at home.

While a majority of parents say they see financial education as one of their obligations,[25] the reality is that a majority of students don't get all the information they need from home. Fewer than half of people say they learned money management from their parents,[26] and a majority of parents in surveys say they haven't discussed financial basics such as budgeting with their children.[27] This makes school-based financial education all the more critical.

THE ROLLOUT

Ideas for launching and publicizing a federal grant program for state-mandated financial education

- **Hold a press conference** at a high school with students and their parents and teachers.
- **Release a short report** documenting the need for financial education among students. For background data, refer to the biennial financial literacy survey conducted by the Jump$tart Coalition, which surveys high school seniors and college students on their financial knowledge.

- **Hold a financial education workshop for high school students** featuring a local non-profit financial education group, such as the Jump$tart Coalition.

CRITIQUES & RESPONSES

Federal financial education grants

It's too expensive.

For yesterday's generation, owning a portfolio was the province of the elite. Today, most middle-class Americans are investors. Money smarts are more important than ever to middle-class success. This proposal creates a five year, $100 million per year grant program—a small investment that will yield big rewards for middle-class Americans in their ability to manage their financial futures. For example, studies find that Americans could save as much as $28 billion a year in lower credit card finance charges if they improved their credit scores by 30 points.[28]

It's unnecessary because states can do this themselves.

There's no stick in this program—just a carrot. No state is being required to offer financial education to its students, but if it chooses to require a program, the grant funding will enable a state to do so at a lower cost. As a result of the recession, state budgets are under extraordinary strain, and at least 26 states have made cuts to their K-12 programs.[29] This program will help overcome the funding and technical assistance barriers that are preventing some states from offering financial education. Moreover, only 21 states require financial education today—clearly, there needs to be a federal incentive to encourage and reward more states to offer financial education.

The federal government shouldn't meddle with the school curriculum.

Again, it's up to states whether they want to participate in this program or not. Moreover, this proposal has no curriculum mandates—instead it establishes very broad guidelines for the topics that a state financial education requirement should cover in order to be eligible for funding. It also establishes a clearinghouse for states to get technical help for developing classroom materials and information on best practices so they don't have to reinvent the wheel.

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ABOUT THIRD WAY

Third Way is the leading think tank of the moderate wing of the progressive movement. We work with elected officials, candidates, and advocates to develop and advance the next generation of moderate policy ideas.

For more information about Third Way please visit www.thirdway.org.

ENDNOTES

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