

Future tuition may delay dad's retirement day

Money Manager/by Karin Price Mueller – www.businessstoday.com

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Problem:

The ailing technology sector has hurt more than investors' portfolios. Thousands of workers have lost their jobs as companies have cut back, hoping to stay in business.

That's what happened to Bev and Harry. The Greater Boston couple, whose names have been changed for publication, came to the Herald for financial guidance after Harry was offered a buyout package from his \$98,000-a-year job with a high-tech firm.

"I've known what the environment was like for a while," says Harry, a business systems analyst. "Concerns about layoffs aren't new."

Harry decided to take the buyout package, effective Dec. 31, from which he'll earn a \$40,000 annual pension. He plans to find another job at the end of the year.

The employment change adds some question marks to the couple's finances. The couple was hoping to retire when Harry, now 52, reached age 58. Now they wonder if that's a reasonable goal.

The other big-ticket expense is college. Their 16-year-old daughter Kelly is starting to look at schools, and Harry and Bev have saved little for the goal. They put away \$25 per month in a Uniform Gifts To Minors Account invested in Van Kampen Emerging Growth. The account's value is \$2,580 - their only college savings.

They always figured they'd either dip into their retirement funds to afford college, or they'd try to pay as they go from their income. But with Harry's job prospects uncertain, the couple isn't sure where the tuition money will come from.

Some tuition funds could potentially come from Bev's employer. Bev, 51, earns \$30,000 as a staff assistant at a local university. After she works at the school for five years, her offspring can receive tuition benefits. But daughter Kelly hasn't decided yet where she wants to go to college, so the couple can't count on the savings from Bev's job.

"We always concentrated on retirement planning," Bev says. "We have enough money to pay for schooling from IRAs, but there would be penalties, and we don't know if it would be worth it."

The couple does have substantial retirement savings.

Harry has \$288,300 in his current employer's 401(k) plan, with the bulk of the funds invested in Fidelity Magellan. He contributes \$5,800 a year to the plan, and he receives a 50 percent employer match.

Harry also has three IRAs. The first, worth \$44,000, is invested in Van Kampen Emerging Growth. He also has \$1,400 in American Express Limited Partnership Technology Funding Partners and \$600 in American Express New Dimensions Fund.

Bev also has IRAs invested, mostly in the same funds. She has \$1,400 invested in American Express Limited Partnership Technology Funding Partners and \$600 in American Express New Dimensions. Her other IRA, with Van Kampen funds, has \$15,070 in Enterprise Fund and \$14,451 in Select Growth.

Harry and Bev have nonretirement assets, too. With the Van Kampen family of funds, they own \$3,700 worth of Comstock Fund, \$7,800 of Emerging Growth and \$3,600 in Focus Equity Fund. They also have 5,000 stock options, at varying prices, for Harry's company stock.

In liquid assets, the couple has \$17,000 in a savings account and \$1,000 in a checking account.

In addition to the \$177,000 mortgage on their three-bedroom home, the couple owes \$6,600 in credit card debt.

“Debt hasn’t been a concern because I’ve always been working,” Harry says.

Solution:

Big-ticket job eases burden

Even if Harry gets another job paying about the same as the one he’s losing, the couple will have a hard time reaching both their goals of early retirement and of paying for college.

“It’s going to be a tough proposition using reasonable assumptions,” says **Femi Shote**, a certified financial planner with Asset Harvest Group in Waltham. “If he instead works until age 62, they can attain full financial independence.”

One reason Harry will probably not be able to retire at age 58 is the cost of his daughter’s college education. Tuition, which makes Shote hear a “huge sucking sound,” will eat into Harry and Bev’s budget over the next several years. But the couple will be able to handle it, Shote says, if Harry finds another job paying in the \$90,000 range. Shote says Harry’s expertise should make him in demand, so he agrees Harry should be able to find employment.

If Harry does find another high-paying job, his pension will become something of a windfall. Harry’s salary, added to the pension, would give the couple an extra \$30,000 in cash flow each year - money that can be diverted to pay all of their daughter’s college bills without loans.

Using that cash to pay for college is much smarter than dipping into retirement savings, Shote says.

“Retirement comes first,” he says. “They can get student loans, but there are no loans to fund retirement.”

Even with a new job, Harry should plan to delay retirement. Working an extra six years will allow the couple’s assets to grow as they continue to add to their retirement accounts. This will give them the extra savings they’ll need to reach financial independence after paying for college.

Shote praises the couple’s ability to save for retirement, but he says the couple’s asset allocation needs some work. Their portfolio is “about as aggressive as it can be,” with about 97 percent of assets invested in large-cap stocks.

“The only way to get more aggressive is to go to Las Vegas,” Shote says.

Instead of betting on large caps, Shote recommends they spread their assets among different asset classes, which will allow them to get nearly the same returns with far less volatility - and fewer sleepless nights.

He suggests they pare down their large-cap growth holdings to 18 percent from 55 percent and lower their large-cap value holdings to 30 percent from 42 percent of assets.

To diversify into other assets classes, Shote recommends the couple invest 18 percent of assets into an international stock fund and 9 percent in a small-cap stock fund. Shote also wants to see Harry and Bev use some fixed-income investments, with 15 percent of assets in a government bond fund, 5 percent in a high-yield bond fund and 5 percent in a money market fund.

Over the long run, Shote estimates the changes will return an average of 17.3 percent over the next 10 years, compared to 19.1 percent for the current portfolio - but without high risk.

There are some other areas that Shote wants the couple to address.

First, the couple's expenses are reasonable given their income today. But if Harry is unable to find work by year's end, the couple will be overspending by about \$30,000 per year.

Their mortgage and insurance payment is \$1,642. Today, Harry and Bev are prepaying their mortgage on a bimonthly schedule, which will allow them to pay off their home in 8 years. Shote sees no problems with the paydown, again, as long as Harry finds another job.

Other costs include \$388 for utilities, \$780 for food and dining out and \$400 per month for personal-care items. Harry and Bev don't have a car payment, but they pay \$405 per month for insurance, maintenance and other transportation costs.

There's plenty of fat that can be cut from the budget in case cash flow becomes an issue - something the couple can examine if needed in the future.

In the meantime, Shote says, there's no reason for the couple to maintain a credit card balance of \$6,600 at about 7 percent interest. Despite the low rate, he'd rather see the couple pay off the debt from their savings - which earns less interest than they're paying on the debt - giving them a net loss.

Shote also wants Harry and Bev to revisit their long-term care insurance purchases, saying the couple doesn't have enough coverage. Their policies cover nursing-home care, but they don't allow for home health care - a provision Shote says they need.

Current policies cost \$27 a year for coverage for both Harry and Bev. Shote says the increase in premiums for more coverage will fit into the couple's budget and be well worth the cost to protect their assets in the future.

``What they have now is like buying car insurance and only buying collision," Shote says. ``The real coverage you need is comprehensive."