Couple wants to keep more of sole salary

Money Manager/by Karin Price Muelle - /www.businesstoday.comr

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Problem:

Many women put their careers on hold while they stay home to raise their young children. Unfortunately, this blessing for the kids is often a curse on the family finances. Going from two incomes to one doesn't have to destroy money matters - but it can make saving more difficult.

That's the challenge facing Melissa and Jeff. They asked the Herald for help in figuring out how they can maximize their saving for the future on one income.

``I feel we could save a lot more. I tend to go to the store and just spend as if it's nothing,'' said Melissa, 35, who taught pre-school before the arrival of Kasey, 4, and Jake, 2. ``Who knows where it all goes?''

Despite feeling that the family's budget is a little unbalanced, Melissa and Jeff, 34, have managed to keep their credit cards clean. They don't even have a mortgage on their southern New Hampshire home.

``Growing up, my parents never were in debt, and they always told me to use credit cards like a check,'' Melissa said. ``You don't use them to buy something you don't have the money for.''

And they haven't spent all of Jeff's $58,400-a-year salary from his job in the auto industry. The couple has translated these good money habits into some disciplined savings plans.

For the children's college educations, Melissa and Jeff have vowed to save at least $1,000 for each child each year, to give them an $18,000 account when they each turn age 18. So far Kasey has $4,000 and Jake $2,000, both in Uniform Transfer To Minor Accounts (UTMA). The funds are invested in savings accounts paying less than 3 percent interest.

Melissa and Jeff know their kids' savings need to be invested more aggressively, but they admit they're afraid to lose money.

``I've never invested any money,'' Melissa said. ``I don't have the mindset for get-rich-quick schemes. Slow and steady wins the race, but 1 or 2 percent right now won't put you in the right direction.''

The couple also wants to know if they should save Kasey's and Jake's EE Savings Bonds, with face values of $1250 and $725, respectively, or if they should cash them out and invest the money elsewhere.

In addition to the kids' accounts, Melissa and Jeff have accumulated a substantial amount of cash. They have $18,000 in a checking account earmarked for future home improvements, such as new carpeting and a fresh paint job. They've also put away $30,000 in a savings account which serves as an emergency fund.

But for retirement, the couple has saved nothing. They hope to retire sometime in their 60s and they plan to live in their house forever.

``We don't know what we have to do for retirement,'' Melissa said. ``We'd like to start now but we don't know what to do with the money so it grows.''

Solution:

Capable savers only need to add structure to plans

Melissa and Jeff still have plenty of time to start a structured savings plan, and they've already proven they can set money aside for the future.

The big plus: they have no debt, so they can earmark more of their earnings to future savings, said Philip Sagan, a certified financial planner and certified public accountant with Philip J. Sagan Financial Consulting Inc. of Lexington.

``The concern Melissa and Jeff have for their children's education is commendable,'' Sagan said. But he believes they can take steps to make the savings work harder for them.

First, he recommends they not place the money in UTMA accounts, which is saved in the children's names. Instead, he suggests Melissa and Jeff save in their own names, so that when the time comes for the kids to apply for financial aid, their savings won't count against them.

Today, financial aid officers consider 35 percent of money placed in a child's name as counted toward a family's expected college contribution.

``Given their income level, financial aid is a good possibility,'' said Sagan, a member of the Financial Planning Association of Massachusetts. ``And having two kids in college at the same time for several years ratchets up considerably what they may receive for financial aid.''

So, Melissa and Jeff should place future contributions in their own names.

The couple also needs to invest the money in a place that will give them higher returns than they're getting, Sagan said. Knowing the couple's concerns about risk, he recommends a few mutual funds that aren't especially aggressive.

Because the children have many years to go before needing college funds, Sagan said they need to invest for the long-term. For equities, Sagan recommends the Dodge and Cox Stock Fund and Dodge and Cox Balanced Fund, two stock funds that take on moderate risk. He also suggests the couple look at Strong Advantage Fund, a short-term bond fund that has historically returned 5 percent to 6 percent.

Though the couple is concerned about college savings, they need to get a jump start on retirement savings.

``They need to start either traditional or Roth IRAs,'' Sagan said. ``Roths might be better for them because when they're much older they may be in a higher tax bracket, and the Roth money will be tax-free.''

Right now, the couple can each save $2,000 a year in an IRA to get started. Recent tax legislation will allow for higher contributions in future years, Sagan said, something the couple should take advantage of, especially when Melissa returns to work. ``With her additional income, they should be able to accomplish a dual purpose of saving for retirement and continuing with at least the $2,000 of college savings each year,'' Sagan said.

They can put the retirement contributions in the same funds Sagan recommends for college savings.

Melissa and Jeff can get started with IRAs today by transferring some of the $30,000 they've put away in a savings account for emergencies. Sagan said having that amount in cash is commendable, but they don't need quite that much in an emergency fund. Next, Sagan said it's essential that Melissa and Jeff have wills prepared. Although estate planning is not yet an issue, provisions in the will should be made for the care of the children should something happen to Melissa and Jeff.

``Any married couple with children should have wills,'' he said. ``Virtually every American citizen should have a will.''

A lawyer could also prepare health care proxies and durable powers of attorney, Sagan said. Jeff should also consider the purchase of disability insurance in order to provide for his family if he is unable to work because of illness or injury.

In the life insurance arena, Sagan said Jeff has adequate coverage with a term life policy worth $500,000. Melissa has no insurance, though, and Sagan said she needs to purchase some. Sagan recommends she buy a term life policy worth $250,000, which could help Jeff pay for the additional support he would need should anything happen to Melissa. A level-premium term policy of 20 years, or until their youngest child graduates from college, would be sufficient, Sagan said.

Overall, the couple just needs to hunker down to get savings plans in place.

``They're living pretty modestly,'' Sagan said. ``They should do just fine.''