Financial *focus*

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In This Issue

Launching the Finances of Your Graduate

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With final exams in May and June for colleges, universities and high schools, thousands have marched for their graduation ceremonies. Whatever the age of your graduate, you should introduce them to the power of the Roth IRA. More than anything, it is an incredible gift to the young with their low taxes and time on their side. With Roth IRA accounts you invest money with a mutual fund company or brokerage firm. You don't get the upfront tax break as you do with a traditional IRA or 401(k), but you get back something more valuable in the form of tax free growth for the rest of their lives.

Grads can deposit up to $5,500 into a Roth every year, as long as they have earned that much income for the year and have an adjusted gross income under $120,000. If you have the extra cash flow, I recommend the "parent match" for the Roth IRA to get them up to their maximum contribution. Convincing your grad to salt away funds for the future may not be the easiest sell. See if you can use the following points to convince them.

The Power of Starting Now. If there's one thing that a college grad has on most of us, it's time. Let's say they were able to put $5,500 a year into their Roth IRA for the next 10 years. After that they stop their contributions. If you assume 9% annual growth in the account, by the time they reach retirement 30 years later they will have $1.1 million in their account. All of that growth came out of $55,000 of contributions.

If instead they wait for 10 years to get started on the Roth and then make 30 years of $5,500 contributions, the numbers look good but not as compelling. With that same 9% growth, your grad would end up with $750,000 in their account 40 years from now. And they had to make $165,000 of contributions. Start your grad saving now to get over $1 million in tax-free growth versus less than $600,000 if your grad starts in 10 years.

Tax-Free for Life. Putting funds into a Roth IRA instead of a traditional IRA is a wager that taxes in the future will be higher than the taxes they pay today on income. With your new grad most likely in a low-income tax bracket and the recent tax law changes, this is a good bet to make. Once you put funds in a Roth IRA, you will never have to pay taxes on them again as long as your withdrawals are qualified. For most people that means waiting until age 59½ before they access their Roth earnings. Unlike traditional IRA and 401(k) accounts, with a Roth your grad won't have to pay income taxes on the proceeds when they need the funds.

You Can Get It Back. Life often happens while you're making plans. What if your grad ends up needing the funds? They may worry that if they require the Roth money for other purposes, it will be unavailable in some sort of retirement vault. A little-known trick of the Roth IRA allows your grad to withdraw the contributions that were made into the account. We consider Roths to be tax-free gold and don't generally recommend this step. But if you need the money, you can always get your Roth IRA contributions out free of tax or penalty regardless of your age or circumstance.

Five Financial Questions *Before* Marriage

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You think sex is intimate? Let's talk about money!

Before you start planning your wedding (a major financial event), you and your intended should have a heart-to-heart about money and your marriage. Fair warning: be ready for surprises and heart-felt bargaining. You don't have to make now-and-forever decisions, but the issues should be on the table so both of you are aware of them.

1. **How much debt do you have?** This is one of the big questions because it can be an embarrassing record of past indiscretions. Does your partner have massive student loans? Does he routinely carry a large credit card balance? Does she even know how much debt she has (a warning sign)? Does he refuse to talk about his debt (a serious warning sign)? We all make mistakes and there are valid reasons for carrying debt, but you shouldn't be blindsided by discovering the numbers after the wedding.

2. **How do you feel about debt?** Does debt drive you crazy or do you feel that making minimum payments is fine? What kind of debt are you (un)comfortable with? Do you pay off car loans quickly or are you happy with smaller payments over a longer time? Is it OK to borrow for a vacation or for new electronics?

3. **How will we manage money?** There are many alternatives, each of which can make a loud (if unspoken) emotional declaration. Will we keep our finances separate? ("I don't trust you around my money.") If so, how will we share expenses? ("If you make more than me, you should pay more than me.") If we keep separate accounts, do we each keep all of our personal income and simply share expenses?

Will we pool our money into one account? ("Two checkbooks now beat as one.") If we pool our money, who will be responsible for the bookkeeping and paying bills? ("I am more responsible than you!") Will we have a scheduled time to talk about our finances and money goals?

4. **How will we handle purchases and saving?** This question gets to the heart of your shared financial life because it directly addresses your personal priorities. What in your personal life do you prioritize financially? How does your partner feel about it?

Do you need to consult over big purchases? How big is big? No one likes feeling micromanaged but many damaging conversations begin with, "You spent how much on what!?" What is worth spending money on? Cars? Vacations? Clothing?

And don't forget ordinary expenditures. If one of you is perfectly happy getting groceries from a dented can outlet store but the other insists on Whole Foods, you need to get this in the open for discussion. Will you regularly support charities? How often and how much and which ones?

The flip side of spending is saving. How much will you regularly save and what should you save for? Do you have an emergency fund? Will you regularly put aside money for vacations? If you plan to have children, should you start a college savings plan now? And, of course, there is saving for your own retirement. Retirement might be far down the road, but it is on the road.

5. **If we have kids, will we both work?** This is a big dollar question and one that dramatically affects finances, life style and professional careers. Children are a serious financial drain. Many of us are very happy with our choice to have children, but make no mistake, the costs are significant. The issue is not simply direct expenditures (a baby stroller and car seat can easily cost $500!), there are also the things you can no longer spend money on (that two-week wilderness kayaking trip).

Then there is the question of your professional career. Will one of you put a career on hold to take care of children? Do you have the kind of career where that is even possible? If you are both career-oriented, does having children even make sense? If these questions are not addressed openly, unspoken assumptions can create anger and resentment.

Each of these questions is very serious and very, very personal. You don't need to arrive at final answers before the wedding, but you and your intended need to start the conversation.

What is a ***Stock***? What is a ***Bond***?

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When my son had braces, I dutifully drove him 127 times to the orthodontist's office. At the end of every visit, the orthodontic assistant would summon me and explain what they did. There were wire changes, which had different colors, or was it different gauges (both?), and this was all being fine-tuned based on tooth movement? She also talked about his palate, his bite, and other various orthodontic "things". She usually told me he needed to do a better job brushing and flossing and to come back in six weeks. I understood the last bit and spent the rest of the time thinking about what I would have for dinner.

Every profession has its jargon, and mine is among the worst.

Recently a client told me her husband liked me, but did not like to come meet with me because he didn't understand what I was talking about. Ouch.

I've resolved not to assume people know what I'm talking about. Today, I define two common investment terms: stock and bond.

What is a stock? A share of stock represents ownership in the company. Stocks are also called "equities". When you own stock shares, you are a shareholder.

Shareholders have a claim on future earnings of the company. The earnings may be paid out as dividends to the shareholders.

However, not all companies pay dividends. A growing company may choose to reinvest earnings back into the company for further growth. These are called "growth stocks." Some companies don't have earnings! (Yet).

Nearly every investment portfolio should have some stocks – they have outperformed other asset classes over time. Key words here are "over time".

What is a bond? Simply put, a bond is an IOU. When you buy a bond, you are loaning a company, or a government, money. The issuer of the bond pays interest, and when the bond matures, gives you your original loan amount back.

So, in short, stockholders are owners and bondholders are lenders.

So which stocks and bonds should you buy? Buy all of them! One easy way to do this is with a mutual fund. A mutual fund is a basket of many stocks or many bonds. Some mutual funds have both!

For example, the Vanguard Total Stock Market Index Fund (VTSMX) is designed to give investors exposure to the entire U.S. stock market. How many stocks are in that fund? 3,629. Three thousand six hundred twenty-nine! Do you like Apple? It's in there, it is the top holding. Like Amazon? It's in there. Like Berkshire Hathaway? (aka Warren Buffett). It's in there. Like CubeSmart? Never heard of it. It's a self-storage company. It's in there too.

Happy investing and don't forget to brush and floss regularly!

Should You Lease or Buy a Car?

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Perhaps you find yourself in the same situation I am in. My bright, orange, 2004 SUV has seen better days, and I'm tired of its never-ending need for repairs. It's time for a new car. There's still another decision that remains after I've chosen what make and model car I'd like to drive: should I lease or buy my next car?

Here are the important questions to answer in order to decide.

How long will you keep the car?

I've always purchased my cars, expecting to drive them for 100,000 miles or until they break down, whichever comes first. I'm rethinking that expectation, however, due to:

- *Rapid changes in technology.* The car I'm still driving does not have Bluetooth technology - but does have a cassette deck! Electric vehicles and parking assistance have recently been introduced, but are not yet standard in most cars. These features and others are expected to be widely available, at lower cost, by 2021, important information as I consider a three-year lease.

- *Lower costs of maintenance.* The standard car manufacturer's warranty, three years or 36,000 miles, is in place for the entire life of a car lease. This is not a small consideration, after the money I've spent the last couple of years repairing my car.

- *New car smell!* It's nice to upgrade to a new car every couple of years. Personal preference will dictate how much weight to place on this.

How much will you drive the car?

Most of my driving is done locally, as evidenced by the relatively low mileage on my close to 15-year-old car. I do like the flexibility, however, of driving upstate for the weekend without worrying about putting too many miles on the car. I need to consider how much I'll be driving, since:

- *Lease agreements limit the number of miles you drive each year.* The limits are relatively low, 10,000 to 15,000 miles per year, and the penalties of 20 to 25 cents per mile can add up.

- *Residual value*, which is the car dealer's estimate of what the car will be worth at the end of the lease. The higher the residual value, the lower the lease payments. That being said, a higher residual value may make it harder to sell the lease, break the lease before the end of the contract, or purchase the car at lease expiration.

- *Money factor*, which is equivalent to the interest rate being charged on the lease. The money factor is often not disclosed, and is affected by your credit score. Multiply the money factor by 2,400 to compare it to average auto loan rates.

I will be leasing my next car. I anticipate driving locally, upgrading with the next technology cycle, and being able to afford a nicer car than if I were to purchase. As a small business owner, I like the ability to deduct lease payments from my business income, whereas only the interest expense portion of car loan payments are deductible.

What have you decided?

Bankrate lease vs buy calculator: https://www.bankrate.com/calculators/auto/lease-buy-car.aspx