Financial Guide for New Parents

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Smashwords Edition
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Introduction

As expectant and first-time parents you are faced with a dizzying array of competing financial priorities. You may want to educate yourself quickly and make smart decisions, but time, money and even downtime often elude you. Caught up in a perfect storm, you may find yourself facing a torrent of concerns:

• Am I *saving enough* for my child's education?

• How about *my* retirement?

• Does my child *even want or need* a college education?

• How does all this fit into my budget?

• What if I am *disabled* or my income stops or slows?

• What if I *die*?

Your number one priority is to secure and protect your family's financial future, but how? This guide is specifically designed for new and upcoming parents eager to learn how they can provide a secure financial future for their families.

The *Financial Guide for New Parents* not only addresses these concerns it gives you easy, thoughtful steps that you can take to help your family achieve a successful financial future. Plus, it offers numerous ways to educate your children, so that they will be ahead of the game.

Best of all, if you have just 30-minutes, you can do it one read. Topics this guide covers include:

• New Baby, New Budget

• Life and Disability Insurance

• The Gift of Education

• Estate Planning

• Financial Literacy for Kids

I. New Baby, New Budget

Unless accounting was your favorite subject in school, most people would rather stick a nail in their foot than sit down and do a monthly budget. This is not your fault. It is the fault of an education system that, for the most part, does not carry courses on useful subjects like: 'Personal Financial Planning'.

Let's agree on one thing: with a new addition to your family, whatever budget you had before has now become completely irrelevant. So, our first step is to create a new family budget.

A budget is a budget is a budget. It is a set of numbers on a page that adds up what you consume monthly and subtracts it from your take home pay. The balance is what you save or, if it is negative, don't save or borrow.

If a solid financial plan is your roadmap to a future of financial security, a well-thought out budget is the engine of your financial plan. Financially speaking, your family cannot go anywhere without one.

Why is a budget so important? A budget will over time allow you and teach you to spend and save responsibly, to be accountable and ultimately to achieve your financial goals and dreams.

Your financial planner or accountant can help you determine your budget in advance of life events, like having a child.

There are sites, such as www.mint.com, where you can record and follow your expenditures to the penny. If you are tech savvy, you can set yourself up with an Excel spreadsheet or work in QuickBooks, which will feed right into your annual tax returns. And then voila, your finances are done!

The next page is a sample one-page budget that anyone can do. This is a good start point and one that you can fill in with your spouse. Our sample budget will enable you both to analyze what you are actually spending. If an expense is something that you do annually, like take a trip to the Grand Canyon for example, you would need to amortize it. Amortize means divide it by 12, and then write it down on the page as a monthly expense.

If your new infant is now a toddler and you still have not done a “baby” budget then take heart. This is not a problem. You can start now, because a budget is a living, breathing thing, like an actual baby, that will grow and change over time. In fact, budgets are meant to change and all budgets should be reviewed at least annually.

II. Life and Disability Insurance

Protecting Your Family

Once you find out that you are growing a brand new human being everything changes. You are now responsible for someone else in a world that can feel unstable.

You and your spouse will become more dependent on one another also as you both contribute significantly to the wellbeing of this new individual. You may support your household by generating income, or you may take primary responsibility for your child's care or you may both use a blend of these valuable talents to generate financial and emotional security for your baby.

But should one of you be unable to contribute, or if you are a single parent, life and disability coverage can provide your family in the event of the death of your loved one with critical protection. *Life insurance* can help replace lost income needed to support your family in the event of the death of your loved one and it can be used to help cover the cost of your mortgage and other debts, while *disability coverage* helps protect a portion of your income should you become ill and unable to work.

Benefits stay with you

The good news is that because most new parents are relatively young and healthy, insurance and disability payments can be very low, even locking-in these low rates for the future.

There are some guaranteed acceptance life insurance policies out there, however, if you want to qualify for the most coverage at the lowest rate, you'll generally need to undergo a health exam or answer health questions. And it will be easier to get accepted if you sign up for coverage <u>now</u>.

Kinds of insurance

There are two basic kinds of life insurance, 'term' and 'whole life'. *Term insurance* is designed to expire after a determined amount of time, when your insurance needs can be lower, for instance, after your adult children have left home.

While the most important reason to have life insurance is the coverage, whole life has cash value you can tap into for education, retirement or other needs. Withdrawals do reduce your death benefit, so you should always work with a professional to make sure there is no loss of coverage.

There are also many forms of *disability coverage* that are just too nuanced to discuss here. Frankly, at this stage the most important thing is to take action, meet with a Financial Professional who can help determine what types of coverage are most important to you and your situation.

How Do I Do This?

Every parent and family situation is different, so you should consult with your financial advisor. Don't be afraid to learn more about something that could make all the difference for your loved ones. A Certified Financial Planner or CFP ® who focuses on planning for new parents can help you review a range of options that best meet your family's needs.

III. The Gift of Education

For the majority of new parents education funding is a high priority. Anyone who has been saddled with college debt certainly does not want that for their own children. On the other hand, a responsible parent also needs to save for retirement, to buy a home, to financially protect their family and to build an emergency fund – and all today.

So, how can you set your priorities? What comes first? What comes last?

Couples can often disagree about how high on the priority list education funding ought to be. For example, maybe one parent simply worked his or her way through school, took out loans or won scholarships, whereas, the other partner's parents were able to foot the bill, and now they'd like to do the same. If you are one of these couples, don't despair. A few guidelines apply, though it is up to you and your advisor to make the final decision.

First, saving for college is no use at all if it throws you and your partner into long-term penury. If you need help from your children during your own retirement, you can make it impossible for your grandchildren to get a great education, because your adult-children will be too busy taking care of you.

Typically, college students can work through school, borrow money at reasonable rates, win scholarships and obtain grants. In retirement, you can do none of these things. So, the most critical step in the process is making sure you have enough in your budget to save. It's a bit like the inflatable masks on an airplane. You place your own on first, then your children's, because it is no good if you are passed out in the aisle.

Does this mean you should not prioritize education - of course not! Many tax-advantaged savings plans today will pay for high school as well as college costs. Grandparents, aunts, uncles and friends can also contribute to your child's savings plan.

Most people use a mix of alternatives to fund education costs. As long as you qualify, you may wish to use several different plans. Here are the most popular options:

<u>529 Plan</u> – Earnings on investments in a 529 Plan may be used tax-free for high school and higher education, including college and graduate school. You receive no Federal tax deductions for what you invest, but you pay no taxes while you earn returns and no taxes on withdrawals for qualified education costs. If 529 Plan the funds are used for anything but allowable education costs, however, taxes and penalties may apply. You can own and control your child's 529 plan. If your child does not use the funds, you may also switch the name of the beneficiary to a sibling or other family member.

<u>Coverdell Education Savings Account</u> – Any individual whose modified adjusted gross income is under the set limit for a given tax year can contribute. In 2018, that limit is $110,000 for an individual and $220,000 for a couple filing together. Like a 529 plan, you receive no deduction for contributions but funds can be withdrawn tax free for qualified education costs, including elementary school, high school and college. Withdrawals for other than education may incur taxes and penalties, so you should check with an advisor to see if a Coverdell is right for you. You can control a Coverdell account until your child is age 30, then your child controls the account and can use the funds as he or she wishes. The maximum anyone can contribute for one child in any given year is $2,000, so this plan is usually used in conjunction with other options.

<u>Life insurance with a savings plan</u> – While the main purpose of life insurance is to provide death benefits to your family, you may opt to use cash accumulation in cash value life insurance to fund all or a part of your child's education. Funds in a whole life policy accumulate on a tax-deferred basis and you may also access your funds without penalties or taxes. Monies withdrawn will reduce your death benefit so this process must be managed by a professional to be sure your coverage stays intact. You may insure yourself or your child, locking in their excellent health and protecting their families in the longer-term. Limits on amounts do apply and all insurers are not equal. You should look for a strong mutual company that provides safety, financial security and durable returns.

<u>Taxable investment account</u> – You can always save for education in an individual taxable account using stocks, bonds, ETFs, mutual funds and etc.. The pros to this approach are that funds are completely flexible and may be withdrawn at any time for any reason. Taxes do, however, apply. You may also wish to have a professional help manage your funds, so you are not subject to significant market volatility as you approach the time your child needs the money.

<u>UTMA or UGMA</u> – These are trust accounts, not limited to education that you may set up with your child as beneficiary. While there are no income tax advantages, apart from a slight advantage as a portion of the funds may be taxed at your child's lower tax rate, these trusts move funds outside your estate. The funds are controlled by a designated trustee and must be used for the benefit of your child, until your child reaches age of majority, 18 or 21 in most states. At that time, your child controls the funds. UTMAs and UGMAs are a commonly used estate planning technique. Gifts to an UTMA or UGMA are irrevocable and permanent, i.e. you cannot take the funds back for your own use. There is no limit on what you may contribute to an UTMA or UGMA though gift taxes may apply.

Every family's situation is unique and each technique has advantages and disadvantages, so please check with a Certified Financial Planner TM as to which options may be right for you and your child.

IV. Estate Planning

You may think you don't yet have an estate, however, if you have anything that you own, even if it's only the clothes on your back, you have an estate.

Will

The most important part of your estate plan at this stage of the game is, of course, a will. And the most important part of your will, as a new parent, is the clause that speaks about guardianship of your child or children. You will want to select a responsible friend or relative and make clear your wishes about schooling, expenses and anything else important to you in the upbringing of your child or children.

It is wise to alert your guardian of his or her responsibilities and your wishes ahead of time and to let them know what provisions you have made for funding your child's care, if any. At the simplest level, you will want to have life insurance to help protect your family and fund your children's developing needs.

Typical provisions in a *Last Will and Testament* include, but are not limited to:

• Guardianship

• Division of property

• Bequests to friends, family and charities

• Establishment and or funding of various trusts

• Names of contingent beneficiaries, should primary beneficiaries pre-decease you

• Powers of attorney, both financial and medical, should you become incapacitated

• Appointments of other fiduciaries, such as executor of your estate

There is one other critical dimension in writing a will. You must make sure your will is signed and executed properly. Rules for signatures, notarizations, etc. go state by state and won't be found in any online service.

An improperly signed and executed may not be valid and can throw your estate into probate, which consumes time and money and may not carry out your intentions. You must speak with a 'Trust and Estates' attorney, and there are many at every price level in your state, to ensure that your will is set up properly.

Update Your Beneficiaries

A second critical part of estate planning is updating your beneficiaries. Now that you have a new family, perhaps your partner or spouse should be the beneficiary of your life insurance and not your mom? If you have an ex-partner, make sure that they are only a beneficiary of the accounts or insurances to which they are specifically entitled.

Your 401K or 403B at work will go to your spouse, *unless you formally request that it doesn't.* For other investments accounts, including, IRAs you are generally free to select and name a beneficiary, unless you wish the proceeds to go into your estate and pass by your will or by probate.

Accurately Titled Property

Third, property, such as a home, should be accurately titled. Title means ownership. Property owned jointly can pass by title to co-owners, or not, so you must make sure ownership structure by contract will accomplish what you intend. A will cannot supersede a beneficiary designation or contractual obligation. In short, a will is a good first step but a will is not enough.

Finally, if you have a child or family member with a special needs or supplemental trust, you want to be especially careful not to put anything in that family member's name or have them as beneficiary on any insurances or accounts. Again, please check with a 'Trust and Estates' attorney in your state for advice on how to proceed.

The information provided is not written or intended as specific tax or legal advice. Representatives are not authorized to give tax or legal advice. Individuals are encouraged to seek advice from their own tax or legal counsel. Individuals involved in the estate planning process should work with an estate planning team, including their own personal legal or tax counsel

V. Financial Literacy for Kids

Give yourself a round of applause! You've reached the very last chapter in your *Financial Guide for New Parents*. But this is the most important section.

This is where we work on making personal finance easier for your children and their children and their children's children – multi-generationally – in the modern world.

Until the late 20th Century, typically government and corporations provided most of the funds that you would need to retire on in future. Pensions were common. They still exist for some unionized professions, like teachers. Moreover, most people passed away at relatively young ages, not overtaxing the health care or social security systems. For example, the average age of death in the US for an American male in 1960 was only 67. [1]

You are the first generation who may be taking care of your parents longer than your children and living in retirement longer than you work! [2] Think of what that means for every dollar you save for retirement. Those are going to have to be some mighty hard-working dollars.

Yet financial planning is not a topic taught at most schools or in most business programs, not even MBA programs. When I ask young parents how many of their parents had "the talk" with them when they were younger, the "money" talk, only about 1 in 30 will raise their hands. So where does one get a financial education? Home is a very good place to start. The earlier, the better!

Pre-School through Kindergarten – Birth to Age 5

Experts say you may start to talk with your children about money when they are as young as 3 years old. You can have fun introducing basic concepts. Pay with real coins when you shop, not plastic. Teach your kids the difference between pennies, nickels, dimes and quarters.

Explain that money is earned by working and used to buy things. Introduce the concept of money as barter, something valuable used in exchange for food, toys, candy. Let your children pay and receive your change for you.

Piggy banks can also introduce the concept of savings and investment. One coin at a time, you can help your kids understand how to delay gratification and garner savings for a rainy day.

Elementary School: Saving by Example – Ages 6 to 10

Youngsters in this age group may not be ready for a lesson on compounded savings growth, but they can benefit greatly by watching their parents model good financial behavior.

At this age, it's important, too, to demonstrate the value of money and sound money management. That's best done by giving them a dollar to purchase something at the mall, a yard sale, or at the movies. Let them see what they can get for a buck.

Elementary school kids can also begin to set financial goals. When they receive birthday money from Grandma, or an allowance, encourage them to save the cash for something bigger they really want. Show them how to compare prices at the grocery store and explain how different brands of the same product cost more or less.

This is also the time to link an allowance to chores. No one ever learned anything from being handed $5 for nothing, except to ask for more. Give your children the gift of feeling worthy and valuable, of earning good money for good work.

Middle School and Money Management – Ages 10 through Tweens

As your children mature, you can start letting them experiment with the money they earn through babysitting, shoveling snow or an allowance. Help them set up three accounts – one for their savings, one for spending money, and one (if you choose) for charity. And explain how interest works.

You may also introduce debt awareness this early on. For example, you can provide your child with a fixed 'credit line' each month to cover the cost of a larger purchase that isn't immediately available to them with birthday or allowance money. They can work off the difference or pay it down with next month's allowance, plus a small interest charge, so they can understand money borrowed is not without a cost.

These are the years to help children establish good saving and spending habits and help them manage impulse-buying control. To help close the knowledge gap, continue to build financial literacy, and reinforce the lessons learned at home, look for activities or public events than help build money awareness.

High School and College Kids: Capital Awareness – Ages 14 to 21

High school and college-age kids are ready for more sophisticated lessons in money management. That includes the management of personal debt and credit cards. Many of the best and brightest graduates get themselves in financial hot water by spending money they don't have and burying themselves in high interest credit card debt.

You can save your kids from a similar fate by explaining how interest rates work, and how those $300 designer sneakers cost much more if you pay with credit and make only the minimum monthly payments.

By paying $30 per month on a credit card that charges 18 percent interest, for example, that $300 would take 11 months to pay off and cost an additional $27 in interest.

Now is also the time to impress upon young adults the benefits of good financial choices – and the cost of poor decision making. Banks and other lenders rely on credit scores, a number that reflects your debt-to-income ratio and repayment history, to determine whether to issue borrowers a credit card or loans for a car or home mortgage.

They also use it to determine what interest rate they should charge. By making payments on time and keeping your debt to a minimum, consumers are far more likely to qualify for the most favorable, lowest interest loans.

Finally, there's nothing like a lesson in compounded growth to motivate your adult children to save for their future. When they receive their first paycheck and must pay taxes, you can explain deductions, help them do their tax return and help set up their first IRA. Explain how their savings will grow for their future.

Some enterprising teenagers and young adults are even ready to run their own businesses. It's worth a discussion. What can your kids do to create income aside from providing a service?

Can they make something? Do they have a cool idea? Can they raise money from a venture capitalist (a relative) to build a small business of their own?

Teaching your kids to earn, build and save gives them financial tools they can use for a lifetime. You can help your kids at any age to use debt wisely, to put money away for the future and to work toward becoming productive adults and smart consumers.

In sum, you can help your child at any age understand money and develop skills to take on appropriate financial responsibilities. These talents and abilities will serve your child well for a lifetime and, passed to your grandchildren, protect your family into posterity. Financial literacy and security is one of the greatest gifts that you can give a child - aside from the buckets of love, that is.

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Paula Brancato is a Financial Planner and Investment Advisor to new parents, growing families, business owners and family offices. Her strategic expertise derives from service as a CEO and CFO, as wells as from her work with hundreds of families and businesses she has advised and helped.

Before joining Barnum Financial Group, Brancato was an advisor at Northwestern Mutual Wealth Management. She also served as Regional Vice President of Alpha Omega Capital Partners, investment bankers. Prior to this, she was a Senior Manager at Deloitte & Touche working with private investors and hedge fund managers, Senior Vice President for Rogers Casey pension consultants, Vice President of Marketing and Product Development for Equitable Capital, and a derivatives expert and senior consultant with McKinsey & Company, Morgan Stanley and The World Bank.

Brancato earned her M.B.A. from the Harvard Business School where she was a Herman Meuhlstein/Godfrey Cabot Fellow. She is a graduate of Hunter College, Series 7, 63, 3 and health, life and P&C insurance licensed, a Certified Financial Planner ™, Certified Exit Planning Advisor, CLTC and CFA III candidate.

A published author and sought-after speaker on topics of business and financial management, Brancato has served as faculty for the graduate programs at the University of Southern California and Stonybrook Southampton. Presently, she runs the Poets and Writers Group at the Harvard Club of NY and resides in New York City and Palm Beach.

Endnotes

1. Statistics on males born in the USA in 1960 from The World Bank Databank.

2. The average age of death for a 65-year-old American woman today is 86, according to the World Bank Database and US National Center for Health Statistics. If she needs long term care at 65 for Alzheimer's for instance, that can be 21 years of care, whereas at age 18 a child is a legal adult and, generally, capable of independent living.