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Divorcée needs her own investment accounts

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Ellen has taken charge of her money life. The 34-year-old divorcée wants a solid financial future, hoping to retire at age 55, all while she raises her 4-year-old child.

"My mother, who was a single parent like I am, lived paycheck to paycheck and was never able to save and, as a result, she will either have to work until the day she dies or seriously alter her lifestyle when she retires," says Ellen, whose name has been changed for publication.

Ellen has been working hard so she won't share her mother's financial fate. She has been saving money for herself and her child in various ways and she also owns two investment properties, from which she receives monthly rent. She also receives alimony and child support from her ex-husband.

The Star-Ledger asked Kenneth Shapiro, a certified financial planner with Shapiro Financial Security Group in Hazlet, to help Ellen review her situation.

"Right now, she's doing all the right things," Shapiro says. "Her strong desire to retire at age 55 puts pressure on the performance of her investments."

Shapiro says Ellen's cash flow is solid now, but it will drop considerably when alimony payments stop in 2008. She can still afford to make the investments Shapiro recommends, though, including for the college fund.

Today, Ellen and her ex-husband each contribute \$250 a month to a college savings account. Shapiro says they need to save more if they want to pay for a college that costs \$30,000 a year today.

Shapiro recommends Ellen open a separate 529 plan for the additional contributions, unless a new agreement is reached with her ex-husband. And because her ex controls the existing plan, Ellen should think about opening the new account herself. Contributions should be increased to approximately a \$660 month range to have college costs fully funded by Ellen's targeted early retirement age.

Additionally, Shapiro says Ellen should open a separate non-IRA account -- earmarked for retirement -- for a nondeductible monthly amount that would normally represent IRA contributions.

Shapiro says while Ellen seems committed to annually funding maximum IRA contributions, her adjusted gross income level precludes qualifying for a Roth or traditional deductible IRA. This account could provide liquidity for funding future real estate investments. Plus, she'll have a big need for liquidity after alimony stops.

Ellen also needs to be aware of her tax situation. Shapiro says her tax projections for 2005 and 2006 indicate that she will be subject to Alternative Minimum Tax.

"Tax-related transactions should be reviewed and restructured to minimize potential exposure to AMT taxes," he says. "State income taxes, real estate taxes and personal exemptions are disallowed in AMT tax

calculation, and her taxable income as determined under AMT formula is above the exemption level."

Finally, some insurance issues. Shapiro says the possibility of future job changes and Ellen's desire for early retirement increase the possibility that she would be without disability insurance coverage during future time periods, putting plans for building a secure financial retirement at risk.

Shapiro recommends she purchase a disability insurance policy to assure coverage. He says the base premium for \$5,500 per month income with a 90-day elimination would cost about \$2,500 a year.

She should also have a detailed review performed on her existing liability insurance coverage, and purchase a \$2 million umbrella liability policy to protect personal assets. She should consider transferring ownership of her rental properties into separate single member limited liability corporation for each rental property.

"The LLC provides insulation/protection of assets," he says. "Right now, if sued by tenant, all of her assets are technically exposed to settle the suit. If real estate ownership is held in name of an LLC, it would limit her risk of loss to just the assets within that LLC."

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