EPISODE 1665

FT: So Money episode 1665. Ask Farnoosh.

[INTRODUCTION]

ANNOUNCER: You're listening to Money with award-winning money guru, Farnoosh Torabi. Each day, you get a 30-minute dose of financial inspiration from the world's top business minds, authors, influencers, and from Farnoosh herself. Looking for ways to save on gas, or double your double coupons? Sorry, you're in the wrong place. Seeking profound ways to live a richer, happier life? Welcome to So Money.

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FT: Welcome to So Money, everybody. I'm Farnoosh Torabi, coming at you from sunny Orlando, Florida, where I am. I'm resting and retreating. I'm at the Entreprenista's Wealth and Wellness Retreat in Orlando. I'm going to be doing a panel tomorrow on investing to an audience of largely women founders, who may be juggling investing in their business, investing in their personal lives, but maybe they're not yet investing for retirement. This is something that I'm really hot on right now. I actually hosted a webinar on Monday, a 90-minute live webinar on how to invest for the long run.

If you want to get access to that recording, which was a sold-out event, but I do have the video and I'm willing to share it with you, you have to be a member of my So Money Members Club. The So Money Members Club has been going on. It's been going on since probably February. We have a nice, warm community of financial go-getters. Within this community, I host monthly workshops, similar to this investing workshop. So far, we've learned about investing and how to earn more and real estate and credit card points. Then the community itself is an incredible resource for one another. There are people in there sharing advice, sharing resources, being accountability partners.

I also host live monthly office hours. Everything is recorded. So, if you're not really a live person, you like to learn on your own time, that's possible, too. Everything that goes live gets recorded and lives forever in our library of videos. Enrollment has not been open for many months. I re-opened enrollment this week and I'm going to keep it open for a short window. If you're interested, check us out. Go to somoneymembers.com.

Going back to this retirement piece, if you're interested in learning more about how to get more retirement ready, especially if you run a small business, or a micro business, my guest on Wednesday, Jean Smart, is the foremost expert on this. She actually has developed a fintech company called Penelope, where the mission there is to disrupt retirement solutions for small and micro businesses, mom and pops. The truth is a lot of these smaller businesses are stretched. They don't have the resources to put behind retirement solutions and 401ks for themselves, let alone their employees. Penelope is a more cost-effective, efficient way for them to get on this.

Jean is the daughter of Korean immigrants. Her parents are both entrepreneurs, but they did not save for their retirement. Jean is their retirement plan. As she described on the show, she wants to break that cycle. She has her daughter, hopefully will not be Jean's retirement solution. She's very passionate about this from a professional and personal standpoint. Go back and listen to Wednesday's episode with Jean Smart. If you're interested in that topic.

On Monday, very excited that we brought on Jannese Torres once more. Janesse is a friend of the show and she's a friend in real life. Her new book is out. It's called *Financially Lit: The Modern Latina's Guide to Level Up Your Dinero & Become Financially Poderosa*. I had the honor of writing the foreword to Jannese's book, where she takes us behind the scenes to her immigrant childhood, her life as a first-generation Latina and how she's resolved to pave her own path pursuing entrepreneurship, autonomy, and financial freedom. That was our Monday show.

If you're listening to this episode and it's Friday and you're an early bird to listening to Ask Farnoosh, I want to let you know that Book to Brand, my author workshop, which is happening on May 17th, doors close today. If you've been thinking about joining us, because you want to finally get your book proposal created, you want to meet literary agents that might be able to shepherd you throughout the process of publishing with a traditional publisher, or maybe you're interested in hybrid publishing. We have actually one of the top hybrid publishers joining us at this workshop. You got to act today. Tickets close tonight at midnight. We have a couple of seats left and we welcome anybody who is interested in writing a non-fiction book.

Maybe you're a thought leader, an entrepreneur, a business owner, a scientist, an influencer, a blogger, a podcaster, all of the above, you've probably got a book in you, and I want to help you bring that to life. I'm very passionate about books. I've written four books myself. Co-leading this workshop with me will be Richelle Fredson, who is the Founder of the Book Proposal Blueprint. She helped me craft my book proposal for *A Healthy State of Panic*, which went on to become published by Simon & Schuster. We're going to introduce you to agents, as well as publishers and editors. We'll also meet some newly published authors who are fresh out of the gates and they can tell you all their lessons learned. Go to booktobrand.co. I'll put the link in our show notes, so you can learn more, and if you're interested, secure your seat.

Okay, let's head to the mail bag. We have questions today, actually, from the workshop on Monday that I led. There were some questions that I couldn't get into, so I promised everybody, listen to Friday's show. I'll revisit the questions on Ask Farnoosh. We've got questions about using your 401k to maybe pay off some debt. What are my thoughts on that? When we're investing in a portfolio, what are the fees that we should look out for? What is my advice for someone who's in midlife, 44 and up, 45-years-old, 46-years-old, a homemaker with two kids who wants to prepare for financial independence? What are my podcast recommendations, my book recommendations?

All right, let's start with LaPortia who wants to know, “Should I use, can I use, part of my 401k to pay off my car loan? What are the penalties and is it worth the risk?” All right, I want to first start off by saying that there are two ways to access the money in your 401k ahead of age 59 and a half. One is just a standard withdrawal, which would be considered an early withdrawal. The other route is to take a loan out against your 401k.

Let's talk first about the early withdrawal, what that will cost you potentially and will it be worth it? Now, I just want to start off by saying that I would consider this a last-ditch effort. You have come to this option potentially, because you have exhausted all other avenues for paying off this debt. Before we get into even discussing how this works and whether or not you can do it, I want to make sure that you have one, reached out to your credit card companies, talk to them about either reducing your interest rate, modifying the debt, getting rid of maybe some of the penalties if you've been late. I don't know what your situation is with this debt, but I would first try to see how far you could get just contacting your creditors and seeing if they would be willing to make these payments more amenable to you.

You can also work with a credit counselor. I've talked about this on the show many times, but I'm happy to repeat these resources. National Foundation for Credit Counseling, nfcc.org. Then there's Money Management International, moneymanagement.org. These two non-profits have been around for decades, and they're in the service of helping people like you who are knee-deep in debt, neck deep in debt, helping them create a pathway to becoming debt free. This isn't an overnight – they don't promise overnight success. They don't promise getting out of debt quickly. This is simply, we're going to work with you to come up with a budget to understand what your debt obligations are. We're going to work with you as advocates to call those credit card companies, to call those lenders, see what's possible. Are there programs you can enroll in? Over the next year, two, three years, will help you become debt free.

That's one thing that I would look into before arriving at this question of, well, should I take money out of my 401k? It would break my heart, honestly, if anyone had to take money out of their 401k. But as we learned during, say, the pandemic, when things were really hard for a lot of families, we saw that the government actually said, “You know what?” The IRS, I guess it was. They said, “You know what? You can take money out of your 401k. Penalty free. As long as you repay yourself within the next three years, you won't pay taxes either.” That provision is no longer available. But at the time, I understood that people needed to do that.

I remember this in one of my expression, like if your house is on fire, you don't worry about the cost of the water. You just use the water. During the pandemic, a lot of our houses, in a matter of speaking, were on fire. I get it. I get why there's a need to turn to this option. But I want to see if you can first visit these other potential ways of helping yourself. Calling your creditors, working with an advocate through one of those non-profits. Obviously, doing the work of looking at your budget, finding ways to make trade-offs, reduce expenses to shore up more money, to put towards the debt, maybe you do consolidate, because you realize, I can take out maybe a personal loan, and use that loan, which will carry a lower interest rate than the average interest rate on all of the credit cards over here. You pay that off, and then start paying back the loan.

You might have a home equity line of credit, where if you took it out in any time in the last few years, the interest rate might be less than the interest rate on these credit cards. In that case, it doesn't matter of math. It's like, I'm going to take money out of my home equity line of credit. I'm going to use that to pay off the credit cards, and then start paying back the home equity line of credit. Of course, the risk there being that your home is the collateral. So, you want to be really careful and certain that you're going to be able to manage that home equity line of credit.

All right, but let's say, you've exhausted all that, and you're still not able to address this debt. At that point, let's talk about what it would mean to take money out of your 401k early. As I mentioned, there's penalties. There's a 10% penalty. Then you pay income tax. You could be facing upwards of 40% potentially, 50%, depending on your tax bracket, could reduce the withdrawal amount. If you're looking at your portfolio and you're like, “Wow, I have $20,000 in here.” Consider it $10,000 or $12,000.

You're going to have to start back at ground zero to rebuild for retirement. I'm not sure how old you are, but if you're close to retirement and you're going to start to deplete this 401k, I would be very worried. I would so much rather you find other ways to pay off the debts. Simply because what you're doing by taking the money out of the 401k is not just losing the money, but you're losing the time. You have to now reverse the clock and start over. This is why, again, taking money out of retirement early, it really ought to be a situation where there are just no other pathways to getting head above water, that you have no other options, you've tried everything else, and this is it.

Kristen, a friend in the audience who was in the workshop attending had a follow-up to LaPortia's question about would I recommend taking money out of a 401k early to pay off credit card debt? Kristen, I guess I answered your question already through answering LaPortia's question. But bottom line here is that you want to obviously be aware of the penalties and the taxes. You want to make sure that you have considered other ways of addressing this debt, whether it's the car loan, or the credit card debt, calling the lenders, working with an advocate, and then having a plan for what you're going to do in the follow-up. Like, how are you going to replenish the 401k?

If you decide to take out a loan instead, some 401k plans allow participants to take out a loan against the 401k, in this case, maybe pay off a credit card debt, pay off a car loan. It's very important to know ahead of time what will be the interest rate? This is a nicer loan in the world of loans, because you're paying yourself back, essentially, but you have to be careful what is the interest rate? What are the repayment terms? Typically, you need to repay the loan within a specified timeframe. I've seen anywhere from five to seven years. Make sure you can afford those payments, while still contributing enough to your 401k to continue participating. I would hate to see that you had to stop contributing to the 401k.

This is where you really need to be careful. If you leave this job for any reason, or they lay you off, you quit, the 401k loan may become due in full, and usually quickly, like within two months. Right now, there is a lot of precariousness in the job market. If you work in tech, or you work in a field where there's a lot of uncertainty and there are layoffs, I don't know if this is the time to be taking this kind of a risk with the 401k, simply because if you did lose your job within the next five years, or left on your own voluntarily even, you would have to pay back this loan in full quickly. Unless, and if you can't, then it would be considered an early withdrawal, and then, again, you're facing those penalties and the taxes.

Similar to taking out an early withdrawal, the loan against your 401k, it reduces, obviously, the amount of money that you have invested, which means it could impact your long-term financial security. This, too, I would put in a category called last resorts. I'm generally not a fan of this, in case you haven't been able to read between my lines. I know, just because you can, doesn't mean you should. I'll be the first to tell you that maybe you shouldn't.

Erica in our audience wants to know, “Farnoosh, when it comes to investing, what are the fees that we should be looking out for?” The two biggest fees are the expense ratios and the advisory fees. Now, I'm going to start with the expense ratios. We covered this in our investing workshop on Monday. These are fees that are charged by those who operate the mutual funds, the exchange-traded funds, ETFs, and index funds to cover their operating expenses. Expense ratios are typically a percentage of the assets under management. By the way, this is a percentage that's taken off of the value of the investment every year. It's an annual charge.

The ones that carry higher fees are typically the ones that have more active management going on. I'll give an example. An index fund, which is a passive investment, because it passively tracks an index, let's say the S&P 500, the broad US stock market, that does not require a lot of work, to be frank, by the institution that is offering this fund. It's a set it and forget it situation, and so that's why the fees for index funds are typically 0.1%, or $10 for every $10,000 you have invested.

Contrast that with emerging market funds. The assets come from stocks, from countries with economies that are considered to be emerging, and there is high risk, but potentially high return. These funds require more oversight, more management, and then you can see these funds typically cost are from 1% and upwards for that expense ratio. This sounds like a little bit of money, 1%, but it adds up, especially as your money grows and compounds, that expense ratio, that percentage is consistent and rides your investment, whether your investment grows, or your investment falls year-to-year. It's really important to be careful about these types of fees. You can find these fees. They're marked clearly whenever you purchase an index fund, or your portfolio manager, whether that's a robo-advisor, or a human selects these funds for you. This is one of the first things you want to ask is what is the expense ratio?

I'll give a quick story. Years ago, I had a portfolio, various funds, and I got schooled on just how important it is to really be careful what these expense ratios are. I learned that anything that's over 1%, you want to question. You want to understand whether there's really an ROI there. Is it worth it? Maybe it's just better to swap that out with an index fund, or an ETF, again, that's passively managed, where you can pay much less year over year, and the performance is maybe the same. I asked my financial planner for an inventory of all my funds, and next to that, I wanted to know all of the expense ratios. We went through it one by one, and highlighted the ones that were a bit red flaggy. Like, why am I spending 2.4% on this emerging market fund? Is it really necessary long-term for me?

I decided, ultimately, that it wasn't, and I cleaned house. I got rid of a lot of funds that were, in my view, too expensive. The thing about index funds is that maybe they won't appreciate as much as, let's say, a higher risk fund over the years, but why they outperform ultimately, on average, is because the expense ratio is so little. After all is said and done, even though one fund outperforms an index fund, because it carries a higher expense ratio, because you're paying more for that fund to be in your portfolio year over year, your take home is actually less than with that index fund.

There's been a lot of data to back that up. That is why many investors just invest in index funds. They don't bother with these expensive, fancy investment vehicles that carry higher fees. Okay, so that's expense ratios. You want to watch out for that.

The other big category of fees is your advisory fee. If you work with a financial advisor, they may charge you their own fee on top of whatever the individual fees are for these individual investments within your portfolio. We have an episode coming out, actually Monday, with Pam Krueger, who's the founder of Wealthramp. I've partnered with Wealthramp. Pam and I discuss finding a financial planner, how much does it cost, how to know you're working with the right person. Traditionally, advisors will charge a percentage of assets under management. If you go to an advisor with half a million dollars and they say, “Okay, our fee is 1%,” they're going to take 1% off of that $500,000, $5,000 at the end of the year. Whether you make money or not, if the portfolio dips, they'll take 1% of that. If the portfolio grows, they'll take 1% of that.

The model is changing and evolving. More planners realize that customers, clients don't love that model. Frankly, paying for investment advice isn't really where the biggest bang for your buck is, because we know now with a lot of these trading platforms that are electronic, that are data-driven, software-powered, AI-powered, you can just give your portfolio to a robo-advisor for a fraction of what a financial advisor who's using that traditional assets under management fee charges you and you get similar, if not better results.

If you're going to work with a financial advisor, and again, stay tuned until Monday's episode, we're going to break down what to look for, how to negotiate, what kinds of fees to expect, what kind of fees to ask for. If you work with a financial advisor, they will charge a fee. You want to make sure you're getting your money's worth there. I don't work with a financial advisor right now. I have in the past. I may in the future. For me, I just feel it's about where you are in your life, the season, the complexity. Right now, we just use robo-advisors and we pay 0.25% to 0.3% depending on the platform. That's of assets under management, in addition to the fees in our portfolios and most of those, if not all of the investments, are index funds and ETFs.

Okay, next question in our mailbag. What resources would I recommend for somebody in the age range of 44 to 60, who is married, who is a homemaker, a woman, two kids, who wants to prepare for financial independence? Are there any podcasts, Instagram accounts, books, courses that I would recommend? You found me, which is great and I hope to be a resource for you.

Before we get the podcasts and Instagram accounts and books and courses, I just want to offer you this. This is a question from the audience, from Bavisha. I would say that it's important that you have a conversation with your partner about what you have, financially-speaking, in your household portfolio. Is there life insurance? Is there an estate plan? Is there potentially a retirement account that you would have access to? That is the first step, I think, if you want to empower yourself and prepare for financial independence. I assume you want to stay married. If you don't want to stay married, then you need to start looking at ways you might be able to bring in some income after you are divorced. You want to, again, still do that inventory of what is in your family's financial picture.

Because depending on your state, divorce laws are determined by the state, unless you have a prenup. You may be entitled to half that, but you want to know what is out there. Getting clear on that is whether you want to stay in the marriage or not, that education will ultimately add up to you being financially independent and educated and having agency. If you want to stay married, I would say, beyond that, conversationally, if you want to have monthly check-ins in the beginning, especially if you're someone in the relationship who has not been tuned in to the finances, you want to get acclimated. Monthly, talking about what cash flow, what the cash flow is for the family, what comes in, what goes out, the budget, the investments, etc.

I would encourage you to join our So Money members club, Bavisha, because it's a small investment every month for a lot of access to me and our community. I think that, honestly, for you, would be so enriching to connect with other women me of the women in our group, our homemakers, some of them are professionals, some of them are breadwinners, some of them are divorced, some of them are single. It's the whole gamut. What really ties us together is our curiosity and our commitment to becoming financially independent. That sounds like where you're at.

Other Instagram accounts and podcasts and books and courses. Oh, gosh. I don't really have a long list here, but I do recommend some books. I like books, especially for those who are just starting out. Foundationally, it's great to just start with a book. We've had many of the authors on this podcast, but Tiffany Aliche has written *Get Good with Money*. That's a great book. We just had on Jannese Torres on this show, *Financially Lit*, where she talks a lot about her Puerto Rican heritage, but the advice, I think, is universal and applicable to all women who want financial independence. Thank you for listening to the show, by the way. I hope this show has been helpful to you.

Then our last question is from Instagram, which by the way, if you aren't following me there, please come join the fun. I'm having a lot of fun on Instagram. I try to keep it fun, educational, light, engaging. Our friend in the audience says, "I have a traditional IRA through Vanguard invested in a Target Date Fund. Is there any added benefit to using a robo-advisor over the Target Date Fund? I'd love your thoughts on comparing the two."

All right, Vanguard offering this Target Date Fund to you is essentially acting as the robo-advisor. Okay, it's easy to just get stuck on these terms, but basically, a robo-advisor is a platform. It's an electronic platform that allows you to sign up and start investing with them electronically. There's not really any human interaction, although if you wanted to call somebody, there's probably a customer service. There's probably some financial planners behind the scenes you can talk to.

Vanguard, in addition to being a company that offers funds and sells funds, they're also a place where you can go to open a portfolio and invest in various investments, largely, probably Vanguard products. But I don't think you need to move this fund anywhere else, unless you want to expand the portfolio and you feel like Vanguard is limiting in that regard. You might decide to go to another brokerage. But Vanguard sells its funds to a lot of other brokerages besides Vanguard, right?

Honestly, just to simplify it and the workshop on Monday was all about simplification. I think you're fine where you're at. If you're happy with this target date fund, if you're happy with Vanguard and you're happy with your investment mix within that target date fund, you don't want to expand, or you're not looking for more bells and whistles, stick with Vanguard. Vanguard's the gold seal in the financial investing space. By the way, one of the downfalls of moving that target date fund is that you have to sell it and then you'd have to open up again wherever you move. You can't really transfer that over. Then you'd have to pay taxes on it. I say, if it ain't broke, why fix it?

That's our show, everybody. As a reminder, a few things. Book to Brand, our workshop in New York, May 17th. The doors to buying tickets closes today. Go to booktobrand.co. If you'd like the replay of Monday's investing workshop and lots more, it's all behind the scenes at the So Money Members Club. You can go to somoneymembers.com to join immediately. I'm going to be limiting enrollment again. The doors were shut for some months and they're going to shut again in about a week or two. If you want to get in on the action this month, we're going to be talking about money and relationships. So much in store. I would encourage you to sign up.

If you have any questions about anything, whether that's a personal finance question, a question about any of my workshops, or the So Money Members Club, you can direct message me on Instagram. You can email me, farnoosh@somoneypodcast.com and you can go to somoneypodcast.com and click on Ask Farnoosh and send me a quick question there.

I'll see you back here on Monday where again, our guest will be Pam Krueger. She's a journalist and founder of Wealthramp, discussing how to really get your money's worth if you choose to work with a financial planner. Have a great rest of your day. I hope your weekend is so money.

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