EPISODE 578

[ASK FARNOOSH]

[0:00:34.3]

FT: Welcome to So Money everyone. Happy almost Memorial Day weekend. It's Friday, hopefully you're on your way to somewhere fun, relaxing. I'm ready for summer. Welcome to the show. I'm your host, Farnoosh Torabi. It's Friday, which means we have a number of questions to answer. What's on your money mind? We've got questions here related to how to reposition yourself for a job after taking some time off. We've got questions about saving for a home, Roth IRAs, and everything in between.

First up, we've got a question via audio, SpeakPipe. It's a little handy tool we have over on somoneypodcast.com. You can click on Ask Farnoosh as always and leave me a question via text, or you can send in your voicemail. On this day, we have a question from Regina. She's 27 years old, lives in New York City, working in the tech industry and she's got a career question. Take it away, Regina.

[0:01:30.2]

R: Hey Farnoosh, Reg here. I love my job. I do make a decent living. Unfortunately, I just recently started saving and it's taking me up until now to realize what I'm actually meant to do in this world, and that's to be a wellness coach and to own my own business.

A couple of things, I'm taking a one year trip. It is a personal journey, something I have to do, some challenges I need to have in my life before I move on, or at least before I turn 30. I'll have enough money for that, for the entire year, and the problem is when I get back, I'll have $5,000 saved up, so I'll need to get a job immediately.

Question there. Any advice you want to give me on this? I'll have this gaping hole in my resume which will make it hard for me to get another job. B; I'd like to start making moves as soon as I get back towards making my own business and not necessarily all of my time but like as an aside until I can afford to only do that on its own. I'll need to take qualification classes and certifications and all of that cost money. I guess is it smart or is it totally stupid to take out loans to pay for those classes and certification as well as just the cost of building a business, or should I just wait a couple, however many more years until I can save up enough money to cover all of those expenses? Thank you so much.

[0:02:53.0]

FT: All right. Two questions from Regina. How to explain the one year gap on her resume when she comes back looking for a job? Then once she decides to start the business, should she take out loans if she needs them? First question, and I love this question. I love that you're doing this, Regina. I love that you're taking time off for yourself, investing in yourself. This is so critical. We need to do this people. We need to do this more. I think as a society we should encourage each other to invest in our spiritual development, our mental development.

The world is vast. We need to get out there and experience it in order to be able to be more productive and meaningful in our day-to-day life. A year to go out and pursue that I think is brilliant, Regina, and I commend you for it. It's brave that you're doing this. It really is. It's not an easy decision, but I think you're going to be very happy when you get back having done this. How you explain this to perspective employers, you want to make sure that there is a story behind this. Why did you pursue this? What did you learn? If you did do any volunteer work while you were away? That's totally applicable to a new job that you're going to start. The people that you met, the cultures that you experienced.

I think being really strong in your explanation of why you did this and very convincing of why you did this is going to be critical in making a compelling case for your future employer. At the end of the day, you don't want it to seem like this was some aimless trip. This sort of lackadaisical 12 months of carefree traveling, which even if it was, nothing against doing that, but of course you have to think of always how this is going to playoff in the minds of a perspective employer. Ultimately, they want to know that. When you took that time off, that is valuable time off. That you learned something, and specifically that you learned a few things that would apply to the job that you have.

I think you want to also be very strong in the why of why you did it. To be honest there, you could say things like, “I was frankly a little burnt-out and I wanted to explore the world. This is the time in my life that I really need to grasp the opportunity. The fact that I don’t have a lot of other commitments; from family, to a mortgage, whatever it may be, I have the opportunity now to really go out there and explore the world, and I did this very intentionally. I planned it out. Here’s what I learned. Here’s why I’m so excited to be back and applying everything that I’ve learned to your workplace.”

You don’t have to have the answer now, obviously, to experience the next 12 months. As you are experiencing it, think about the things that you are taking in that you’re experiencing that would be of interest to a future employer. Ultimately, you want to be your own boss. The next question is; how do you finance the new startup? It is smart to take out loans to start the business?

Taking out to accomplish a goal, whether it’s school, whether it’s a business, whether it’s to buy a home. Nothing really wrong with that, you just need to have a plan to pay it back, right? You need to over-leverage. You want to take on just enough. I think simultaneous to taking out this loan. You want to make sure that you have yourself sufficient savings. The bank would probably love to see that, that you have collateral, that you have cash, so that they know that you will be able to make good on this loan.

First, see how much you can get by without having to get into debt. Having your own financial runway, saving up as much as possible now, selling assets to short-cash to star the business. I think that’s a more prudent way to go about it. Certainly, loans can be something that you can add to the mix, but you definitely want to also have your own savings to support this business. Good luck and I wish you all the best on this trip.

Moses has a question about transferring his old 401(k) to a Roth IRA. He says it’s from an old employer that he was with for a short period of time. Is it a good idea to do the transfer?

Well, you do have this option, Moses. We all have this option. When we leave a 401(k) with a previous employer we can choose to convert it to Roth IRA. In some cases, it’s very easy to do this when you get the paperwork from your old 401(k) provider. You can check a box that says, “Please directly transfer this to my new Roth IRA at such and such brokerage.”

In other cases, you might have to open up a traditional IRA, transfer the 401(k) to the traditional IRA and then convert the traditional IRA into a Roth, so an extra step. It really just depends on the way that your previous 401(k) provider was setup. Is it a good idea? It could be. As you know, we talk about IRAs ad nauseam here on So Money, and I’ve written about this for the blog over at Mint. Ultimately, this can be a very positive move if you are someone who thinks that your taxes are going to increase in the future, that you’re going to be earning more money in the future.

As we know, Roth IRAs have income limitations. After a while, you are phased out of being able to contribute to Roth IRA. You can still do the transfer at any income level, but if you want to continue contributing, then the income limitation rules will apply. Of course, with the Roth IRA, you can withdraw this money tax free in retirement. If you do think that your taxes are going to go up, then you might want to go for a Roth.

I like having a Roth. I like having a traditional IRA as well. I like having a 401(k) as well. The reason is I like to have the tax diversification in retirement. Some vehicles will require that I pay a tax. Other will not. I think that diversity will come in to benefit me, because there are many unknowns in retirement. You can only guess what’s going to happen with your income when you reach 59-1/2 an the years after that. For that reason, it’s good to have your bases covered and why Roth IRA might not be a bad vehicle to add to the mix, to the mix of your retirement accounts. Good luck, Moses.

Heather says, “You’ve had a lot of different authors on the podcast, Farnoosh. Which book do you recommend for a college graduation gift? My 21-year-old baby cousin is graduating.” Well, congrats to your 21-year-old baby cousin, Heather.

As I speak, I’m looking at a copy of *Broke Millennial,* written by Erin Lowry. She was on the show not too long ago. Back, I think, it was early May when the book came out. The book is awesome. I’m not just saying this because Erin is a friend and she was on the show. Truly, it’s been getting a lot of media attention. It’s called *Broke Millennial: Stop Scraping By and Get Your*

Financial Life Together. A true gift for anyone graduating right now who's entering the real world without a clue as to how to manage their money, which I would suspect is many 20-somethings.

I was at 20-something. Coming out of college, I knew that I would never tell my parents how much debt I was really in, and that's about it. That was my rulebook. Don't talk to mom and dad about money because they will kill you. I figured it out. Fortunately, I worked with some smart people at Money Magazine, and my dad also gave me some good advice too, I will say. He told me to open up an IRA. He told me to invest in my 401(k), but I would never talk to them about the $4,000 in credit card debt that I had that was growing. I took that upon myself and did a lot of side hustles. I figured it out, but *Broke Millennial* would have been a great book for me at that point. I think it will be great for your cousin.

Thanks for your question, Heather.

Katie says, "I own a coop that I'd like to sell and use the money for a down payment on a house. Should I use all of the profits or just a portion and invest the rest?"

She says she's got about $200,000 in an emergency account. Whoa! She has about $20,000 in investments. I think it wouldn't hurt to bulk up your investments, Katie. I think that you never want to be house rich, cash poor as they say, putting all your money into a house when you're left with not a lot left in liquid accounts. Your emergency fund is awesome. It sounds like you're well-funded in the event of an emergency. You might even want to take some of that and put it towards investments. I think that might be a little too much cash to have that's earning nothing, unless that is actually what you need in case you lose your job in a six-month period. I would think that that's more than enough, but I don't know. If that is more than enough, you might want to transfer some of that over to investments so that that can actually grow more aggressively.

Yeah, I think if you sell the coop and you've got more than enough in proceeds where you can put maybe half towards a down payment on a future home or two-thirds towards a future home and the rest in investment. I think, mathematically, that might be a better payoff for you down the road as investments over decades-long period of time do well better, in fact, than an average rate of return on a home over the same period of time. Again, this also depends on where the house is located. I will say that in New York, in some cases, your home could double in value within a 10-year period. It's happened. I've seen it in my block, in my building. New York is an outlier.

I also think that for yourself, for your future, you need to start saving more aggressively than just the $20,000 that you have in a brokerage account somewhere, I assume, or in a retirement account. Use this home sale as an opportunity to take some of that cash and put it there, and good luck, and tell us if you have any other questions about real estate. I love that topic.

Last but not least, Janet says, "Should I take out a loan for my 403(b) for a down payment on a home in two to three years, or save money in a separate account the traditional way?"

I like the traditional way, Janet. I really think that retirement accounts, like 401(k)'s, 403(b)'s, IRAs, they're retirement accounts first and foremost. Let's respect that and just keep the money in there for the long run. This isn't an emergency where you have a health scare, you need to pay for medical bills that you don't have the money for. In that case, I would say the present is more urgent than the future and you should be able to take advantage of any investments you have, any money that you have and do what you can to afford that emergency, but buying a home is not an emergency. If you can save money in a separate account the traditional way, even if it takes a little bit longer to do that, I think that's going to be better for you in the long run.

In fact, I know that will be better for you in the long run. Stick with the later plan, and I think you'll be prouder of yourself too. It's tempting to take the cash out of a 403(b) or a 401(k), and you can do that. You can take loans out against your own retirement account. These plans are setup to provide for you in that way, but I think that we should be harder on ourselves, right, and a little more prudent and say, "You know what? I can do this on my own. I'm' better off if I do this on my own."

The other thing too to remember when you take out a loan against your 401(k), or your 403(b)s, a lot of times it's interest-free and it feels like a no-brainer. I'll just put the money back when I have it. A lot of times, those 401(k) providers, 403(b) providers, will prohibit you from continuing to invest in that retirement account until the loan is paid back. A lot of times, the loan has to be paid back within five years, sometimes sooner. That's another limitation. For all those reasons, going back to my initial instinct, which is that you should just do it the traditional way. Maybe it's more boring, but I think you'll thank me, I think.

All right everyone, thank you for the questions, Janet, Katie, Heather, Moses, and Regina. I hope you all have a safe and relaxing Memorial Day weekend. On Monday, although it's a holiday, we do have a fresh episode. Joe Piazza, she's a prolific writer and she's got a new book out called *How to be Married?* It's hilarious people, and also very honest and raw, very Joe. Hope you'll tune in to that one.

Thanks so much, and I hope your weekend is So Money.

[END]