EPISODE 617

[ASK FARNOOSH]

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FT: This episode originally aired on May 20th, 2016.

Welcome back to So Money Everyone. It's Friday. I brought back on our friend of So Money, Sophia Bera. She is the founder of Gen Y Planning. It's a financial planning service for people primarily in their 20s and 30s all across the country. She's my friend. She's excellent at what she does. Check her website out at genyplanning.com.

Sophia, are you there?

[0:01:04.9]

SB: I am. I'm so excited to be here, Farnoosh. It's great to be back. Thank you.

[0:01:09.4]

FT: It's been a long, long spring. It's all I can say. We were supposed to have nice weather. It's been raining. I put on a sweater today. I almost put on my UGG boots. I don't know about you, Sophia. You're all the way in Austin. I hate you. Up here in New York, it's ridiculous. This morning, I went to get coffee with my son. I put him in the stroller and he had on his Christmas sweater, a parka and boots and I could tell he was still cold and that I regretted taking him out but I needed to get my coffee and I ran out of Keurig Pods. You can call that So Money, maybe it's not, but I think that Keurig Pods save my life. It means that I save money, and it's not the most environmental thing, but in our household it's what gets us through the day and it's cheaper than buying coffee.

Anyway, all these to say, TGIF, and thank God, Sophia, you're here on the show. Sophia Bera, everybody, round of applause. I wish I had like one of those buttons that I could like applause.

[0:02:08.4]

SB: That would be great.

[0:02:09.2]

FT: But we're all doing the gold clap over here at So Money. We love having you on the show. You are one of our trusted financial advisers who really understands the millennials like nobody. It's your job. You have a website called Gen Y —

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SB: Planning.

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FT: Planning.

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SB: There you. I'll fill in the blanks.

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FT: Yes, genyplanning.com. I was going to say, "Gen Y Experts? No. No. No." genyplanning.com. I get these questions every day. They come in the bag loads questions to my inbox. I'm trying to get up to speed everybody. I have people tweeting me like, "You haven't answered my question yet." Just keep listening. I'm getting to everything as fast as I can and with the help of trusted experts like Sophia, because truth be told, I don't have all the answers. I'll be honest. I don't know everything, especially when it's really technical, right? Yeah.

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SB: You're Farnoosh.

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FT: I'm human. I'm imperfect. I know. I know a lot of things about a lot of things, but I don't know all the answers and you got to be very careful when you're giving financial advice, right? I like to bring on the experts who do this day-in and day-out, and Sophia you're one of my favorites. Welcome back.

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SB: Thank you so much. That was such a fun introduction, Farnoosh. You gave me the giggles over here and then you're making me happy like I'm not on cold weather anymore.

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FT: Normally, I would have totally redone that introduction. I would have started over, but I don't care anymore.

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SB: No. That was fun.

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FT: I'm going live. People loved your last visit by the way, when you came on right around tax day. It was the Friday before tax deadline and you answered a lot of great questions about what to do if you're a last minute tax filer and people really wrote in to how much they enjoyed it. Thank you for coming back.

How is Austin? I know that you've newly relocated. You've chosen Austin as your destination even though you work virtually. That's how much you love Austin. You don't have to live there and you are.

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SB: Anybody who knows me knows that I love Austin and I will try to convince everyone to move here, because I just love this city. It's my favorite U.S. city. We've been having crazy weather here too, Farnoosh. It's been 90 and rainy and so I have no idea how you dress for that.

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FT: 90 and rainy versus 40 and rainy. I think you win.

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SB: Yeah. At least we can go to the pool, right?

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FT: Oh well, not really worth complaining about. Small problems in the grand scheme of life, and today is Ask Farnoosh, and so we have some more serious issues at task, which is people's financial questions. I'm happy to say though, Sophia, my audience is pretty sharp. They're smart people. They are ambitious and these questions, you'll see, they are — It's not basic. It's like, "I'm doing great. I want to do better." Tweaks to their retirement accounts. I'm, again, happy that you are here to navigate.

Let's start with Krista here, Sophia. She says that she's interested in investing in target date funds and she wants to know what my view, your view is on target date funds. She says it seems like an easy way to introduce some bonds to my portfolio since I don't currently have any. She's 31 and she's looking at some 2050 target date funds. The easy aspect makes her nervous, because they are marketed as, “Oh! Set it and forget it.” She says, “What’s the downside?”

Just a primer for everybody, a target date fund, basically a fund that — For example, 2050, that’s the anticipated retirement date, and so from now until 2050, that target date fund will move to kind of make sure that it’s got the right allocation given that you’re not going to retire for the next, in this case, 34 years.

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SB: Basically it starts out with a more aggressive asset allocation, so you would have more stocks in the beginning and then it would slowly overtime shift the asset allocation to a more conservative asset allocation which should be replacing some of those stocks with more bonds. It might start out 90% stocks, 10% bonds and then a few years later shift to 85% stocks, 15% bonds until you get towards retirement, in which case at that point it would be a much more conservative asset allocation, but not 100% bonds. I think there’s sometimes the misconception that you’re slowly switching to 100% bonds. Usually, even those target date funds, the 2020 fund often times are 60% stocks, 40% bonds, or 50% stocks, 50% bonds. That’s something to be aware of as well.

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FT: Good point. Just in general, when you’re investing for retirement, people think that once you hit 50 or 60 you should go all the bonds. Get rid of stocks. Actually, even though you’re 60, 65, you should be invested in equities. You’re still able to take on some risk because you’re not pulling all that money out at one time.

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SB: Exactly. You’d be able to have a more moderate asset allocation if you were planning on pulling that money out over the next 30 years in retirement versus the next five years where you would need more short term catch reserves.

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FT: What's the downside? These all sounds great. I want to invest in a target date fund, but there are obviously some criticism around these.

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SB: I think one of the problems with target date funds is that they all invest a little bit differently. They have a different mix of stocks and bonds depending on who is administering the fund and managing the mutual fund. It's important to check what the actual ratio of stocks to bonds is and what types of stocks and bonds are included in that mix. You'll see some are very simplistic, it might only have four different index funds that make up that target date fund. You might have very little international exposure, for example. Other times you might have more emerging markets or small cap exposure than you want.

Just to take a look at what are the actual funds that make up the target date fund I think is really important and what percentage of stocks to bonds is that ratio. Another thing to look at is the expense ratio that you're charged to own that fund. Often times it's less expensive to invest in index funds, because somebody isn't choosing that asset allocation for you like they are with a target date fund which has a mutual fund manager.

Target date funds tend to —

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FT: I.e., more expensive.

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SB: Right. Target date funds tend to be a little bit more expensive to own than if you have to choose your own investment mix with index funds. However, if you are looking for a simpler solution early on in your career especially, it can be a good one-stop-shop for people who are interested in just getting started, getting going. I like to say that asset accumulation is more important than asset allocation in your early investing years. It's more important that we just put money into your 401 (k) every month rather than be concerned if we have the perfect mix of stocks and bonds. Nothing is ever going to be perfect, so just getting close is really good and I think that that's where the target date funds can really come in handy.

Just to do your research, look at the expense ratio. An easy place to look up the expense ratio is on morningstar.com. You enter the ticker symbol in the box, in kind of the toolbar area and then you're able to click on the fees associated with the account and that's where you'll find the expense ratio.

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FT: Yeah, and I think 50 basis points or less is what you want to highlight. I think I read a study that found that the average target date fund expense ratio was like around 70 basis points or .70%, and that's kind of high. That could be a lot of money over the course of 30 years invested. Just try to go for the lowest fees as to sort of narrow down your search. You're 31 years old so it's okay to have a lot of stocks in your portfolio and to make some mistakes and maybe take some additional risk now because you'll have the time to make up for it.

Let's move on to Erin. She says her father is thinking of putting some of his money in a trust and making her the beneficiary. Oh, isn't that nice? What are his options and what are the tax benefits of different types of trusts? Sounds like maybe he needs an estate planning attorney in this case. What do you think?

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SB: yes. That's exactly what I was going to say. This is where it's really helpful to get an estate planning attorney in on your team, with your father's financial planner as well. Erin, if you are going to be the beneficiary of the trust, it might be a great idea for you to step in on those meetings as well so that you really understand how the trust works and have a relationship with your father's financial planner and your father's estate planning attorney and you know the ins and outs of that, because there's a lot of different trust provisions that he can set up as well.

Some trusts are designed so that they're revocable, meaning he can change the terms of the trust at any time. Others are irrevocable, which means that he cannot change the terms of the trust, but there are other tax benefits to irrevocable trusts.

One thing for him to note is that if he wants you to have access to the money at different ages, he can make those provisions in the trust as well. Some trusts are set up so that you receive a certain amount of money at age 25, another amount at age 30 and the rest at age 35, for example.

There's a lot of different flexibility that your father has when it comes to the trust. I think the big thing is finding a great estate planning attorney to be on his team in addition to working with the financial planner to figure out which assets do we want in the trust. What types of accounts? Also, if your father has charitable intent there might be certain assets that are better for him to give to charity versus other assets that would be better to give to you.

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FT: Where do you start to find a good estate planning attorney? We worked with one. He was great. We honestly didn't do a lot of research. It was someone that our financial planner recommended.

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SB: Yeah. I actually think that asking your financial planner is a great place to start because they've worked with a bunch of different estate planning attorneys, CPAs, and they usually have an extended network. A lot of times they have other clients that have worked with that estate planning attorney, and so they know and they like their work.

I think starting with your financial planner is a great place. Talking to your CPA, see who they recommend, and then friends and family. Seeing where did your friends go for their estate planning. Then interview a couple of people.

The other thing I like is that some cities and some areas offer different classes through parenting classes and whatnot. They'll actually have a night where an estate planning attorney comes in and educates people on why a will is important. That's where you name a guardian in your will for your child. What you need to know about trusts and just like getting basic estate planning documents in place.

I would say check if there's local parenting groups and things like that that you're a part of that they might have an estate planning expert that they bring in to speak and educate people on the importance of estate planning documents.

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FT: Yeah. Erin, your father may already have an attorney or at least whoever helped me set up his will initially, probably also the same person or team that could help him or at least recommend him an estate planning attorney for specifically this trust issue. I like your idea, Sophia, for having her sit in on those meetings.

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SB: Yeah. I think there's a lot more financial planners that are doing this legacy planning, where they're working with grandparents, parents, and grandchildren as part of the entire financial planning process and it allows them to do a lot of advanced tax and estate planning that other financial planners really wouldn't be able to do unless they had that CPA and that estate planning attorney on their team and then could really also inform all of the family members of the ins and outs of the trusts and how those work. I think it can be a great time to really get involved if that's something that you're interested in and if your father is open to that.

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FT: Great advice. Okay, let's move on to Katerina. She says she wants to open up a high yield savings account. She wants to know what is it and how different is it from a regular savings accounts. She wants to open an emergency savings fund, "Ideally, one that I'm less tempted to drain," she says. Any thoughts?

I think definitely high yield savings account for an emergency fund, especially because you're not going to want this tomorrow. It's for the future in the event of an emergency. In the meantime they can be earning a higher yield, which is it's self-explanatory, a higher yield savings account. The reason they can pass on those higher yields to their customers is because typically they're just online banks. There're no brick and mortar expenses. There are a lot more bare bones. They don't really also do a lot of marketing and as a result their savings, they pass on their customers in the form of higher yields.

What are your favorite high yield savings accounts, Sophia?

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SB: A good standby is Allied Bank. They have one of the highest interest rates and the least strings attached, I like to say. Right now Allied Bank is offering a 1% interest rate on their high yield savings account and there's no minimum, which I really like, and you link into your already existing checking account. This is great if you don't want to switch banks entirely. You have your payroll already set up going to your checking account. You can literally just go to allied.com, set up a new savings account, link your checking account and set up a monthly transfer every month so that you have money going from your checking account to your savings account and it will help separate that money from being all at one bank with your checking and savings in the same place.

Right now on your savings account at maybe a brick and mortar bank, you're probably earning . 1 on your savings and you could be earning 1%, 10 times more by having it on an online bank, which is why it can be really important especially as we're getting into 10, 20, 30 or even $100,000 in cash that people might have that they want to save for. That can really be the difference between a couple of hundred dollars a year that they're missing out on an interest.

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FT: And it's just a matter of where you're parking your cash. A couple of websites for you to look at; bankrate.com, nerdwallet.com. Check out those two websites. They have some great charts and lists. You can search by high yield or whatever you're looking for, CDs, bonds. They can show you what the various banks that they have relationships with and affiliations with. What are their going rates right now? You can do a quick search that way.

Alright, let's see. Who is next? Bonnie. Bonnie is 33 years old, Sophia. She's a former adjunct professor. She now makes $40,000 a year running her family's small business. She has a 453b that has $7,000. She has a $3,000 emergency fund and she has 16,000 in students at a 0% interest rate. What kind of a loan is that? I'd be interested to find out. Have you ever heard of that, Sophia? 0% student loan?

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SB: It could be because she mentioned that she's continuing to take some college classes, so she's deferring her loans right now.

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FT: Right. Let me finish the question, Sophia. You went ahead. Right, maybe I should read the whole thing before I start asking questions. This is what happens when you're guest is smarter than you are. Okay, she goes on. She says, "This rate is because I have continued to take classes at a community college to defer the interest from accruing." Okay, got you.

She says, "I rent and I live in Southern California where real estate is really expensive. Should I continue to pay down my student loan?" She says, "It's going to take about two years to get rid of that loan at the current rate, or put some of that money towards savings for a down payment for a house, either on a savings account or through rolling over my 453b into Roth IRA and beginning to contribute a monthly amount, and what should monthly amount be?" Wow!

A few questions here, one; she continue to pay down her student loan, or put that money towards a down payment for a house. If it's the house, should it be in a savings account or through ultimately the Roth IRA, which gives you that provision?

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SB: Yeah, lots of great questions in here. I'm a big fan of paying off the student loans.

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FT: Yeah. I don't like the idea of paying money through your retirement account. That's for retirement.

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SB: Yeah. I also feel like regardless of what the interest rate is on your student loans, I've never had a client say, "You know, Sophia? I really regretted paying off my student loans last year. I don't know why I did that."

Even if they're just at a few percent, people always feel better paying off their student loans. The other thing is, right now, that 0% interest rate, she's getting that because she's taking classes. I would maybe kind of refocus on whether you still want to be paying money to take those classes when that money could be going towards paying down your student loans. I would say really revaluating how you want to spend your cash flow. It sounds like this is a really good time to do that. Aggressively pay off the student loans I think sounds like a great idea and it also builds up that emergency savings.

She mentioned she has about $3,000 in emergency savings, which is probably about one month of her net pay. However, having that three to six months of net pay save for emergencies before she even starts saving for a down payment on a home. There's nothing wrong with renting. I think, right now, we're kind of in this time where people are feeling like, "Oh, I'm in my 30s. I should buy. It's like the right thing to do." It's not necessarily, and I think that people are getting a lot of pressure from family to buy homes and I don't necessarily think that that's the best thing for this person's financial situation especially if you have student loans and not a fully funded emergency fund. I think a Roth IRA is just a great account that you should be contributing to now especially if you're working for your family business and you no longer have that option of contributing to a work retirement plan if they don't have something set up. You're making it a goal to max out your Roth IRA every year with $5,500 is a good idea. You may also qualify for the savers credit depending on your income and how much you put into your retirement account, so that's a good tax credit to look into as well.

I would say that I love that she's thinking about saving for a down payment on a home, but I think that there's some other financial priorities here first in terms of fully funding emergency savings, getting rid of that student loan debt and getting on track for retirement.

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FT: Agree, and making more money perhaps sooner than later. $40,000 in Southern California, 33 years old. I don't know how you're doing it. I know that's similar to me living in New York City, L.A., New York City, similar cost of living in some cases. Rent is not as high, but food and everything else. Of course, you probably have a car too, so that's an added expense. I would try to look at ways to increase your income.

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SB: I love that idea, Farnoosh, and I think that that's one that a lot of people don't think about, but I think especially when you're young, in your 20s and 30s, I think it's a great idea to just really focus on your earning potential, because your income stream is your biggest asset. If you can increase your income now, it could really have a huge impact exponentially on your income over the long term. While it's really great that you're able to help family out right now, it sounds like you're doing that by discounting your value and how much you could be earning working at another company, maybe doing a similar position. It might be a good opportunity to look into that as well.

[0:23:13.8]

FT: Yeah. I know so many of my friends who, let's say, got a lump sum of cash in their 20s or they got an extra job and they were able to save a lot of that money and it became five figures. Look, that's money that you're going to be able to use to ultimately buy that house and suddenly you're in a new income bracket, a new wealth bracket. I think with your experience as a professor, you're running a business, you have a lot of skills that maybe you're not monetizing all of them, but there are ways out there. There are markets out there for things that you can offer and make money on the side passively.

One more question, Sophia, I think we have time for, and this one is Kerry, also in her 30s. She says she's chronically single, in my 30s, but that's not the problem. It's true. Being single now in your 30s is just the norm, and who cares if you want to get married or not? There was actually an article this weekend in the Times that getting married is not the capstone of life anymore. It's a cornerstone. It's like if it happens, it happens. If it doesn't, it doesn't.

She says, "I want to make sure that I'm financially prepared as I get older just in case I remain single, but I'm having a hard time finding money advice for never married singles who aren't younger and expected to marry someday. I have plans in place to tackle my consumer debt and an enormous student loan debt, a small savings and a decent 401 (k) and pension. I want to make sure all aspects of my life are covered. Do you have any suggestions for planning a solo life? I would rather undo and/or reallocate the money elsewhere should my status change and to wake up in my 60s completely unprepared." I love that she's thinking ahead.

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SB: I love this question. I think it's great. I'm single in my 30s so I can totally relate to this question, and I think that it's — I love that she's wanting to be financially independent regardless of whether she's married or single later on, and I think that that's really important. She has a lot going on. I really think that she could benefit from talking to a financial planner especially if she's a higher income earner but also has the higher student loan debt, because really working through a plan to pay off the student loan, get on track for retirement, payoff the rest of her consumer debt can really help set her up financially by building that basic financial security. If you meet somebody else and you decide that you want to merge your life with a partner, you're just going to be in a better financial position and which to do so.

I think that she's taking the right steps. I think the first step would be tackling that consumer debt. If you have any high interest rate credit debt, getting rid of that right away. Then, also, making sure you have emergency savings. Building up at least three months of emergency savings and figuring out a plan for those students loans. Do you want to take a look at student loan refinancing options? If there are private student loans, and taking a look at are you maximizing your 401 (k) and what is your pension look like as well.

This is more of a complex question. I think it'd be great for you to talk to a financial planner. Come on over to my website, genyplanning.com. I love working with clients like you. I have a lot of clients that are single women in their 30s. I do think there are resources out there and it's just going to take a little bit of digging, but it might be really great to have somebody on your team to help you navigate through that.

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FT: If I may add one more resource to the mix. Last week I was meeting with Sallie Krawcheck in person. She's been a guest on the show. For those of you who don't know Sallie, she is a financial trailblazer, female trailblazer. She was at one point one of the most powerful woman on Wall Street and has since started a website called ellevest.com. Essentially, this is a platform for women and created by women that helps you get a personalized plan for reaching your goals, whether it's retirement, whether it's starting that business, whether it's buying that car, all of the above. It takes into account things like not just your risk tolerance, but what are the sort of things that you are willing to trade off to accomplish these goals? What's your time horizon? What are your aspirations? I think that it's very easy to use. It's actually not open to the public just yet as far as anyone can sign up. They are taking it by invitation only, but go to ellevest.com to learn a little bit more.

The reason I want to recommend this to you, Kerry, is because you are, in many ways, their target market; educated women in her 30s who's aspirational, who's thinking ahead and is goal oriented. I would say that one of the biggest gaps outside of the gender income gap is the gender investment gap. Women aren't investing as much as men. Frankly, we need money more than men in retirement because we are living longer.

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SB: This is so interesting, Farnoosh. I haven't heard of this yet. I just, while you were talking, signed up.

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FT: Oh, good! Yeah. As I said, they're not open to the public right now. They want to be careful about onboarding because what they're worried about, and it would happen I think, is they would just get overwhelmed and they just want to be very really thoughtful. Sallie told me she wants to review every single financial plan in the beginning. I think that if the site actually executes everything that, in theory, it's promising, it's going to be a game changer. Happy to see that there are products out there specific for women. We need them. Don't you think?

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SB: Yeah, absolutely. I think that it's really exciting now that we are controlling more wealth and that millennials are getting older and getting great jobs, that they're starting to build products designed for us, that these fin-tech companies are coming out with really cool innovative products to help millennials, to help women with their money and what not.

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FT: Totally. It just occurred to me that every single question today came in from a female. I just want to thank Kerry, and Bonnie, and Katerina, and Erin, and Krista, and you, Sophia, for coming back and sharing all your wisdom with our audience. It's always such a treat to have you.

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SB: Thanks so much for having me, Farnoosh. It was great to be here.

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FT: Absolutely. Everyone, go to genyplanning.com and Sophia is going to help you out. If you have any other questions, you can ask her. As always, go to somoneypodcast.com and click on Ask Farnoosh.

Thanks again, and hope your weekend is so money.

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