



Planning Issues for New Parents

With the birth of my first grandchild, I recently had the opportunity to help my daughter and son-in-law welcome home their first child, assisting with diaper duty, morning feedings, and, probably most importantly, sleep relief! I loved it; it was one of the most rewarding jobs I have ever taken on. They're sleep-deprived now, but my daughter and her husband will soon be tackling the array of financial planning issues that any new parent faces.

Cash Flow Planning: The Work vs. Stay-At-Home Decision: Childcare can be very expensive and if one spouse earns only enough to cover child care costs, you may wonder if staying home make sense. Not to discount the non-financial aspects to this decision, based on the numbers, the only way to know is to understand your income and expenses and weigh them against the average cost of childcare in your area. In this analysis, it will be important not to overlook employer benefits, including a matching 401(k) contribution from your employer; run a comparison of what it will cost to replace them if you leave your job.

Health Insurance: You'll need to add your new baby to your health insurance. If you're insured through work, check with your Human Resource department for any special rules and deadlines for adding a new dependent to your policy. Your health care plan may only let you make coverage changes during the open enrollment period unless you have a 'life status change'. The birth or adoption of a child generally qualifies as a 'life status change'.

Life Insurance: At this stage of life, the primary need for life insurance is usually replacing income in the event of a premature death. Insuring future income streams will allow the surviving spouse to keep the current lifestyle and not have to make changes to educational or retirement goals. We determine the appropriate amount of insurance through our financial planning process; however as general rule of thumb, most experts recommend an amount equal to at least five times your earnings, plus the total amount of household debt and enough to cover college tuition. As new parents, term insurance will most likely meet your needs. Consider a term that lasts until your dependents are through college and no longer in need of your financial support.

Disability Insurance: Disability insurance may actually be even more important; between the ages of 35 and 65, your prime earning years, you're more likely to experience a disabling incident that leaves you unable to work than you are to die. Most employer-sponsored plans will pay you 60% of your salary if you become disabled. Many companies offer this coverage as part of their group plans—either as an employer

paid benefit or an employee paid elected coverage. If it's an elected coverage, be sure to sign up, even if it means some cash out of pocket. If your company does not offer disability insurance or you are self-employed, consider obtaining private disability insurance.

Tax Planning: A new baby gives you some additional tax planning opportunities. You will need a social security number for the baby, so apply as soon as possible. There is an annual child tax credit of \$1,000, which applies to children under age 17. Couples filing jointly who have one child and earn no more than \$110,000 can claim the full credit.

If both you and your spouse will be working there are a couple of tax benefits for childcare. There is a childcare credit with the maximum credit for one child being \$1,050 (twice that for two or more children) or if your employer offers a flexible spending program (FSA), you can put up to \$5,000 of pre-tax money for childcare through an employer-sponsored savings program. However, you can't do both; you'll need to calculate which option gives you the biggest tax benefit. Generally, the higher your marginal tax bracket, the more likely the pre-tax FSA program will give you the greatest benefit.

Education Planning: The sooner you start, the better off you'll be. College expenses are projected to rise faster than other expenses; the College Board projects the cost of a four year college education 18 years from now will be \$242,400 for a public school (in-state), \$386,300 for public (out-of-state), and \$494,700 for a private university. Starting early will keep the monthly/annual savings target much lower.

The website www.savingforcollege.com is a wonderful resource for education planning. The site outlines all the options for saving and has the most up-to-date information on all the active 529 college savings plans.

One note of caution here: knowing the magnitude of future education expenses, you may be tempted to allocate resources to education funding at the expense of retirement funding. Retirement funding should always come first; you and your child will be able to figure out other ways of getting through school -- but they don't give scholarships for retirement.

Estate Planning: For a new parent, having a will drafted is essential. Without one, if you and your spouse die prematurely, the fate of your child's guardianship and your assets are in the hands of the court.

It may not be an easy task, but take the time to determine who you would name as an executor or personal representative, who will pay your debts and distribute your assets, and who will be the guardian of your child. These may be two different people; for example, your sister Sue may be a great mom, but she may not be good with money. If you have specialized concerns, such as lifelong support for a disabled child, you may want to set up a more complex estate plan that includes a custodial account or a trust.

Your beneficiary designations on your retirement accounts and insurance policies will also need to be updated; these assets pass outside the will.

For new parents, bringing home that little bundle will be the most joyful and exhausting job they will ever take on. However, after settling in a bit, it's a smart move to take a look at these financial planning issues in order to get the family off in a financially sound direction.

--Karen O'Brien Posted 8/15/09.