

# Saving for a Residence or a Ride



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## Saving for a Residence or a Ride

- The Practical and Psychological Approach to Budgeting
- Saving for a Lump Sum: Closing Costs, Down Payment, Emergency Fund
- Planning a New Monthly Budget: Principal, Interest, Property Taxes, Insurance
- Other Considerations: Your Credit Score Counts!

# Practical and Psychological Approach to Budgeting

## Why Bother to Budget?

### **Create a Plan to Reach Your GOALS:**

Home purchase, car purchase, college savings, retirement, vacation, new computer, new furniture, etc. ...

### **Process:** Track income and expenses

Calculate a **surplus** (\$\$\$ left over) or **deficit** (you spent too much)

Adjust your income and expenses to meet your goals

# The Budget Process

## Tracking Income and Expenses

- Add all \$\$\$ spent and all \$\$\$ received over a time period (usually 3 months)
- Classify income and expenses into categories
- Expense category examples: Rent, vehicle payment, grocery store, gasoline, utilities, toiletries, eating out, clothing, personal care, medical co-payments, etc.
- The categories need only to make sense to you. There is no right or wrong category.

# The Budget Process

Income – Expenses = ???

Surplus – Extra money at the end of the period

Deficit – You spent more money than you earned

Take time to think about the results. What surprised you?

# The Budget Process

Adjust Income and Expenses to Meet Goals!

**Psychological Aspect** – Separating needs from wants

Thought: Can you give up or reduce some expense over the next year to save for your GOALS?

**Practical Aspect** – To reach goals you either increase your income, reduce your expenses, or BOTH.

Example: Waiting tables each weekend should both increase income and correspondingly reduce discretionary spending.

# Saving for a Residence or a Ride

## Saving for a Lump Sum (Large Payment)

- Psychological: Needs vs Wants. No magic. Just reality.  
What will change?
- May be easier to decrease expenses: Give up things temporarily for a “big enough” goal.
- May be easier to increase income: Additional job, change jobs, apply for a promotion

# Saving for a Lump Sum

How Much Money is Needed and for What?

Home Closing Costs: Down payment, transfer taxes, escrow cost for home owners and property taxes, title insurance

Other Home Costs: Furniture, flooring, safety fund

Vehicle: Varies by dealership

Other Vehicle Costs: Insurance, gas, maintenance

# Closing Cost for a Home

**Down Payment**: Percentage of the selling price. 20 percent is the traditional goal. It avoids mortgage insurance and tells the lender you know how to save. 10 percentage or less is possible, but with extra costs.

**Transfer Taxes**: In Pennsylvania it is customary that the buyer and seller each pay 1% of the selling price in transfer tax.

**Escrow Down Payment**: A proportionate share of real estate taxes and home owners insurance to be paid during the next year.

**Title Insurance Premium**: Lenders title insurance is required at a cost set by the state and based on loan value.

# Closing Cost for a Home - Example

## \$200,000 Home

Down payment 20%:	$\$200,000 \times .20$	=	\$40,000
Transfer tax 1%:	$\$200,000 \times .01$	=	\$ 2,000
Escrow (calculated by lender) varies greatly		=	\$ 3,800
Lenders title insurance premium estimate		=	<u>\$ 1,200</u>
Optimal lump sum needed		=	\$47,000
Possible lump sum needed 10% down		=	\$27,000***

\*\*\* If you have \$50,000 and are buying the \$200,000 house today, it probably makes sense to put less than 20 percent down and keep cash for other home expenses and your safety fund.

## Saving for a Lump Sum – Other Costs

Furniture – Are you going to buy new or used?

What can you get from family?

Do you fill the whole house?

What's in your budget?

Safety Fund – Goal is to build up to 6 months of expenses.

Why a safety fund? You lose your job, unexpected child, furnace fails, major appliance breaks down

## Saving for a Lump Sum - Monitor

- You have created a plan to reach your goals.
- Monitor your progress.
- Make it fun. Celebrate milestones!
- Share your plan with “trusted” friends and family. They can help keep you on track.
- Adjust the plan as your situation changes.
- If you get off track, reset your goals and start again!

# Saving for a New Residence or a Ride

## Budgeting for the Additional Monthly Cost

- Don't let someone else tell you what you can afford.
- Use online calculators to back into the amount financed.

Examples:	\$1,500/month, 15 years at 3.5 %	= \$209,825
	\$1,032/month, 30 years at 4.25%	= \$209,825
	\$1,500/month, 30 years at 4.25%	= \$304,915
	\$500/month, 5 years at 2.5%	= \$ 28,173

- Real estate taxes are often under-budgeted.
- Utilities are often under-budgeted....electric heat. for example.
- Home owners and auto insurance – know the cost.

# Your Credit Score Counts

What is a credit score? – A mathematical prediction of one's ability to pay their debts. In general it's a grade on how financially responsible you are. The higher the score the better.

Experian, Equifax, and TransUnion are 3 national credit reporting agencies. Each has their own proprietary formula for determining your credit score. In general, the FICO score max is 850.

Review your credit report at no cost 1 time per year per agency at [www.annualcreditreport.com](http://www.annualcreditreport.com).

# Your Credit Score Counts

Check Your Credit Score:

- Pay for your credit score when you obtain your credit report.
- Have a lender pre-qualify you for a loan. (Your credit score will be obtained before any loan amount and interest rate are determined.)

What score do you need in 2014?

650 seems to be a minimum score (talking to lenders).

750+ should be your goal.

# Your Credit Score Counts

## Effects of a Poor Credit Score:

- Higher interest rates on loans
- Higher cost of auto and home owners insurance
- Ability to get a job

# Resources

[www.IneedaCPA.org](http://www.IneedaCPA.org)

[www.feedthepig.org](http://www.feedthepig.org)

[www.360financialliteracy.org](http://www.360financialliteracy.org)

[www.annualcreditreport.com](http://www.annualcreditreport.com)

[www.nmlsconsumeraccess.org](http://www.nmlsconsumeraccess.org) (national mortgage licensing system)

[www.finra.org](http://www.finra.org) (broker check)

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