

2016 Personal Finance Case Study

12-30-15

*Your team focuses on providing clients with comprehensive financial planning from a fiduciary standpoint. Steve and Loretta Weaver were referred to your firm by a current client who praised your ability to consider all available information and provide families with a number of options so that they may best meet their goals.*

*In your first meeting with Steve and Loretta you are able to learn the facts below and complete parts of the attached balance sheet and budget. Use all of the information provided to you to assist the Weaver family in reaching their financial goals and improving their financial health.*

**PERSONAL INFORMATION**

Steve and Loretta Weaver currently live in Glen Allen, Virginia and are both 60 years old. They have been married for 39 years and reside in a duplex with their recently adopted cat, Tom. Mr. and Mrs. Weaver are the parents of Laura Steiner who is 35 years old. She has a daughter, Lana, who is 10 years old and a son Chad who is 8 years old.

Unfortunately, Laura knows now that she and her husband probably married “too soon.” They divorced shortly after Chad was born and have not kept in touch. Neither has her former husband had much communication with his children. They have not heard from him in five years. Laura knows only that he has had a difficult time keeping a job. Recently Laura has had some serious personal issues and is very challenged to care for herself or her children.

Mr. and Mrs. Weaver and their daughter believe that for Laura’s sake and her children, Lana and Chad would be much better off living with their grandparents for the foreseeable future. These recent circumstances have caused them to re-evaluate their financial situation and how they wish to spend the rest of their lives. While they hope that the children might be able to return to live with their mother, the Weavers believe it is best for all to assume they will be caring for the grandchildren until they begin college. They have always been a part of their grandchildren’s’ lives and enjoy spending time with them. This decision was an obvious choice since their father’s parents live in California, have been alienated from the family for years, and have only met the children on a handful of occasions. The Weavers, on the other hand, live nearby so the transition would not constitute a geographical change for the grandchildren who have a rooted interest in the area. For example, Lana enjoys gymnastics and is currently training with a local team and Chad fell in love with baseball after playing for the first time last year and hopes to play for his school years into the future.

Steve was a partner and an owner in a software engineering company before he retired at the age of 58. He sold his share of the business 2 years ago and has been living off of the income from the sale. Steve has always considered himself as being financially savvy. Throughout his lifetime he has handled his own investments and financial plans. His savings habits have been fair and have resulted in an accumulation of wealth. However, recent events have caused him to reconsider how much money he may need for the future. Steve enjoys reading in his free time and would like to see as much of America before he reaches the later stages of life. Loretta was very involved in her daughter’s life and stayed at home until Laura began elementary school. She then proceeded to work at a local hair salon until she retired at age 55, earning about $35,000 in her final year. In retirement, she has been spending time traveling with her friends and enjoys time away from home.

The Weavers would like to begin looking for a new home that has the additional space needed to raise their grandchildren. Their 3 bedroom 2 bath duplex, which they own outright, does not have the space to comfortably fit two children along with their cat Tom. The home will also need to be in the Glen Allen area and must have a minimum of 4 bedrooms and 2.5 baths to accommodate the children and also allow space for their mother to visit should that be possible. The Weavers need help determining if they can afford a larger house or if they are better off squeezing into their current duplex. If they sold their current home, the Weavers suspect it would only sell for $250,000 since the interior has not been updated for several decades. The lack of upgrades is due to their love of camping and their decision to purchase a camper instead of updating the home. The only home listing in the area they would consider moving into is worth $450,000, but they are not sure if they can afford it. The Weavers would like to take out a 10 year loan for with a 3.84% APR and use 100% of the sale price as a down payment. The loan payment would be $2,010. The insurance premiums and other related expenses for the new home would also be the same as the current home.

**ECONOMIC ASSUMPTIONS**

Your firm uses a conservative inflation rate of 3% in order to ensure that families meet their goals. Steve believes that the economy is going to contract in the near future, thus lowering investment returns pre-retirement and during retirement. Loretta is also fearful of the market due to the market crash of 2008. The crash made her very nervous about retirement and what might happen to their investments if a similar scenario occurred in the future. Mr. and Mrs. Weaver are in the 25% income tax bracket.

**REAL ASSETS**

Steve is 2 years into the buyout period of 12 years for his company ownership payout of $1,200,000. The remaining balance of $1,000,000 will be paid to him monthly over the remaining 10 years.

Buyout Expected Income: $1,000,000 or $100,000/yr ($8,333/month)

Non-Taxable Money Market Mutual Fund (MMMF) Account: $150,000

Steve's 401(k): $500,000

Checking Account: $10,000

Savings Account: $15,000

3 bedroom 2 bath duplex: $250,000

2014 E-class Mercedes Sedan: $55,600

* 9yrs left on loan paying $553/mo @ 4.25% APR

2010 Honda Pilot: $18,000

$17,500 in Jewelry

$5,000 in Baseball Cards

2 credit cards

* 1st: $18,000 balance, 18% APR
* 2nd: $6,000 balance, 20% APR

**EXPENSES FOR GRANDCHILDREN**

Having the grandchildren in the house is going to significantly increase the Weaver’s household budget. This increase is expected to be nearly $10,000 per year and will cover food, clothing, increased transportation expense, estimated medical expenses, and other related expenses for both children. However, should the Steve and/or Loretta return to work additional childcare expenses are estimated as follows:

* In-home, after school nanny: $50 per day
* After school activities camp: $400 per month per child
* All-day care in summer months: $800 per month per child

**EDUCATION PLANNING**

Loretta feels that they should plan for and be able to fund Chad’s and Lana’s college tuition expenses.. Unfortunately, no saving has been done to date. Steve reluctantly agreed to this decision but stipulates that he will only fund their education to an in-state school when they are 18 years old. This tuition cost would also take into account inflation for all years of college. Steve also said that he would only pay for 4 years of college per child. The expected tuition inflation rate is 6.8% per year and the current estimated tuition at an in-state school is $14,000 per year per child. The Weavers have decided to start a Virginia inVEST 529 plan for each child. They are not sure how much they need to save each year to adequately fund each of their grandchildren’s college expenses. Savings would be funded at the end of each year and payments would be made at the beginning of each year.

**INVESTMENTS**

Steve has decided to stop handling his investment decisions so that he will have more time to spend with his grandchildren. While he does not like giving up the control of his retirement accounts, he knows that this will ultimately be the best decision. He has found a financial planner that is willing to charge a monthly fee of $149 for her services. However, he still wants to have a say in the initial selection of the investments. He wishes to have a balanced portfolio such as the one listed below.

Balanced Portfolio:

* 50% bonds, 50% stocks
* Average annual return: 8.4%.

**RETIREMENT**

Steve and Loretta have been retired for two years. Recent events, however, have them reconsidering retirement as they do not think it will be possible to support the grandchildren and still maintain sufficient income for their later years. If they do return to work, they would like to retire again as soon as possible while still having enough to support the grandchildren and live a comfortable life in their later years. They desire a 75% wage replacement ratio in retirement. This would be based on their current income and they would receive the money at the beginning of each year. Savings would occur at the end of each year.

If Steve were to go back to work he has two options available to him. First he has an old friend that has indicated his desire to have Steve come to work for him full-time at an annual salary of $60,000. Steve has also considered part-time consulting work that he could do from home. He believes that he could make $30,000 per year doing this. Loretta’s opportunities to return to work are more limited as she no longer feels confident about working in a hair-salon as she has developed arthritis in her elbows that restricts her movement and stamina.

The Weavers are in great health and they both expect to live until age 95.

**SOCIAL SECURITY**

Steve and Loretta are having trouble deciding when to start receiving Social Security. They have both been educated on their Social Security benefits and prefer to begin receiving their benefits at age 70. Steve’s benefit at 70 will be $2,754 per month and Loretta’s benefit at age 70 will be $1,271 per month.

**INSURANCE COVERAGE**

The Weavers do not have life insurance, as Steve has always believed that he could invest the premiums he would be paying into the stock market and receive a higher return. However, seeing some friends who did not have enough insurance lose everything when the major “bread winner” died has made him reconsider the importance of life insurance. Loretta will also feel safer because they will not be fully relying on investment returns. However, they do not know if they will be able to afford a policy that holds a cash balance or if they should purchase term insurance. If the Weavers do begin working again to support all of the new expenses, they will also need to consider disability insurance, especially since they have very little time between now and retirement. Long-term care insurance is also a concern, as there is no one for the Weavers to rely upon once they reach the age where they can no longer take care of themselves. They need advice on what this coverage would cover and the benefits or disadvantages of purchasing the previously mentioned forms of insurance.

Another area of concern for the Weavers is health insurance. Currently they are paying $12,000 a year in premiums and experience around $4,000 in deductibles per year. The plan’s deductible is $5,500 per year, and the out-of-pocket maximum for their policy is $13,200.  After shopping on healthcare.gov, the Weavers discovered that health insurance premiums for the family of four would be $17,000 per year for a silver level plan. This new plan will have the same deductible and out-of-pocket maximum. It is estimated that the family will pay $5,000 in other expenses such as deductibles and co-pays once the kids are added to the plan. Their home and auto insurance is as follows:

Auto Insurance:

- Split-limit coverage: 100k/300k/100k

- Collision and Comprehensive deductibles: $500

- Annual premiums: $3,500

Homeowners Insurance:

- HO-3 Policy

- Annual Premium: $700

**ESTATE**

The Weavers also believe it is important to ensure that their wills are up to date with new beneficiaries and also want to fix any small changes that may be needed.

Considering their ages and the ages of the children, the Weavers’ worst fear is to pass away and leave the grandchildren with limited funding for education and life expenses. While the chances of that occurring are low, they do not want to take the risk especially since they are not sure if their daughter will be in a position to care for her children.

The Weavers want to establish a trust with Lana and Chad Jr. named as the beneficiaries but need help deciding what is most appropriate.  One trust would need to be used for life insurance policies since they have no other beneficiaries they would like to designate and the grandchildren are under 18 years old. They also wish to have the college funding accounts established within a trust.

**MISCELLANEOUS EXPENSES**

* In the past they have donated $5,000 a year to numerous charities

**GOALS:**

* Fund their retirement while also taking on the added expenses of the two grandchildren in the house
* Fund college for the children
* Obtain sufficient insurance coverage
* Determine if they can afford a larger house

**QUANTITATIVE QUESTIONS**

1. The Weavers need to consider paying off their credit card debt. If they pay $500 per card at the end of each month, how long will it take them to pay off both credit cards? What if they paid $1,000 per card per month?
2. What will be the cost to the Weavers to put both grandchildren through school and how much should they save each month in order to accomplish this goal?
3. How much do the Weavers need to save per month in order to fully retire at age 70 when the first grandchild enters college?
4. After taking on all of the added expenses for the grandchildren, can the Weavers afford to move into the larger home without paying off the credit cards as set out above? How much income would they need to add this year, including the $2,000 in credit card payments, in order to move into the new home?

**OVERALL RESPONSE TO THE WEAVERS**

1. What would you advise the Weavers to do to meet their goals?
2. What other professionals, if any, should the Weavers consult and why?
3. If you find that all of their goals together are unattainable, what recommendations or alternatives would you suggest?

*Case study provided by students* Zach Bennedsen, Christian Litscher, Allison Masoero, Holly Remsing, Thomas Ward, and Grant Wilburn, *members of the Student Financial Planning Association at Virginia Tech, under the guidance of student leaders Leotie Fukawa and Trey Isom and faculty members Mr. Derek Klock and Dr. Ruth Lytton.*