



### The Basics

## New parents' top 10 money mistakes

A tiny new baby comes home with a mountain of money issues for its overjoyed, overtired parents. Here are the most common ways parents go wrong, and why these financial flubs can be so costly in the long term.

By Karen Hube

To most new parents, getting settled with a new baby means figuring out how to function on three hours of sleep and finding what detergent will best minimize spit-up stains.

Financial issues rarely get the time of day, even though numerous important issues crop up once you have a child.

As a result, many new parents put their family's long-term financial security at risk by making rash decisions or avoiding issues altogether.

Here are 10 of the biggest mistakes that new parents make when it comes to their finances:

### Skimping on life insurance

Once you become a parent, having enough life insurance is essential. "If one or both parents dies, you have to make sure your dependents will be provided for," says Lynn Ballou, a financial planner in Lafayette, Calif.

While you may have some life insurance coverage through your employer, "that's usually not enough," Ballou says. "Anyone with a kid these days should at least have a \$500,000 policy as a bare-bones minimum," she says. What's more, if you are healthy, group policies are rarely any cheaper for you than an individual policy, and they aren't portable. If you get laid off, you lose your life insurance. "Imagine if you got laid off when you were having medical problems. Getting a new policy would be extremely expensive," Ballou says. "It's much smarter to simply get an individual policy."

How much insurance do you need? Generally people need five times their earnings, plus the total amount of their household debt and enough to cover college tuition for their children, says John Ryan, owner of Ryan Insurance Strategy Consultants in Greenwood Village, Colo.

Don't forget to run the same calculation for a stay-at-home spouse, whose premature death may mean having to hire full-time child care, Ballou adds.

For new parents, most planners recommend term insurance. "It meets most people's needs," and it's the simplest and cheapest kind, says Peg Downey, a financial planner in Silver Spring, Md. A 30-year-old healthy man recently could have gotten a \$500,000 term policy from First Penn Pacific Co. for \$475 a year, says Ryan, the Colorado insurance consultant. Choose a term that lasts until your dependents are through college and no longer in need of your financial support, Ryan says. And then, be sure your policy has the option to convert to a permanent whole life or variable life policy. That way, if you decide later that you want lifelong coverage, it will be cheaper to convert than to buy a new policy.

You can get life insurance quotes on MSN Money, as well as read more about insurance issues and find out if you have enough coverage overall.

### Shrugging off disability insurance

Disability insurance is arguably even more important, because it's statistically more likely that you will get injured than die while you're in the workforce. Most employer-sponsored plans will pay you 60% of your salary if you become disabled. As a rule of thumb, if you're earning under \$100,000, that's probably enough coverage, Ryan says. "People who earn more usually have the need for a supplemental plan."

Take a realistic look at your family's spending to figure out how much coverage you should have. Get a policy that would enable you to cover expenses and maintain your standard of living if you had to be out of work for a while.

Prices vary dramatically between insurers, but generally, for a 30-year-old male, every \$1,000 per month of supplemental coverage would cost about \$370 a year, according to Ryan. For a woman the

same age, that extra coverage would cost \$540 a year. You can read more about [disability coverage on MSN money](#).

### Buying life insurance for baby

If an insurer tries to peddle you life insurance for your kid, walk away. "You buy life insurance on someone only if their death would create financial hardship," says Marilyn Capelli, a financial planner in Bloomfield Hills, Mich.

Some salespeople say a lifetime policy on a child is a smart security measure. If your child develops a medical condition later in life, insurance would be very costly. So if you buy a policy for less now, at least you will know he will always be insured. "But it's unlikely a healthy child will develop a problem that will last into adulthood," Capelli says. "And if he did, by then the coverage would probably be small relative to his needs."

### Delaying saving for college

Most parents start fretting about tuition when their kids are entering high school - way too late. "The best time to start is when you child is born," says Dennis Gurtz, a financial planner in Bethesda, Md. There are a couple of attractive tax-free college savings options:

**529 college savings plans.** You can contribute \$25 a month or up to \$250,000 each year to these state-sponsored plans. Your money grows tax free as long as it is used for college costs.

All states sponsor one, and each is managed by a brokerage or mutual fund company. The Illinois plan is run by Salomon Smith Barney, and Maryland's is managed by T. Rowe Price. No matter where you live, you can participate in any plan and your child can attend any school she chooses.

The plans invest your money in a portfolio of stocks and bonds that gets gradually more conservative as your child nears college age.

For information on the performance data on 529 plans, see [SavingForCollege.com](#). (See link in left margin under Related Resources.) For a listing of all 529 plans, check out The College Savings Plans Network Web site. (Also listed under Related Resources.)

**Coverdell education savings accounts.** Formerly called education IRAs, these let you contribute up to \$2,000 a year in a tax-free accounts. The earnings build up tax-free. There are some income limits, however: \$220,000 for couples filing jointly, and \$110,000 for singles. For more on Coverdell accounts and college planning, visit [MSN Money's College Planning page](#).

### Forgetting what's most important: retirement savings

Once you're faced with the monumental task of saving for your child's college tuition, it's easy to shrug off saving for retirement. Big mistake, Ballou says. "Saving for retirement always comes first, college comes second," Ballou says. "You and your child can figure out other ways of getting through school. It would be worse if your child had to support you during your retirement."

Max out on your 401(k), an IRA, or whatever retirement plans are available to you. Stay-at-home spouses should sock cash into an IRA. Of these, look into a Roth IRA. These take after-tax dollars. Earnings inside the account build up tax-free, and, later on, you can withdraw money without incurring taxes. Read [more about retirement planning](#) on MSN Money.

### Postponing a will

Many parents assume they don't need a will, because they don't have large estates. But if you have a child, a will is essential to designate guardians. "If you and your spouse die prematurely without a will, a court will appoint guardians for your children," says Elizabeth Lewin, co-author of "Family Finance."

Hire an attorney to draft a will (cost: \$500 to \$1,000) in which you name an executor, who would pay your debts and distribute your assets, and a guardian for your children. "These may be two different people; sister Jane may be a great mom, but she may not be good with money," Lewin says.

Also, name two backups for both child and money issues, advises Ballou. "What if you want your sister to take care of your kids, but for some reason she's not able?"

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.

An alternative is to write your own will using computer software. For more information on these programs, read "[12 easy steps to preparing your estate plan](#)" on MSN Money. But, as Ginger Applegarth notes in that article, if your estate is at all complex, you're probably better off consulting

a lawyer.

### Overspending on baby costs

The higher your income, the more expensive it is to raise a child. For a child born in 2003 to a family with annual income of more than \$65,400 a year, the basic expenses of child-rearing will set you back more than \$344,000, according to the U.S. Department of Agriculture. And that's just until age 18.

While a lot of this spending is necessary, some of it isn't. Many seasoned parents admit their most irresponsible spending occurred in their children's earliest years and before they were even born. Who really needs a \$500 hand-stitched crib bumper? "New parents think they need everything, want everything to be perfect, and don't know what things cost," says Downey, the Maryland planner.

Before you start setting up a nursery, come up with a spending plan. Accept hand-me-downs, and shop at yard sales and consignment and second-hand shops.

Remember that a lot of what you buy will only be used for about a year, sometimes less -- especially baby clothes.

1 | 2 | [next >](#)

#### Rate this Article

Click on the stars below to rate this article from 1 to 5

Low  High

[E-mail us your comments on this article](#)

[View all top-rated articles](#)