

And baby makes ... 3 on 1 paycheck?

Would-be parents advised to plan carefully before raising a family on a single salary

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When Brent and Reneé Dunn decided that she would become a full-time mom after their baby is born in February, they knew what it would mean for their income. "We started preparing a year and a half ago," says Mr. Dunn, 31, who has a joint professional counseling practice with his wife in Frisco. "It's amazing what percentage of income we're losing." But they're committed to providing their baby with a full-time parent and are preparing to move from a two-income household to one with a sole breadwinner.

Many families dream of being able to do what the Dunns are planning, and financial planners say anyone should be able to do it if they're willing to sacrifice.

Planners' main advice: Families need to plan in detail and come to a firm agreement on how they will adjust to living off of one paycheck. "I'm all for people who want to make lifestyle changes for their family, but the two ought to walk together," says Bob Stowe, a certified financial planner at Stowe Financial Planning in Plano. "They have to integrate the financial reality of their decision." There are tradeoffs to downsizing to one paycheck, and you'll have to weigh whether the positives outgun the negatives.

Part of the evaluation process is doing a dry run before one spouse actually gives up his or her income. "Practice, practice, practice," advises Trudy R. Turner, a certified financial planner and president of the Dallas-Fort Worth chapter of the Financial Planning Association. "My greatest piece of advice would be for the family to practice being a one-income family before they cease the second income. The family needs to actually live on one income for an extended period of time – three to six months or more – to see if it is realistic."

She recommends that a family:

- Deposit the entire secondary income into a savings account and don't touch it.

- Live only off of the primary income. Make a budget for one income. "We can't replace all of her income, so we will be cutting some expenses," Mr. Dunn says.

- Build up an emergency fund. What will help is that you will be saving money you were spending for things such as day care, work clothes, transportation, gasoline and meals.

- Keep track of the budget results.

"Record the family's experience of living on one income, including how they felt, their frustrations, their sacrifices, their surprises," Ms. Turner says. "Was it frustrating? Easy? What sacrifices had to be made? Can the family adjust to the changes? What did they not miss at all?"

For example, if you barely missed the extra money – because you didn't spend as much to feed that frantic both-spouses-working lifestyle, such as dinners out, maid service, lawn care, dry cleaning and lunch money – living off of one income may suit you. "If they find that their experience was frustrating and filled with anxiety, they will want to evaluate further before making the final decision," Ms. Turner says.

If you decide to do it, here are some other things to consider:

Attack your debts: One thing that you must do before ratcheting down to one income is to pay off or pay down your debts. "Be as debt-free as you possibly can be before you do that," suggests **Debra Outlaw**, a certified financial planner at Perryman Financial Advisory Inc. in Dallas. "Pay off all debt, starting with credit card debt, then pay off car loans."

Get medical coverage: The biggest factor you should consider is the impact on your health insurance coverage once you leave your job. Will you be covered by your spouse's health insurance policy or does your spouse have any coverage at all? "We see people who are self-employed or who work for a small company that doesn't have that insurance," says **Ms. Outlaw**, the Dunns' financial planner. "Without the health benefits, a lot of people are sunk, especially if she is thinking about leaving to take care of the kids and the husband doesn't have health insurance."

The Dunns currently have health insurance through Mrs. Dunn's part-time job at another company. They understand the implications of her planned departure from the firm after the baby is born. "Our medical expense will increase because we will be paying for our own medical insurance without the help of a company," says Mrs. Dunn, who's also 31.

Keep funding that retirement plan: When Mrs. Dunn leaves her part-time job, she will lose the company match to her 401(k) contributions. "I will continue saving for retirement without any kind of matching program, so all of our investments will be in a Roth IRA," she says.

Going to one income may leave you less to save for retirement, but don't eliminate it, "because it's a habit, and you don't want to lose the habit," Mr. Stowe says.

"The main breadwinner needs to continue to be saving for retirement because of the compounding factor, doing that over time and the dollar-cost averaging," **Ms. Outlaw** says. "All of those things are a real benefit."

Don't forget college savings: Another expense for couples who are losing one income because a baby is coming along is the added cost of raising the baby. For example, couples have to stretch their money to support a college fund. "A 529 [college savings plan] or whatever we select represents an additional new expense/outflow specifically connected to the very reason we will be shifting to a single-income family: because we are having a baby," Mr. Dunn says.

Take advantage of tax breaks: One advantage is that having a single income may push you into a lower tax bracket. "A family with one income tends to be advantaged tax-wise under the Internal Revenue Code, although those advantages have been reduced somewhat by efforts to reduce the marriage penalty in the tax code in recent years," says Mark Luscombe, principal federal tax analyst at CCH, which publishes information for tax professionals.

The so-called marriage penalty is a quirk in the tax law that forces many two-income married couples to pay more taxes than if they were single. "The primary advantage of a single income is that, under the higher marginal rate brackets, a given level of income tends to be taxed at a lower rate for a married couple filing jointly than for a single taxpayer with the same income," Mr. Luscombe says.

That's called the "marriage bonus." "If a single taxpayer has \$100,000 of taxable income in 2006, everything over \$74,200 is taxed at the 28 percent marginal rate," Mr. Luscombe says. "However, if that same taxpayer is married to someone with no income and files jointly, the highest marginal rate that applies to \$100,000 of taxable income is 25 percent."

At lower income levels, the marriage bonus has become larger as the marriage penalty is eliminated. "For the 10 and 15 percent marginal tax brackets, the income limits for married filing jointly are now double the income limits for single taxpayers," Mr. Luscombe says.

Increase your insurance coverage: Spending more money on life and disability insurance will take on special importance, because your family will be relying on the salary and earning power of one person. "I need to increase my disability insurance because if something happens to me as the sole provider of the family, then it's really putting my wife and my child in a risky position," Mr. Dunn says.

Finally, be realistic about how becoming a one-income family will change your life. "It's important to think about those things before they make that decision because if you stay home and you're miserable with your kids [because of financial pressures], I'm not so sure that you've benefited them more than going ahead and working and having some income," **Ms. Outlaw** says.

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