Money Makeover: Debt puts couple's retirement at risk

Family has to cut costs but also needs to earn more money, planner advises

By: Deanne Gage Special to the Star, Published on Thu Mar 26 2015

THE PEOPLE

Susan and Robert, both 57, are parents to two elementary school-aged children. They conceived their kids later in life due to medical issues. Susan has been a stay-at-home mom until recently, while Robert is self-employed in the arts field.

THE PROBLEM

Robert's business produces inconsistent income for the family. His earnings of $65,000 a year is just one-third of what he made five years ago. And after paying his business expenses, he's down to a modest $44,000. Susan works at two part-time administrative jobs that collectively pay her $18,000 a year. To keep afloat, the couple regularly overspends by $2,000 to $3,000 a month. They have a $94,000 line of credit, a mortgage of $149,000 and another $140,000 worth of business debt. They have no benefits so must pay out-of-pocket for dental care and other medical expenses. The one saving grace: the couple's home, purchased well before Toronto's real estate boom, is now valued at $1 million.

THE PLAN

Cutting costs goes without saying but to really tackle their debts, they'll also need to find ways to earn more money, says Sheila Walkington, a financial planner and money coach with Money Coaches Canada in Vancouver. "This couple needs to stop the bleeding. The debt is not only taking an emotional toll on them, it is putting their retirement in jeopardy," she says. Step one is revisiting and re-evaluating every expense they have, from groceries to gifts, and asking three questions:

- Can we do better?
- Can we cut out completely?
- Can we forgo until there is more money?

For instance, Robert's car and parking in downtown Toronto cost him $892 a month. Can the family downsize to one car?

The couple also spends $2,500 per year on summer camps and sport leagues for their kids. Is this necessary under the circumstances?

Robert faces some of the typical issues affecting the self-employed, Walkington notes. Cash flow is variable, business expenses add up and taxes are not deducted at source. But having a clear cash flow plan and forecasting is crucial to the success of any business, she adds. "He should work with a bookkeeper to get a clear sense of what is coming in and what is going out," she says. "How much can he afford to pay himself every month while also setting aside money to cover taxes each year?"

Walkington suggests he use Susan temporarily as she has a good aptitude for numbers and could help with the books and bill-paying for the business. This would then allow Robert to focus on his clients and building the business revenues.

Susan is looking for another job with more hours and benefits that will help cover some of the family's annual medical and dental expenses. "A higher income will not only help with cash flow it will also help build her payout from Canada Pension Plan," Walkington says. "Contributing more to CPP will help when it comes to retirement.

Luckily for them, the couple's home can help improve their situation. They could downsize, but that might be tough to do in a city with rising real estate values. They could sell and relocate to less costly part of Greater Toronto. Their current equity of more than $800,000 means they could roll all their current debts into the mortgage, which will help with cash flow. "But I only recommend it if Susan and Robert re-evaluate their spending/expenses and commit to living within their means," Walkington says. "They cannot afford to run up any more debt."

Since the couple has little in savings, their house is also their retirement plan, so it is imperative that they preserve as much equity as possible and not add any further to their debt, Walkington says.

Once the kids are finished high school, the couple should consider downsizing if they haven't managed to pay off their mortgage and all debts. "This will be necessary as their only retirement income source will likely be their government pensions which will not likely be enough to cover their cash flow needs in retirement," she notes.

Since their kids are still young and they have many liabilities, Walkington recommends the couple purchase term life insurance policies and disability insurance. They should also ensure they have a current will and powers of attorney in place.

THE PARTICULARS
Assets:
House: $1 million
RRSP: $19,000
RESP: $24,000 (plus undisclosed amount from grandparents)

Liabilities:
Mortgage: $149,000
Business debt: $140,000
Line of credit: $94,000
Credit cards: $2,900