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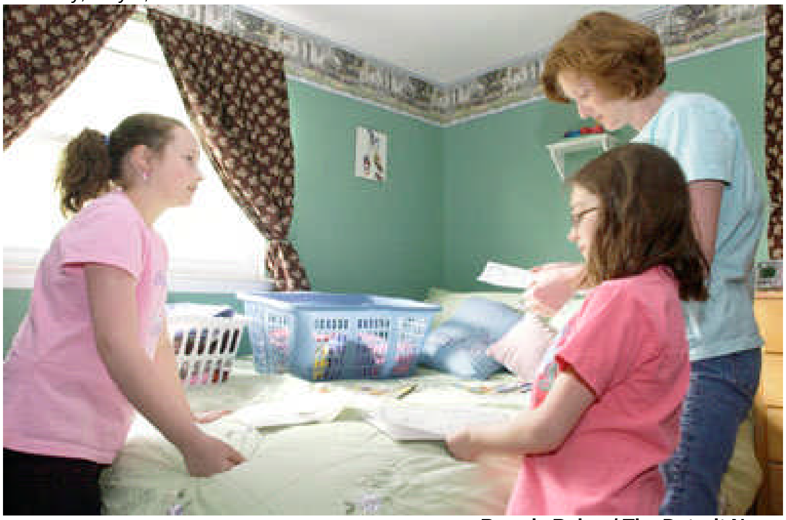

Brandy Baker / The Detroit News

Beth Moore, right, helps daughters Zoe, left, and Helen do homework in Moore's mother's Livonia home. Moore is working toward buying her own house and saving for her three daughters' education.

Money Makeover

Buying a home is tough, but possible for single mom

Even on a modest income, smart planning can secure retirement, other money goals

By Melissa Preddy / The Detroit News

Beth Moore didn't expect her life's journey to include a stretch as a single working mom.

But for the past three years, the divorced mother of three young daughters has made the best of what fate dished out. Thanks to her parents' willingness to share their Livonia home, Moore has paid off debt that lingered from her marriage, purchased a new van and landed a secure job as a 911 dispatcher in Ann Arbor.

Next on the list: a house of their own for Moore and daughters Zoe, 10, Helen, 7, and Lily, 4.

With an eye to home ownership, Moore has saved up more than $11,000 in a credit union account. She also took advantage of an Individual Development Account program, which uses grant money to provide cash matches to people who earn less than 200 percent of the federal poverty income guidelines.

The IDA loans, which are administered though social service agencies, are available to those saving for a home purchase, higher education or to start a small business.

In Moore's case, the IDA program will match her $2,000 contribution with $4,000 for a total of $6,000.

The Subject

Beth Moore, 34

Occupation: 911 dispatcher

Her objective: To buy a house, save for retirement and plan for her three daughters' education.

The Expert

Keith Southwick

Keith Southwick is a certified financial planner and owner of StraitGate Financial LLC in Novi.

His advice: If Moore must buy a home before she saves more cash, she should structure her mortgage to avoid private mortgage insurance. She'll be able to cover expenses but should look for ways to boost her income in the coming years.

Certified financial planner Keith Southwick lauds Moore's accomplishments.

"I admire you a great deal," said Southwick. "You have worked very diligently."

Nevertheless, Southwick has qualms. He points out that Moore's $48,000 income, which includes $8,820 annually in child support, will be stretched thin if she takes on the expenses of a house.

In fact, Southwick says, when the child support starts expiring in 2012, Moore will actually be operating in a deficit.

Has she considered renting a single-family dwelling? Southwick asked.

Yes, but the cost of renting actually runs a couple hundred dollars more each month in Livonia than her anticipated $800 house payment, Moore said. She really wants to stay in that city, where the kids are in school and near their grandparents, who provide free baby-sitting services. Any savings realized by moving to a lower-cost suburb would be eaten up by child care costs.

Another factor: the IDA funds must be used by next March or Moore will lose the $4,000 match.

Southwick's primary concern is that a substantial down payment would wipe out Moore's cash reserves. He wants her to earmark $6,500 — roughly three months of current expenses — as a rainy-day fund. If she does get into a house, higher costs would dictate that the emergency fund be raised to at least $10,000.

Setting aside the $6,500 now will leave Moore with roughly $10,500 for a down payment on a house in the $115,000 range.

By putting down less than 20 percent of the purchase price, Moore will be socked with the extra cost of private mortgage insurance, which protects the lender in case the borrower defaults. Known as PMI, this usually adds $50 or more to a monthly payment.

"I feel caught," Moore said. "Rates are really low now, but I don't have my complete emergency fund yet."

Well, Southwick said, "We are certainly not recommending that you *not* buy a home. The key thing is to walk in there knowing you have options."

For example, the planner said, sometimes a lower-cost variable rate mortgage is the best choice for people who plan to hold a property for less than five years.

Since Moore hopes to settle down for longer, Southwick suggested that she look into an 80-10-10 structure for her mortgage. That calls for a 10 percent down payment, a conventional mortgage for 80 percent of the purchase price and a home equity loan or second mortgage for the remaining 10 percent.

This strategy will eliminate the need for PMI. And while the interest rate on the home equity loan will be higher than on a regular mortgage, it will be tax-deductible, unlike PMI payments.

Should Moore buy a $115,000 house with a $10,000 down payment, Southwick figures the monthly charges for the 80-10-10 route will be $888, compared with $938 if Moore opted for a conventional mortgage and PMI.

Looking long term, Southwick projects that Moore's cash flow can cover the payment and other basic expenses through 2012. But taking into account rising expenses and the toll of inflation, she will need to figure a way to supplement her income by $15,000 a year by that point. Without it, Moore will start running in the red by about $4,000 per year; with it she can augment retirement savings and make progress toward other goals.

As for securing her own old age, Moore is eligible for a 457 account — a tax-deferred retirement account similar to a 401(k) — to which she currently is contributing about 5 percent of her gross pay. Another 5 percent goes to an employer-funded pension program.

"Work your way to 15 or 20 percent," Southwick urged. "Every raise, contribute at least half of it to financial independence."

Moore isn't sure of the terms of the pension, which Southwick urged her to review as soon as possible so she can determine whether to continue those contributions or add more to her 457 account.

Going by a standard formula, and assuming that Moore stays at her current job until 2030, Southwick figures the pension would pay out around $11,000 a year. When Moore starts collecting Social Security in 2032, it will provide about $17,000 annually. By drawing on her 457 for another $15,000 a year, Moore will have about $45,000 to live on at age 62.

This is much less than the $60,000 Southwick figures she will need to maintain her standard of living, and it assumes that she boosts her income by the $15,000 a year he suggested earlier.

While allowing that Moore is quite young and any of these variables could change dramatically by the time she nears retirement age, Southwick urges her to give top priority to her own security.

“Because you need to finance your own financial independence and wish to purchase the home, I really don’t see that you’ll be able to do much to save for the girls’ education,” he said.

Fortunately, grandparents and great-grandparents have already contributed some college funds for the children. And Southwick encouraged Moore to look into cost-cutting options, such as having her daughters complete their first two years of higher education at a local community college.

Other recommendations:

* Moore’s down-payment and emergency cash is earning only 0.4 percent interest in a credit union account. To reap more income, consider transfering it to ING Direct, a “virtual bank” accessed via Internet or toll-free phone number which currently is paying 2 percent on its Orange Savings Accounts.

* When she does buy a house, she should try to get on a bimonthly payment plan, which cuts interest paid over the long haul by whittling down the principal balance faster. Beware of fees and set-up costs, Southwick said, and make sure the money is applied promptly to the loan or the advantages of paying more often will be moot.

* Comparison-shop every year for everything from telephone service to auto insurance. The time spent in calling for updated quotes and taking advantage of special offers can pay off by keeping the “inflationary creep” at bay, Southwick said.

* With three dependents, Moore really needs disability insurance to augment the 24 months of coverage she gets through her job. Find out if more coverage is available via payroll deduction, Southwick said, keeping in mind that while the cost of group disability insurance is usually lower, the benefits tend to be capped at 60 percent of pay.

* Moore should raise the insurance deductible on her new Windstar to $500. “And when you get your emergency fund together, raise it to $1,000 and you’ll probably save $300 to $400 a year on your premium payments.”

* The 457 plan offers an asset allocation’ fund that distributes contributions across stocks, bonds and cash investments automatically, saving the investor the chore of diversifying the account. Unless Moore enjoys researching investments, “this would be the easy way for you to allocate,” Southwick said. “It’s nice — a lot of plans don’t offer this. It won’t be the winning fund, but it will be safe and steady for you.”

Brandy Baker / The Detroit News

Beth Moore looks over daughter Helen's homework as she talks on the phone. Financial planner Keith Southwick lauds Moore's efforts to save money for a home.