My 7 Smartest Financial Moves

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I admit, it seems a bit egotistical to write a column about my smartest financial moves. But I hope that, after reading my list, you'll reach two conclusions:

No. 1: "Clements' smartest financial moves aren't all that smart."

No. 2: "This stuff could make a big difference in my clients' lives."

CHEAP DIGS

I bought my first home in 1992 at age 29. It cost $165,000, which seemed like a boatload of money at the time.

In truth, I could have stretched and bought a more expensive place and, as my salary rose and I collected some hefty advances for various books, I could have traded up to a much larger house.

Instead, I stayed in my inexpensive starter home for almost two decades. And it was one of the smartest financial moves I ever made. Thanks to my modest housing costs, I was able to put away great gobs of money every month.

Indeed, I've come to believe that holding down fixed-living costs is perhaps the biggest contributor to financial success.

Many Americans want to save more for retirement and other goals, but simply can't afford to because they're boxed in by hefty mortgage payments, large car leases and a litany of other costs. My advice: Push clients to limit these fixed costs to 50% or less of their pretax income.

MORTGAGE FREE

By 2005, I had paid off my mortgage, which meant I was able to save even more each month. It also made it far easier to cope with the tuition bills when my eldest child headed off to college in 2006.

This might have some readers scratching their heads. Isn't a mortgage one of the cheapest ways to borrow, thanks to the mortgage-interest tax deduction and relatively low interest rates? That's true. Nonetheless, a mortgage's after-tax interest cost will typically be higher than the after-tax interest you can earn by purchasing high-quality bonds. To me, paying off my mortgage was the best bond I could buy.

SPLITTING UP

I would have paid off my mortgage even earlier — except I got divorced in 2000 and had to cash out my ex-wife. Divorce is sort of like a brutal bear market: It's a super-fast way to lose half of your money.

But many divorcing couples make it even worse, with endless legal wrangling that fills the pockets of the legal profession, ultimately resulting in the couple walking away with far less than 50% of their assets.

Aware of that danger, my first wife and I negotiated our own property settlement, and only then hired lawyers to put our agreement into legal language and calculate the child support payments. Our total legal tab came to $900.

SWAPPING OVER

For years, I couldn't fund either a tax-deductible or Roth IRA because I was covered by a retirement plan at work and my income was too high. Instead, I was left making nondeductible contributions to a regular IRA.

But the story has a happy ending. In 2010, the income limit for converting a regular IRA to a Roth disappeared, allowing me to convert my $111,249 traditional IRA.

Because the account included $48,575 of nondeductible contributions, I was taxed on just $62,674 of additional income.

In return for paying that tax bill, I now had a $111,249 Roth growing tax-free. My hope is to leave the account untouched and bequeath it to my children.

CHILD'S PLAY

Readers of my old *Wall Street Journal* columns might recall that I have two children. I used to write regularly about my efforts to instill good financial habits in Hannah and Henry. This was partly self-defense. I knew that, if they grew up to be financial deadbeats, there was a good chance that I would end up bailing them out, at which point their problems would become mine.

But my educational efforts were also partly about my own reputation. I figured it wouldn't look good if a widely followed personal finance columnist had two money-dumb kids.

Fortunately, the finance lessons worked. Hannah, now 27, and Henry, 23, are both financially responsible. I don't think any single strategy did the trick. But one tactic seems to have been especially effective: From early on, I made sure they felt like they were spending their own money, not mine.

When children are growing up, their parents foot the bill for everything, so kids have no incentive to curb their desires. I got around that problem by depositing my kids' pocket money

into a bank account every three months. Thereafter, if they wanted to buy something, they wouldn't ask me. Instead, they would have to ask themselves — and then troop down to the cash machine.

PRIVATE MORTGAGE

How much trust do I have in my children's good financial habits?

This year, I lent my daughter $381,000 so she could buy her first home. It was a good deal for her: She was able to behave like a cash buyer when bidding on properties, she didn't have the hassle of dealing with a bank and her closing costs were far lower.

It was also a good deal for me. We settled on the current average rate for a 30-year fixed-rate mortgage, which was 3.97%. That's more than I could earn by buying high-quality bonds. To keep everything on the level, we used National Family Mortgage in Belmont, Mass., to handle the paperwork and service the loan.

INDEX SUCCESS

I haven't just owned index funds for more than two decades, collecting the global market's performance while incurring tiny investment costs. I have also been a noisy advocate in a handful of books and countless columns.

I don't feel any great need to bang the table again now. People have heard the arguments, seen the performance numbers and used their dollars to cast an overwhelming vote in favor of index funds.

Are you still recommending actively managed funds? Good luck with that — because you, and your clients, will almost certainly need it.

Yet, on a few rare occasions, I have behaved as though markets weren't efficient, and never more so than in early 2009. As stocks tumbled and the cries of despair grew louder, it struck me that there were two possible outcomes: Either the global economy was going to implode, in which case even bond investors would have trouble getting paid, or the markets would come roaring back. I shifted my portfolio from 70% stocks to almost 95%.

But opportunities like that certainly don't roll around very often, so most of the time I sit quietly with a fistful of index funds. Honest.

Jonathan Clements, a new Financial Planning columnist in New York, is a former personal finance columnist for The Wall Street Journal. He's author of the newly released Jonathan Clements Money Guide 2016 as well as the forthcoming How to Think About Money. He's also former director of financial education at Citi Personal Wealth Management. Follow him on Twitter at @ClementsMoney.