RIVERPINE SERVICES
INCORPORATED

October 15, 2015

[redacted]

Dear [redacted] and [redacted],

It was a pleasure meeting with you recently to discuss your financial situation. I appreciate your time and the openness with which you discussed the relevant matters.

After reviewing your current situation as well as your financial goals, I see your path to financial freedom being complete in three phases. Phase I is to address the immediate negative cash flow and should be completed in around 75 days. Phase II deals with eliminating the remaining non-mortgage debt, as well as beginning a savings and investing program. Finally, Phase III is about getting the mortgages paid off and really being able to live, and give, like no one else (to steal a phrase from FPU).

Phase I – Immediate Steps to Address Monthly Cash Flow Issues

Not surprisingly, this step includes suggestions that may feel uncomfortable to either (or both) of you, but it's important to quickly address the negative cash flow issue.

For this phase, I've broken down the unsecured debt into two parts – school loans vs. non-school loan obligations. Per the spreadsheet data, total unsecured debt is $91,000, of which school debt totals $25,000.

Phase 1 is the elimination of the $66,000 in non-school loan debt, and reducing the payments for the mortgage loans. Here is the plan to do so:

Description (See *Additional Details* below)	**Amount Generated for Debt Elimination**
Refinance personal residence (with "cash out" to repay debt) (1)	$44,000
Refinance rental property (with "cash out" to repay debt) (2)	$12,000
Sell the current [redacted] to eliminate the debt and use the net proceeds to replace it with a fully paid for unit (3)	(Debt eliminated) $10,000
Total	$66,000

P.O. Box 1675 · Ashland, Virginia 23005 · 804-883-6528 · 804-883-6568 Fax
www.riverpineservices.com - www.60minutefinance.com

Additional details:

(1) Refinance personal residence:

- 30 year, fixed rate loan
- 80/20 loan to appraised value – new loan balance of around $158,400 (old balance is $114,315).
- Interest rate should be around 4.25% based on current marketing conditions, credit score of mid-700's or above, and documented (via tax returns) income for the last two years
- Monthly payment on the primary residence will go from the current $2,018 per month to $1,103 ($803 plus your escrow payment of $300).
- The unsecured creditors will be paid off by the closing agent. They will require that the credit card accounts be closed, which I'd recommend, too.

(2) Refinance rental property:

- 30 year, fixed rate loan
- 70/30 loan to appraised value – new loan balance of around $70,600 (old balance is $50,000).
- Interest rate should be around 4.75% based on current marketing conditions, credit score of mid-700's or above, and documented (via tax returns) income for the last two years
- Monthly payment on primary residence will go from the current $670 per month to $370.
- The unsecured creditors will be paid off by the closing agent. They will require that the credit card accounts be closed, which I'd recommend, too.

(3) Instead of selling the [redacted], another option would be to use $6,000 of the cash on hand, and increase the primary mortgage loan by an additional $4,000 to raise the $10,000 needed to pay off the current [redacted] loan. However, I prefer selling the [redacted] instead as doing so maintains more liquid cash and a lower mortgage balance and payment. Later a more expensive [redacted] can purchased with cash.

To review the results of these steps:

A. Your unsecured debt is reduced from $91,000 to $25,000.
B. Your minimum payments on your unsecured debt goes from $1,800 per month to only $180 (the two student loans) – ***a monthly savings of $1,620 per month***.
C. While the amount owed on your mortgages increases from $165,000 to $229,000, your payment drops from $2,680 per month to only $1,473 – ***a monthly savings of $1,207.***

D. The total reduction in your monthly payments (B and C above) is approximately $2,800.
E. Some of your current mortgage debt is subject to periodic rate adjustments, which exposes you (not the lender) to potential interest rate risk. The interest rates on the newly refinanced mortgages are fixed for the entire term of the loan, so that risk is transferred to the lender.
F. No additional withdrawals from your 401(k) plan would be required each month, allowing those funds to continue to grow tax deferred.

Phase I should flip your monthly negative cash flow to a positive amount instead. From here you are ready to move to Phase II……

Phase II – Pay Off Remaining Unsecured Debt, Build Cash Reserves and Begin Long-Term Saving

With the positive monthly cash flow generated from Phase I, I recommend the following:

A. Increase your giving to your church to a full tithe of 10% of your monthly income – around $200 more per month depending on [redacted]'s job situation. As the Bible states in Malachi 3:10: "*Bring the whole tithe into the storehouse, that there may be food in my house. Test me in this," says the LORD Almighty, "and see if I will not throw open the floodgates of heaven and pour out so much blessing that there will not be room enough to store it.*" This is the only reference in the Bible where He explicitly instructs us to test Him.

   This is an area of personal financial planning/spending that is truly counter-intuitive: to increase your wealth, spend more money! I can't explain it mathematically, but I've seen so many instances where God delivered on this promise. Please strongly consider increasing your tithe and then watch as God will *throw open the floodgates of heaven!* Of course, be sure to do this with a spirit of love for the Lord, appreciation for what He has given you, and your desire to be obedient to Him, not with a selfish heart seeking financial gain.

B. Use the remaining positive cash flow (after Step A above) to make additional principal payments against the two remaining student loans (estimated to be around $1,500 extra paid to them each month). These debts should be eliminated in approximately 16 months (perhaps even shorter depending on [redacted]'s employment status).

C. Do **not** make extra principal payments to the mortgages at this time.

D. Once the student loans are paid in full (Step B above), use the funds previously dedicated to the student loans to build your emergency cash balance from the current $7,000 to the $25,000 - $30,000 range. These funds should be in a savings account linked to – but separate from – your checking account. I use CIT (www.bankoncit.com) for my emergency fund and have been pleased with my experience. They also pay a higher rate of interest than most local banks and are FDIC insured.

Remember these funds are not an investment – they are "*insurance*" to be used only for ***true emergencies***. If funds are used from this account, other savings and investments should cease until they are replaced from monthly cash flow.

E. Once your emergency fund is fully funded (again, I would recommend $25,000 to $30,000), you could then consider any ***modest*** (perhaps $5,000) home improvement projects that had been deferred pending the repayment of unsecured debt. Additional funds for car replacement or other capital projects should be saved here. ***Please keep these amounts modest*** as long term savings has not yet started, nor have the mortgages been repaid in full (Phase III).

F. Once Step E is complete, I'd recommend beginning to save 15% of your income toward long-term needs. If you have earned income, a Roth IRA is a great investment vehicle for tax-FREE growth. As a custodian I recommend Vanguard (www.vanguard.com) as they offer a wide-range of low-cost index funds. We have not discussed investment strategies, but I'd be happy to do so in the future. To better understand my investing recommendations, please review the various investing posts on my blog: www.60minutefinance.com .

Phase III – Pay Off The Mortgages

Phase III is quite simple. After you have increased your tithe, paid off all unsecured debt, built up your emergency fund, begun long term savings, and saved for any modest special projects and sinking funds, direct your positive cash flow toward paying off your mortgage early.

There is a debate about whether at these low interest rates it makes sense to pay off your mortgage early. I am firmly of the opinion that being debt-free (in other words, no longer a slave to the lender) is a key step on the road to true financial freedom. While investing the funds could *theoretically* return more than the interest cost, you eliminate the risk of investment losses if the funds are used to retire the mortgages instead. Begin with the mortgage on your personal residence and repay the loan on the rental property second.

Other Items for Consideration

Listed below are a few other items for your consideration:

- Adopt and commit to a monthly spending plan, prepared before the month begins, that allocates every dollar of income. Understand that it will take time to perfect the process. Utilize the cash envelopes for categories that are easily overspent for most couples: groceries, eating out, entertainment, and clothes at a minimum – add other categories as you see the need. Keep the lines of communication open and work together on the budget each month. It is fine for one person to prepare the budget, but the other spouse must take an active interest in reviewing and making changes to the spending plan. Even after all three phases are complete, continue to prepare your monthly budget.

- You should commit to not using debt in the future (other than for the mortgage refinance described above). I understand the use of credit cards as a payment convenience, but even if the full balance is paid each month, it's very easy to overspend when we use credit. Thus the reason to use the envelopes discussed above for the categories that overspending is the easiest. At a minimum, try to use envelopes for a few months and test whether you spend less when using them. So far I've never seen someone who didn't realize a savings by using envelopes for certain expenses.

- Overall your discretionary spending seems reasonable. However if reductions for a period of time can be found, even small ones, plan to do so. For example, reductions in groceries, eating out, and perhaps lower cost cell phones/Internet access are possible. I know the amounts provided on your budget forms were just estimates, but if they are somewhat accurate, they would be prime candidates for reductions.

  While individually these costs are not necessarily material, in total they will make a difference in the speed with which the debt can be paid off. After a period of time of serious debt elimination, some of these reductions can be slowly reversed.

- Should your income increase during Phase I or II above, please dedicate the vast majority of the increase to the step on which you are currently working. *Don't allow your spending to increase dramatically until Phase II is complete*. It's much better to continue to live as modestly as possible to complete the steps in a timely manner.

- We didn't specifically address this in our meeting, but I'd recommend implementing important personal documents such as wills, living wills, POA's, etc., if they don't already exist. Obviously it's better for you to make such decisions instead of the court system. The probate process (and cost) can be greatly reduced with a properly designed estate plan.

- The 401(k) investments are invested very aggressively. While this may fit within your risk *tolerance*, as you age your *capacity* to handle such risk will most likely diminish. I would recommend reviewing your investment allocation looking for lower cost, lower risk, and better diversification. I'd be happy to share some recommendations about investing strategies to minimize risks and costs. Let me know if you'd like to discuss this later.

I know the achievement of these goals can seem a long way off, but they are presented in this order for a reason. I'd much rather see it take a bit longer, but be completed in the order listed, than to skip a step and later find yourselves in a financial mess. If you'll both commit to living frugally for a period of time, you will be amazed at how quickly these goals can be attained. God really can work miracles when His children earn, spend, and save as He directs in His Word.

Please review these recommendations and feel free to contact me to discuss or clarify any of the items. Congratulations on committing to the steps necessary to bring financial peace and freedom to your life.

Best regards,

John A. Madison, CPA

Disclosure

Counseling and coaching services are designed to give you accurate and authoritative information with the regard to the subject matter covered. It is provided with the understanding that we are not engaged to render legal, accounting or other professional advice. Since your situation is fact dependent, you should additionally seek the services of an appropriate licensed legal, accounting, mortgage or investment professional.