Financial Planning Checklist for College Grads

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According to the National Postsecondary Student Aid Study (NPSAS), graduating seniors with educational debts carry an average debt load on the order of $20,000. More and more, college students are beginning their working lives with fairly heavy debt loads. It's more important than ever for newly-minted grads to hit the ground running with a plan for their finances.

Based on the things I've observed in my clients (and others), here are nine key things that I think new college graduates should give attention to:

(1) Understand How Your College Loans Work

A surprising number of graduating students don't understand the potential benefits of consolidating their college loans after graduation. There are lots of resources for understanding educational loans at finaid.org and studentloandconsolidator.com has resources to help you understand loan consolidation rules and strategies.

(2) Don't Mess with the IRS

Once you start working, be sure that you have a rough idea of how much you should have withheld from your paycheck for taxes. Your employer's payroll department may be able to help you with this. If you withhold too little, you could wind up having to pay a tax penalty. Withholding too much is not as risky, but it's dumb – you're basically giving the government an interest-free loan.

You need to be especially careful if you work as a self-employed contractor. In this situation, you're responsible for paying estimated taxes on a quarterly basis. Fail to do this, and there's a chance that you'll be hit with some nasty penalties. If figuring out how much to pay in estimated taxes is too overwhelming, the last thing you want to do is avoid it altogether. In a pinch, try using one of the many tax software programs available to estimate how much you need to pay, or consider yourself an exception to item #9.

(3) Get Health Insurance (and perhaps disability, too)

Many employers provide group health insurance coverage that can be paid for through payroll withholding. In Massachusetts, having health insurance is mandatory. As a new college graduate, you may feel invincible, but if you break a leg or come down with appendicitis, not having health insurance could leave you stuck with big-time debts.

Ditto disability insurance; this coverage provides partial continuation of your income if you become unable to work due to a long-term illness or injury. Statistically speaking, a person under 60 is much more likely to be disabled for a period of time than they are to die.
As for life insurance, it's good to have if there's someone who is dependent on your income. If you're single, though, odds are that you don't need life insurance coverage yet. Take a quick look here to see reasons why a person might need life insurance.

(4) Hold off on Buying a Car

A lot of people don't realize that a car is usually one of the biggest sources of household spending. If you can get by using public transportation, you'll save a lot of money *. If your circumstances require that you own a car, check out a good-quality used vehicle. There are tons of resources online to help with buying a used car. Doing this will save you money, and if you absolutely have to get a car loan, you'll be able to pay the loan off more quickly.

* (Addendum) – The American Public Transportation Association just released a study on the average amount that a person can save by using public transportation instead of owning a car. Boston ranked first among twenty cities listed, with an estimated monthly savings of more than $1,000/month for those who use a public transportation pass instead of a owning a car.

(5) Start Saving for Retirement

When you're just out of college, retirement probably seems like a ridiculously distant goal, but the sooner you start saving for it, the easier it will be to do. If you want to be able to retire early, you'd better start saving early.

If your employer offers a retirement plan into which you can contribute, be sure to sign up for it if there's an employer matching contribution. If there's no employer match, you might be better off opening a Roth IRA. In that case, be sure to set up your contributions through an automatic withholding system so that you don't even

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(continued)

have to think about saving the money. You'll get used to just spending what's left.

(6) Work out a Rough Spending Plan

If you start planning your spending now, you can develop good habits that will make your life a lot easier. Try using one of the online budgeting systems, like mint.com or wesabe.com so that you can minimize the amount of effort required to pull this off.

(7) Fight the Urge to Splurge

If there are some cool but expensive items that you're dying to have, start saving for them. Buying stuff with long-term credit should be avoided; you'll spend a lot more for things if you pay for them using long-term credit.

(8) Start An Emergency Fund

Especially these days, it's good to be prepared for the possibility of a layoff. For most people, it's not realistic to try to build an emergency in a short period of time because you have lots of things to save for. But if you're doing the other things in this list, you'll be less vulnerable in the event of a financial emergency. Set a goal of building up an adequate fund over a couple of years. Browse some earlier posts for pointers on why you need an emergency fund, how big your emergency fund should be, and how you should invest the money in your emergency fund.

(9) For Now, Ignore People Who Tell You to Hire a Financial Planner

Okay, I realize that this is a heretical statement coming from a financial planner, and I'll probably get some flack for it from my peers.

But I say this because most people just out of college have nothing to invest, and their finances are pretty simple. In this situation you mostly need to focus on developing good money habits and learning what you can about managing your life. Do that for a few years, and by the time you have your next big life event – marriage, a better job, etc. – you'll be a logical position to consider getting professional financial advice. Unless you manage to leave college with some inherited assets or you just need serious help with tax planning, it's probably not cost-effective for you to hire a financial advisor.

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