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A CRASH COURSE IN SETTING A BUDGET

By: Lynn Asinof, Globe Correspondent
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When Rachel Berman graduated from college in 2002 with a degree in neuroscience, an essential part of her education was missing: She'd never learned the basics of money.

Although Berman clearly demonstrates frugality she drives a 10-year-old car and shares rent with four other people she knew little about basic financial tools like credit ratings, mutual funds, automatic deposit, and retirement accounts. Now with plans for graduate school taking shape for fall 2007, she's realized that her real-life education needs some help. "I've been out of college for three years and have yet to save a penny," she said in applying for a Boston Globe Money Makeover. "I have no idea how to invest or what to do with the money I make other than spend it."

Berman is like many others her age who find they lack the tools to manage their finances. Too many young people today graduate with big college loans, a pocketful of credit cards, and little knowledge of how to budget. Indeed, state officials say research shows that young adults spend 30 cents of every dollar they earn paying down debt, while their annual bankruptcy filings have increased 51 percent over the last decade.

Berman, 25, who makes $34,000 a year as a clinical evaluator for a Dartmouth University study at the North Suffolk Mental Health Association, is in better shape than many. She has purposely avoided getting a credit card, and she's conscientious about paying off her $13,600 in college loans.

But she's still living from paycheck to paycheck and stymied how to ever get ahead. "I'm just trying to figure out where I spend my money," she said.

To find out, fee-only financial planner **Ted Yoos** of Back Bay Financial Group in Boston had her write it all down. The questionnaire he provided asked her to calculate everything from the pet care expense for her two dogs ($660 a year) to charitable contributions ($400 a year).

The resulting data showed not only where Berman's money was going, but also that there was no wiggle room in her budget. To create some savings, **Yoos** said she could either look for a part-time job to supplement her income or cut back on some of her expenses. And if she opted to cut back, he said, the food bill which was eating up 20 percent of her income was a good place to start.

Berman, a vegetarian, says her macrobiotic diet means that she buys all organic food, often at pricey markets. She likes to eat out, and she loves cooking with friends at regularly scheduled group dinners. "I tend to buy the highest-quality food that I can, and that adds up to a lot of money," she says.

But when she saw the numbers, Berman was "pretty horrified" at the nearly $7,000 annual food expenditure, and agreed it was time to "tone it down a bit."

One good way for Berman to enforce savings, **Yoos** said, is to make sure the money never shows up in her wallet. He suggested that money be automatically taken from her paycheck and deposited in some sort of savings vehicle.

Yoos recommended a two-pronged approach, starting with a savings or money market account that serves as an emergency fund.

"I usually recommend that clients have an emergency fund equal to three to six months of living expenses," he said. In Berman's case, a three-month safety net would come to about $7,000.
At the same time, **Yoos** said, Berman should start saving for retirement. He bolstered his recommendation with a long explanation of the benefits of tax-free compounding. Berman was enthusiastic.

The first step, he said, was to find out if her employer provided matching funds for contributions to its 403(b) retirement plan. "You don't want to pass up free money," he said.

If not, he said, she should open a Roth individual retirement account while her income is still low enough for her to qualify. Income limitations for single people kick in at $95,000 of adjusted gross income. Among the advantages that the Roth offers is the fact that contributions which grow tax-free can be taken out at any time without penalty. The earnings, however, would have to remain until she is 59 1/2 to avoid penalties.

Applying ethical considerations to her soon-to-be investments, Berman said she wanted to put those retirement funds into "green" investments. **Yoos** recommended she investigate three well-known socially responsible options: Vanguard Calvert Social Index fund, TIAA-CREF Social Choice Equity fund, and those offered by Pax World Funds.

By tucking away $150 a month half into her emergency fund and half into her retirement savings Berman would build up $900 a year in each. And if she got a bonus or raise, **Yoos** suggested she increase the amount.

"I can do that," Berman said. In fact, she said, if she just trimmed her purchases of expensive olive oil and organic sea salt she would probably be halfway to her goal.