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Getting Today's Best Returns from a Home Renovation

It's a much different picture renovating a home in 2007 than in 1997. Fueled by huge gains in the price of real estate, homeowners a decade ago were tapping home equity with little care since prices were expected to keep climbing, more than covering the cost of such improvements.

Today, with the slowdown in real estate and the widening damage in the subprime loan market, home prices aren't rising much – and falling in some places. And lenders tend to be a lot choosier these days about who to do business with. So before considering a home renovation, it makes sense to make sure your financial house is in order:

Start with your credit report: If you're considering borrowing, make sure your credit report and payment records are in the best possible shape. As in most economic crises, lenders go from being permissive to squeamish in an instant, so even people with good credit behavior are going to be under the microscope. Start by checking your credit report -- you have the right to get all three of your credit reports – from Experian, TransUnion and Equifax – once a year for free. You can do so by ordering them at www.annualcreditreport.com, but do so at staggered times throughout the year so you can catch potential errors in your report as they happen. Also, if you need to clean up any bad behavior – late bills, heavy credit card debt, clean it up before you wander back into the real estate market. Remember that a bad credit score can raise the total cost of your mortgage.

See what kind of payoff your chosen renovation will have: During the housing boom, people thought virtually any renovation would offer big returns. That wasn't true then, and it's particularly untrue now. Take the time to figure out what renovations have the best chance for return on investment now – go to *Remodeling* magazine's annual *Cost vs. Value* report online (<http://www.remodeling.hw.net/content/CvsV/CostvsValue-project.asp?articleID=381305§ionID=173>) and check 2006 project cost averages for your region of the country. In this market, renovate because it's going to bring you comfort or pleasure, not because you're expecting immediate profits.

Know how long you'll need to stick around: When you sell, remember that most married couples can exclude from their taxable income up to \$500,000 of gain and most individuals filing single or married filing separately can exclude up to \$250,000. It's required that you must have owned and used your home as your principal residence for two out of five years before the sale. The exclusion is generally applicable once every two years. However, if you are unable to meet the two-year ownership and use requirements because of a change in employment, health reasons or unforeseen circumstances, then your exclusion may be prorated.

Beware the bump in property taxes: The great thing about a more valuable home is the potential higher value when you sell. The bad thing is a visit from the county assessor – more valuable property tends to lead to higher tax assessments. Make sure you cannot only afford the cost of renovation, but what you'll need to pay higher taxes if your home is reassessed.

Don't forget to deduct applicable sales tax: If sales tax was imposed on a major renovation or if your state or locality imposes a general sales tax on the sale of a home or the cost of a substantial addition or major renovation, you might be able to deduct it. This alternative is particularly valuable in low-tax states, and the sales tax paid on the purchase of some large items including the purchase of a home or major addition can be added to the table amounts.

Make sure your renovation makes your home salable: A discussion with a real estate agent or someone familiar with the value of improvements in your immediate neighborhood can tell you what will add to value or take it away. For instance, a big addition can take away from the value of a home if it's not aesthetically in tune with the rest of the neighborhood. Obviously, any renovation that keeps your house on the market longer better be worth it now because it might damage your sales prospects later.

You May Love Each Other, But Should You Invest Together?

It's one of the most important questions a couple will face in their relationship but it so rarely gets asked until a relationship is well underway – should we pool or separate our money for investment?

The answer is as unique as the both of you. But there are some critical facts and some questions to consider as you develop a financial strategy for a lifetime.

Pooling can be a great idea after a marriage because the both of you are legally bound together, so why not bind your finances for potential maximum return? Many financial experts believe it's a good idea for the simplest of reasons: The bigger the pile of money you two can gather, the greater the potential for financial gain with the right advice.

But there's more to it than simply combining your assets. Pooling your investment dollars should produce not only shared decision-making, but shared awareness of everything going on with your finances for a lifetime. It's the kind of cooperation that will not only benefit you all the years of your marriage, but also provide a surviving spouse the knowledge to function if the other dies suddenly or is incapacitated.

It's a move that woman need to consider in particular – it's to their advantage to maximize the total investment pie because chances are they will be the lower-earning spouse, as they may go years without income if they stay home to raise children. And if the marriage breaks up – as roughly 40 percent of them do these days – she'll need extensive assets to prepare for a retirement that will be statistically longer than her husband's.

But how about a couple that wants to plan separately? The first question is: Why? There may be compelling reasons – for instance, one spouse has assets he or she wishes to protect from another spouse engaged in a high-risk business proposition. Others may have significant inherited family assets that need to be protected for heirs from potential loss in a divorce. And of course, this is the least attractive reason, but it happens: One spouse doesn't simply trust the other.

These questions and more are a good reason for a couple planning to marry to sit down with a trained financial expert like a Certified Financial Planner™ professional to go over their respective and combined goals for home ownership, retirement, kids' college savings and various other lifestyle goals. A visit to tax and relevant legal professionals makes sense before the wedding as well.

THINGS TO CONSIDER:

What approach will get you to your goal faster? Young people starting out literally need to save every nickel to save for a first home. It makes sense to figure out how much you can jointly put aside and where to invest that money based on your risk tolerance.

How can your employer help? Obviously max out on your 401(k) and other retirement savings options – particularly if there's significant company matching involved, but check to see if your other benefits will do more for you and your spouse. See if joining on one or the other health plan might be a better value than going it alone on your respective plans. If you have a health savings account that your spouse hasn't, see how you can make that a part of your overall joint investment strategy. Also, don't forget employee discounts that might cut your overall household spending.

Let your competing investment styles...compete: There are plenty of studies on this, but they seem to hold steady: Men tend to take more investment risks, women seem to be risk-averse. One of the advantages to working with a trained financial expert is not only their ability to make solid investment suggestions for you, but to identify the differences in your investment approaches and find compromises that work best for the both of you.

Talk: Talk about your financial expectations and what goals you'd like to achieve. Talk about what you're afraid of. And most important, talk about your money history – your credit rating and score, any troubles with credit in the past, including bankruptcy. Oh, and if you survive these initial discussions, make a promise to talk about money once a month.