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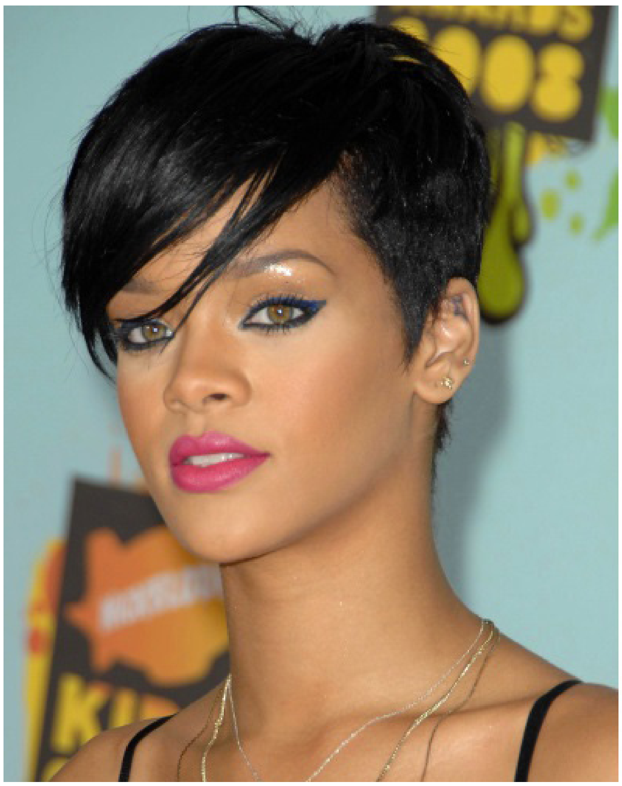
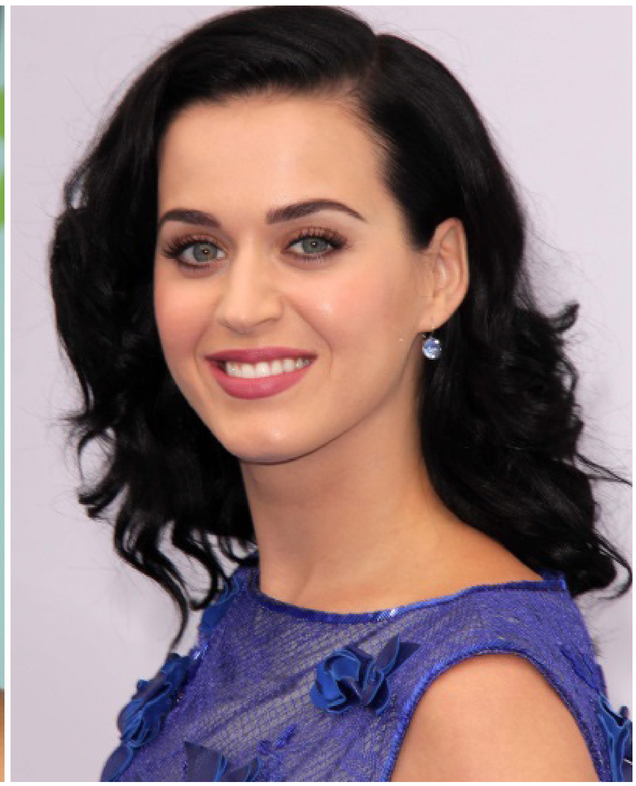
Author: Molly Triffin

5 Ways Katy Perry and Rihanna Botched Their Finances — What You Can Learn





You can cruise around in a convertible and sip Moët like it's Perrier, but a high net worth doesn't automatically grant you a high financial quotient.

"People tend to assume that wealthy individuals must either be pretty darn fiscally smart in order to make that much money in the first place — or they are able to afford the very best in professional advice," said Judy McNary, certified financial planner (CFP) and founder of McNary Financial Planning in Broomfield, Colo.

"While this can be true — Mick Jagger, for instance, studied at the London School of Economics — there are far more examples of celebrities who have fallen prey to poor money decisions," McNary says.

You need look no further than the late actor Heath Ledger, Katy Perry, Madonna, NBA player Tim Duncan and even current White House contender Senator Marco Rubio, who all have one thing in common — seriously mismanaging their money.

From succumbing to lifestyle inflation to turning a blind eye to proper estate planning, you can see the various ways some of the world's brightest — and wealthiest — luminaries have botched their financial lives so you can avoid the same costly mistakes.

Mistake #1: Neglecting to Draft an Estate Plan

Like a cluttered garage, a will is probably something you know you should tackle… just as soon as you have a spare afternoon.

But not putting thought into an estate plan has its consequences. Just look at actor Heath Ledger. When he passed away in 2008, his will hadn't been updated since 2003, which meant that his partner, actress Michelle Williams, and their daughter, Matilda, weren't included. So Ledger's millions went to his parents and sisters.

"Nearly two thirds of Americans don't have a will," said attorney Andy Mayoras, coauthor of "Trial and Heirs." "Part of the reason is that people don't want to think about dying."

"Many of us also mistakenly assume that we don't have a big enough estate to merit a will," added "Trial and Heirs" coauthor and attorney Danielle Mayoras. "But when you add up home equity and personal belongings, there's often a substantial estate."

How Not to Make the Same Mistake as Heath Ledger

Consider hiring an attorney who specializes in estate planning — and once your plan is in place, review it every three to five years.

"Your financial and family situation can shift, as do the laws, so you need to reevaluate accordingly," said Danielle Mayoras. For example, the threshold for estate tax laws have changed dramatically over the years, which might influence you to give away more money during your lifetime or set up an additional trust.

Plus, legwork now can prevent conflict later. "Families tend to fight over estates when the proper groundwork isn't done," said Andy Mayoras.

Mistake #2: Succumbing to Lifestyle Inflation

After inking an $800,000 book deal, Florida senator Marco Rubio proceeded to splurge on all sorts of luxury items that he really couldn't afford — like an $80,000 speedboat and a leased $50,000 Audi Q7.

As a result of his mounting debt, Rubio had to liquidate a retirement account, sell his home at a loss, refinance his mortgage and even take on a second job teaching.

It's called lifestyle inflation — and it's often driven by a need to maintain appearances.

“Celebs may feel they need to show a level of status to promote their image and maintain their success,” McNary said, adding that plenty of average earners also fall victim to the temptation to live a more lavish lifestyle than their income can cover.

In fact, McNary once had a client say, “I don’t get it — my husband and I both make good money and we’re still driving Toyotas. How are our friends affording McMansions and fancy cars?”

How Not to Make the Same Mistake as Marco Rubio

The hard truth is that someone will always have more than you, so try to avoid comparisons. Instead, identify the indulgence that’s most important to you and focus your savings efforts there.

“It’s fine if a speedboat is your thing. After all, we work in order to be able to do things we enjoy,” McNary said. “But you need to scale back on other purchases.”

Once you’ve pinpointed your key splurge, set up a dedicated savings account to fund it and have a portion of your paycheck automatically deposited into that account. “The better you are at controlling your everyday spending,” she said, “the more you’ll have left over for the fun stuff.”

Mistake #3: Not Paying Your Taxes on Time

April 15 can trigger waves of dread, but simply ignoring your taxes will only make things worse.

Consider the case of photographer Annie Leibovitz. According to New York magazine, the I.R.S. put $1.9 million worth of liens on her properties because she failed to pay income tax.

Or skier Lindsey Vonn, who owed $1.7 million in back taxes. In a Facebook post, she claimed that she had been unaware of the balance because she wasn’t handling her own finances.

How Not to Make the Same Mistake as Annie Leibovitz and Lindsey Vonn

Hiding your head in the sand and pretending a financial problem doesn’t exist is a natural impulse. There’s even a term for it — “the ostrich effect.” Economist George Loewenstein of Carnegie Mellon University described it as a human tendency to “avoid information following neutral or bad news, which can induce costs due to delays in information acquisition in adverse environments.”

Fail to pay enough in taxes, and you could be slapped with a penalty equaling 0.5 percent of your total unpaid sum per month. If you never file in the first place, the fine rises to 5 percent. On top of that, you’ll have to pay interest on the unpaid tax liability — the federal short-term interest rate, plus an additional 3 percent. There’s a different program for those who owe more than $50,000.

If you find yourself owing big bucks, Lisa Greene-Lewis, a certified public accountant (CPA) and tax expert for TurboTax, said overwhelmed taxpayers have options. “Under the I.R.S. Fresh Start program, you can set up an installment plan to pay your tax debt back over six years,” she explained. There’s an initiation fee of $100, plus nominal interest, but the I.R.S. will slash the penalty on your bill from 0.5 percent to 0.25 percent.

To try and avoid a hefty year-end tax bill altogether, Greene-Lewis had a few suggestions: If you're self-employed, pay estimated quarterly taxes. Expecting a bonus or raise? Readjust your withholdings. And consider maxing out your retirement accounts, if possible, to lower your taxable income.

Mistake #4: Skipping a Prenup

A prenup spells out what happens to your financial assets in the event of divorce or death. But the legal document does more than simply safeguard the money you already have — it also shields you from any debt your spouse might accrue, and protects your future earnings.

Consider the defunct marriage of Madonna and director Guy Ritchie. Even though her fortune was much more substantial, the Material Girl never sought a prenup from her director-husband-to-be. Eight years later, when she filed for divorce in 2008, she had to fork over between $76 million and $92 million to her ex — nearly a fifth of her net worth at the time.

But even if you and your partner are in the same financial boat when you wed, your career could soar over the years while his stagnates. Katy Perry earned an estimated $44 million during her marriage to Russell Brand, far outpacing his pay. They, too, didn't have a prenup. So, Brand was legally eligible to receive half of her assets, although he decided not to go after her money.

"Highfliers will often have the opportunity to remake the money they lost in a divorce, but if you lose half your retirement nest egg, you may not have a chance to rebuild it," said matrimonial lawyer Arlene Dubin, author of "Prenups for Lovers."

How Not to Make the Same Mistake as Madonna or Katy Perry

If you're already married, you can opt for a postnuptial agreement — although it's not as airtight. Los Angeles Dodgers owners Frank and Jamie McCourt signed a postnup in 2004, yet it was thrown out as invalid during their legendary 2011 settlement. Theirs was one of the most expensive divorce proceedings in California history, and it highlights how a postnup can offer too little legal protection, too late.

So, if you're getting married, bring up the P word as part of a broader conversation about how you'll approach your finances as a team, making it feel like a truly collaborative process.

"Be open and honest, and express what your motivation is," Dubin said. "Try something like, 'We've had a seaside cottage in my family for years, and I need to make sure it will remain in my family,' or 'I have substantial student loan debt, and I don't want you to ever be saddled with that.'"

Another advantage of a prenup is that it requires full disclosure of each person's assets, liabilities and income — getting it all out in the open prior to the Big Day.

Mistake #5: Delegating Too Much Financial Responsibility

A financial advisor can help you navigate all manner of potential money mistakes, but before you partner with anyone, do your homework to ensure you're working with an accredited professional.

In 2014, Rihanna won a $10 million settlement after claiming that her accountant mismanaged her funds, leading to tens of millions of dollars in losses. And San Antonio Spurs MVP Tim Duncan recently sued his financial advisor, alleging he forged his signature and siphoned his earnings, costing Duncan over $20 million.

In other words, you can pay a high price for assuming that hiring a money manger gives you license to check out of overseeing your finances.

How Not to Make the Same Mistake as Rihanna

"Go with someone who has professional credentials, like a CFP, CFA or Personal Financial Specialist (PFS)," McNary said, highlighting the subset of no-fee planners who have a fiduciary responsibility to put their clients' needs first and are not licensed to receive commissions.

"These advisers will lay out your options, but you are ultimately responsible for deciding how you want to invest," explained McNary. And when you have an initial meeting with a potential planner, McNary suggested saying something like, "We have an extra $100,000 and are considering using it to expand our house, contribute to our IRA or build up our son's college fund. How would you work with us?"

"If they tell you exactly what you should do, such as directing you to put it all in a brokerage account rather than present you with different options, that's a red flag [in that first meeting]," McNary warned.

So heed the hard-earned lessons of these celebs, and take control of your finances — regardless of how many digits make up your net worth.

Read more: http://www.gobankingrates.com/personal-finance/5-ways-katy-perry-rihanna-botched-finances