Set Priorities for Spending

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When Your Income Drops

A reduction or loss of income usually forces a family to alter its spending patterns. While this is painful at best, the pain can be minimized if family members communicate openly and if the family works out and follows a spending plan.

When dollars are scarce, their value, in effect, grows. No longer can the family afford to "waste" money on luxurious, frivolous, or unnecessary items. The "opportunity cost" in terms of necessary goods the family could have purchased is simply too high. It is important, then, that family members try to reach agreement as to which goods and services are high priority, which less important and which can be postponed or replaced by less expensive substitutes until the financial picture improves.

If your family does not follow a spending plan, this is the time to start. A spending plan is like a roadmap. It tells you where you are now, where you have been and how to proceed toward your desired destination.

Creating a spending plan is not difficult. Major requirements include income and spending records, a knowledge of family spending goals and priorities, and a certain amount of patience and discipline to get the plan started and see it through. Financial counselors point out that the most difficult and time-consuming step in any financial activity is the first one—getting started. Once underway, chances are any required record-keeping will only take about an hour a week. This may be less time than you spend watching television reruns—and in all probability, the payoff will be higher!

The first step in creating a spending plan is to calculate how much income your family will have to work with over the coming year. Also important is when the income will become available. On a record sheet labeled "Income" list all expected income for each month of the year. Include any expected earned income of all family members. When income is uncertain, it is a good idea to err on the conservative side in your estimates. You may wish to make a few different projections of expected income—low, medium, and high. To be safe, though, gear your spending plan to the "worst case" estimate.

Along with earned income, list expected income from unemployment compensation insurance if you are eligible. In Indiana in July 1986, for example, unemployment benefits ranged from $96 to $161 per week for a maximum of 26 weeks.

Other possible sources of income include Aid to Families with Dependent Children, child support payments from an absent or divorced spouse, union benefits or severance pay, food stamps, general assistance and social security.

Also list any "unearned" income from stocks, bonds, or real estate.

Once all projected income for the year is listed in black and white, calculate your average monthly income (divide the total by 12). This average amount will provide the upper limit for your family's average monthly expenses. Remember—it is better to plan on the basis of a low estimate. Do this even if you feel your income reduction is only temporary.

To see if your family is operating within its available income or how spending patterns could be improved, you need to take a serious look at expenses. Expenses divide into those that are fixed, at least in the short term, and those that are variable or flexible.

Fixed expenses include all those for which your family is obligated to pay a set amount. Fixed expenses may be monthly: mortgage or rent payments, base utility charges, payroll deductions for retirement, health, or life insurance, etc.
example. Or fixed expenses may come due annually or semi-annually—perhaps in the form of real estate taxes or an insurance premium due every 6 months. Also included under fixed expenses are any debts for installment, consumer or auto loans, or on charge cards.

List all fixed expenses for the year under the month they come due. For large semi-annual expenses, such as insurance premiums, it may work best to total them for the year, then calculate an average monthly amount which is then listed under monthly fixed expenses. This helps you set aside enough to cover the bulky payments as they come due.

If your family has lost a major source of income you may quickly discover you don’t have enough projected income to cover your current fixed obligations, or to pay necessary living expenses. If this is the case, some difficult decisions must be made. These are discussed in the next section.

Once fixed expenses are listed, flexible expenses are the next concern. These are trickier to estimate and to control. If your family has no clear idea where the money is going, a little detective work and a lot of communication will pay off. Look back through checkbooks, receipts or charge account records for amounts spent on food, clothing, long-distance telephone calls, entertainment, personal care items and household supplies. Begin cutting back and keeping track of outgoing dollars. Give each family member a small spiral notebook for daily expenses, or find a shoe box or spindle to keep labeled receipts.

When your family begins to see how money was and is being spent, it is time for a family conference. Lay out the records of anticipated monthly income and scaled-down expenses for all family members to see and evaluate. Subtract expenses from income: Is the remainder positive or negative after all monthly fixed and flexible expenses are subtracted from monthly income? Do you have savings that can be used to meet expenses in an emergency? Are some expenses out of line with family priorities or expected income? Where can cuts be made so they cause the least sacrifice in family welfare?

It’s easier to see the general pattern of spending if expenses are categorized. This reveals the percentage of income spent on food, housing, clothing, medical care, insurance, and other items. There can be no hard-and-fast rules for family spending because individual needs, tastes and economic circumstances are so important. Examining spending by
category does highlight potential differences between a family’s stated goals and priorities and its actual spending patterns and income.

If these differences are significant, the family needs to reach agreement on a plan for changing the way income is allocated.

If a family is operating “in the red” month after month, a couple of things must happen: expenses must be reduced, income must rise, or both. Spending records and a spending plan provide a roadmap for how this can be done. For some ways to save on various types of expenses, see Part 8 in this series. For help in finding a job and other community resources for economic hardship, see Part 3, “Your Community Resources.” For help in planning to pay bills, see Part 5 in this series.

Suggested Resource


References


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