

Consumer and Family Sciences

Department of Consumer Sciences & Retailing



When Your Income Drops: Fact Sheet 5

Set Priorities for Spending

If you or your family are faced with a reduction or loss of income, you'll need to develop a plan to help you meet your expenses. When they occur, many people try to hide financial problems from themselves or other household members. Not facing problems can be very destructive, because the worry and stress caused by financial uncertainty and lack of cash may be worse than the financial problem itself. It's important to look realistically at the situation and actively seek solutions to your problems, despite the discomfort it brings.

The publications in this series were adapted by Purdue Extension specialists based on subject matter from a publication by Carol S. Kramer, Extension specialist, consumer economics, Kansas State University, Manhattan, Kansas.

Because spending decisions affect everyone who lives in your household, it is important to communicate openly with them about the situation. Let them know everyone needs to change his or her spending patterns. Involve everyone in deciding spending priorities. If others understand the tough choices that must be made and have a voice in making the decisions, they will be more willing to accept the decisions.

As members of your household talk about what is most important, be sure to listen to what they say. Supporting each other can help you pull together and get through these tough times.

How others handle reduced income

Studies show that individuals and families respond to reduced income by cutting their spending. Spending for nonessentials such as vacation, eating out, recreation, and home furnishings are eliminated first. If the financial situation does not improve, many people report reducing spending for basic needs including food, shelter, transportation, and medical care.

When dollars are scarce, people say they revise their budgets. Most make a new spending plan that includes a new strategy for getting bills paid. Some people report increasing their income or using more credit to manage finances. Borrowing or using credit to pay bills brings only temporary relief. In studies of financial stress, those who increased their use of credit were more unhappy with their financial situation the more they borrowed. Those who quickly made changes in their spending habits were the most satisfied with how they were managing. Those who didn't make changes felt more out of control and more dissatisfied.

Making a spending plan

Creating a spending plan is not difficult. The major requirements are income and spending records, 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 you have begun, chances are any

Worksheet 1 — Monthly Income

Wages	_____
Wages of other family members (if used to pay expenses)	_____
Child support	_____
Unemployment benefits	_____
TANF	_____
Union benefits	_____
Severance pay	_____
Food stamps	_____
Veterans benefits	_____
Social Security	_____
Unearned income (stocks, bonds, real estate)	_____
Total income	_____

required record keeping will take only an hour a week or less. This probably is less time than you spend watching television, and the payoff is likely to be higher.

Worksheet 1 above, “Monthly Income,” can help you set up a spending plan for your current income. By comparing your income and planned expenses, you can see what changes are needed. The first step in creating a spending plan is to calculate how much income you will have to work with over the coming year. It is important to know when income will become available as well as how much. Add up your current income from all sources. Include income from other members of your household if used for shared expenses. Use the take-home amount, which is what you actually have to spend after payroll deductions. 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” scenario.

Along with earned income, list expected income from unemployment compensation insurance if you are eligible. In Indiana, for example, unemployment benefits range up to \$390 per week for a maximum of 26 weeks. Other possible sources of income include TANF

(Temporary Assistance for Needy Families), child support payments from an absent or divorced spouse, union benefits or severance pay, food stamps, veterans benefits, and Social Security. Also, list any “unearned” income from stocks, bonds, or real estate. Once you have listed all projected income for the year, calculate your average monthly income (divide the annual total by 12). This average amount will provide the upper limit for your household’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 household is operating within its available income or how spending patterns could be changed, you need to take a serious look at expenses. Use Worksheet 2 on the next page, “Expenses,” to compile your list. Expenses can be divided into those that are fixed, at least in the short term, and those that are flexible.

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

Once you have listed fixed expenses, move on to flexible expenses. These are trickier to estimate and to control. If you had a spending plan before your income was reduced, you probably know how much you were spending for monthly expenses. If not, a little detective work may be needed. Look back through checkbooks, receipts, or charge account records for amounts

spent on food, clothing, telephone, entertainment, personal care items, and household supplies. As you begin cutting back and keeping track of outgoing dollars, give each family member a small spiral notebook to record daily expenses, or find a coffee can, shoe box, or spindle for storing labeled receipts. As you think about how you were spending, and try to plan how much you can now spend, think about these questions:

- Which expenses are essential to the family's well-being?
- Which expenses have the highest priority?
- Which areas can be reduced to keep family spending within its income?
- How much can you afford to spend in each category?

When the members of your household begin to see how money was and is being spent, it is time for a conference. Lay out the records of anticipated monthly income and 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?

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 household spending because individual needs,

tastes, and economic circumstances are so important. However, examining spending by each category does highlight potential differences between stated goals and priorities and actual spending patterns and income.

If the household is operating "in the red" month after month, a couple of things should happen: You must reduce expenses, increase your income, or achieve a combination of both. Do you have savings that can be used to meet expenses in an emergency? Are there assets you

Worksheet 2 — Expenses

Fixed expenses – actual

Rent/Mortgage	_____
Payroll retirement deductions	_____
Contributions	_____
Child care	_____
Debt repayment	_____
Debt repayment	_____
Allowance for self	_____
Allowance(s) for others	_____
Car payment	_____
Savings	_____
Set aside for occasional expenses	_____

Fixed expenses total

Flexible expenses – actual

Food at home	_____
Personal care	_____
Telephone	_____
Clothing	_____
Medicine	_____
Gas/Bus	_____
Laundry/Dry cleaning	_____
Household supplies/Home care	_____
Food away from home	_____
Entertainment	_____
Other	_____

Flexible expenses total

Total fixed expenses (above)+ _____

Total expenses _____

could sell to cover expenses? What are the possibilities for part-time or temporary work to supplement your income? Are some expenses out of line with stated priorities or expected income? Where can cuts be made so they cause the least sacrifice in household well-being?

If much of your income goes to fixed expenses such as housing or debt payments, there may not be enough money left to cover your other living expenses. You may need to refinance your loans, move to lower-cost housing, or surrender your property to your creditor to get out of debt.

The publications in this series

- 1) Don't Panic – Take Control (CFS-704-1-W)
www.ces.purdue.edu/extmedia/CFS/CFS-704-1-W.pdf
- 2) Control Stress (CFS-704-2-W)
www.ces.purdue.edu/extmedia/CFS/CFS-704-2-W.pdf
- 3) Take Stock of Family Resources (CFS-704-3-W) www.ces.purdue.edu/extmedia/CFS/CFS-704-3-W.pdf
- 4) Take Stock of Community Resources (CFS-704-4-W) www.ces.purdue.edu/extmedia/CFS/CFS-704-4-W.pdf
- 5) Set Priorities for Spending (CFS-704-5-W)
www.ces.purdue.edu/extmedia/CFS/CFS-704-5-W.pdf
- 6) Plan to Pay Creditors and Protect Family Welfare (CFS-704-6-W) www.ces.purdue.edu/extmedia/CFS/CFS-704-6-W.pdf
- 7) Keep a Roof Overhead (CFS-704-7-W)
www.ces.purdue.edu/extmedia/CFS/CFS-704-7-W.pdf
- 8) Meeting Insurance Needs (CFS-704-8-W)
www.ces.purdue.edu/extmedia/CFS/CFS-704-8-W.pdf
- 9) Sharpen Your Survival Skills (CFS-704-9-W)
www.ces.purdue.edu/extmedia/CFS/CFS-704-9-W.pdf

PURDUE EXTENSION

Revised 01/08

It is the policy of the Purdue University Cooperative Extension Service that all persons have equal opportunity and access to its educational programs, services, activities, and facilities without regard to race, religion, color, sex, age, national origin or ancestry, marital status, parental status, sexual orientation, disability or status as a veteran. Purdue University is an Affirmative Action institution. This material may be available in alternative formats.