Family Financial Obligations: the undiscussed budget issue

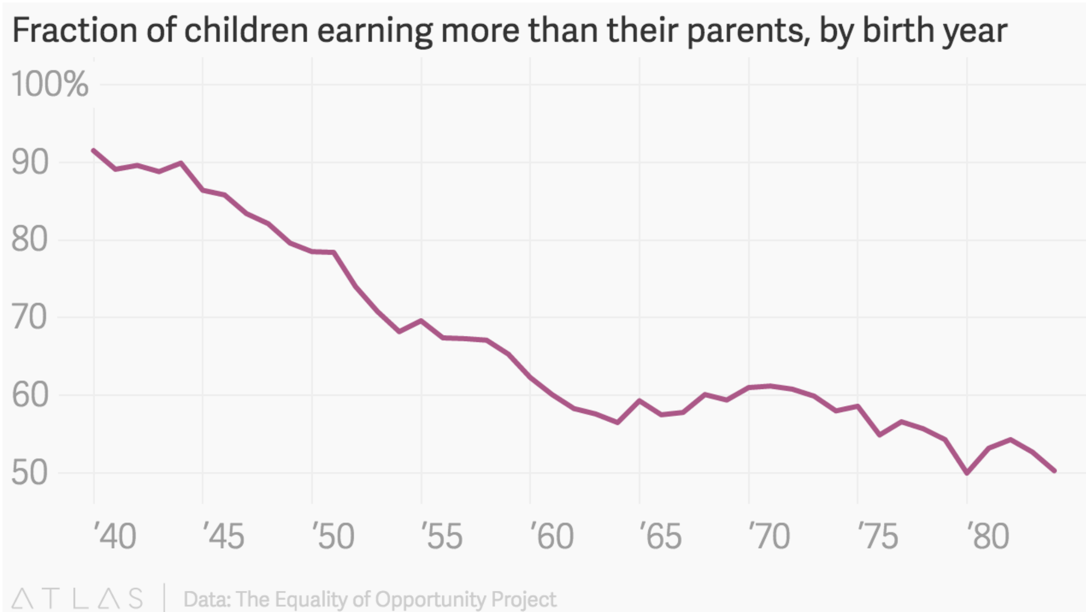
Most of us tend to manage our finances in the context of our direct family need – usually two partners/spouses and some number of kids. Likely, there is no real cash flow analyses or inventory of expenses – or even a realistic and comprehensive budget, for that matter. The focus is on just basic survival expenses without consideration of long-range planning strategies before you decide to buy that expensive car like your neighbor's. Typically, we save money where it's the most convenient and discussed in the media the most frequently – usually a 401k at work, where contributions come out of your paycheck.

Your cash flow looks something like this:

Income from work – basic personal expenses – basic savings = net income before taxes

Income shifts by generation

Most of us grew up in areas where our parents always expected us to earn more income than they did. In fact, according to research from the Equality of Opportunity Project, led by Stanford economist Raj Chetty, 91.5% of 30-year-olds in 1970 earned more than their parents did at the same age, adjusted for inflation. It's not an uncommon sentiment to want your child to earn more and "do better" than you did. And since this is true more often than not, it has led to a whole host of sociological trends that I see every day in my practice. Except for the Gen-Xers, who typically make more money than their parents (Baby Boomers), there has been a downward shift in income, so this is not the case anymore. The millennial generation does not, as a rule, out-earn their parents.



Source: https://www.theatlas.com/charts/ByZA8BP7x

Consider these three examples in which either the child or parents must consider giving or receiving an additional income flow from within the family.

Scenario 1:
In cultures where there's typically a strong family unit, the kids feel a family obligation to send money home to their parents or siblings to make sure that they have enough to cover everyday expenses. I typically see this in more cultural markets or when parents have a low socioeconomic status.

Scenario 2:
Another trend I often see occurs in more affluent families. The minute they get their kids off to college, there's rarely any monetary support needed or required. That is, until an extended care event.

Daughter is earning $250K in her VP position at XYZ Fortune 500 Company and gets word that her mom had a stroke. Her parents have modest retirement accounts and very low non-investment income, outside of Social Security. The cost to take care of mom is $4000/month. Dad will use up most of their assets if he continues to pay for the care Mom needs and doesn't have the physical or emotional energy to provide it himself for years on end. Because the daughter doesn't want her mom living in an assisted care facility, she helps pay for in-home care. She is choosing to cover an extra 48K per year out of her own income and assets. Initially, Dad doesn't want to accept financial help from his daughter, so it's critical the conversation is positioned just right.

Scenario 3:
Millennial son graduates from ABC Ivy League College with a degree in Public Policy and $200K of student loan debt. He is not able to immediately monetize his degree and comes back to Atlanta to live in his parents' basement. His parents offer to pay for some basic necessities.

Now the income shift has reversed and the parents are supporting the child again. This additional outflow of cash could potentially postpone retirement or have other impacts on mom and dad's cashflow statement.

All three of these scenarios should make you emotionally cringe because they all require uncomfortable financial conversations within the respective families. While no one is "obligated" to help fund their family's lifestyle or solve their financial problems, there's an unspoken moral obligation that may require people to contribute. Doing nothing and letting your parents or kids figure it out is certainly a valid choice, but many times people want to help. In any of the above examples, your own moral framework needs to be your guide in determining whether or not you wish to "help out."

Why does this matter?

One of the key pieces of my financial planning process is to get a copy of the client's living expenses. To clarify, I don't do budgets, but I do need to understand the cost of the current lifestyle clearly. Therefore, when I model for a future event – retirement, paying for college, etc. – I know what it will truly cost. But when the topic of whether your parents have enough assets (or insurance) to pay for an extended care event comes up, the answer is inevitably, "I don't know." And usually, clients aren't excited to go talk to their parents about their personal cash flow. The same is true for conversations with their millennial children regarding their job aspirations and income flow, so you know their potential additional monthly cash requirements.

Have the conversation

It's really important, in the context of your financial plan, that you know if family members will need financial help at some point. By not talking about it, you are limiting your ability to effectively plan. Those additional expected or unexpected expenses need to be accounted for, so you aren't caught by surprise and forced to make a large financial mistake, like liquidating a 401(k) plan before 59 ½, so that you can help your family.

I encourage all of my clients to have an annual family meeting. While no one wants to talk about death and taxes, that family meeting should go over the estate planning documents and what everyone's intents are around financial planning in life, upon death and in case of a major healthcare event.

Surprises are for birthdays, not for money.

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