WHAT SHOULD I DO WHEN MY INCOME TIGHTENS, BUT EXPENSES REMAIN THE SAME?

By: Shelly Arnold, Senior Vice President, Private Banking Team Leader

You may be hesitant to talk about your financial situation with family and friends, especially if you have concerns about your current financial status. You've worked hard to build your career and reputation to provide a certain lifestyle for your family. You've grown accustomed to the personal comforts your wealth affords—as well as status in your community and access to the best business and social circles. No one, perhaps even your spouse, suspects you're having these feelings—and you prefer to keep it that way.

So far, you've managed to keep up with your expenses. But you're quietly grappling with the fact that your obligations are beginning to pile up. Maybe it's a just a matter of better managing your cash flow to address current payment schedules. Perhaps it's a bigger issue brought on by a major event such as a downturn in the economy and the impact on your business.

Whatever the reason your finances are off track, you're beginning to wonder how to meet your current and future obligations.

TAKE THE FIRST STEP.

First, you have to diagnose a problem before you can fix it. Answer these three questions:

"How did this happen?" As mentioned above, often cash flow issues are brought on by an event's bad timing combined with the snowball effect of large payments, such as tuition, unexpected repairs or club dues, coming due. There are many other events besides an economic downturn that can trigger a cash flow problem: a job layoff or furlough, a natural disaster, bad investments, business interruption, or an unexpected and costly family or legal situation.

"Is your financial situation a temporary or long-term issue?" If you need to have a long-term plan, think about the risks or downsides to possible solutions and how you are going to track your progress.

"What are my options?" Your answers not only help you understand your financial dilemma but also help you determine the best solution for your situation. Consider the following suggestions in your decision-making process.

TRY TO KEEP YOUR OVERALL WEALTH STRATEGY INTACT.

Without proper planning and financial resources in place for an emergency, your first thought might be to liquidate investments that are allocated for other purposes like retirement or an upcoming purchase. But this could disrupt your investment plan and have significant tax ramifications.[1] For example, if you take a non-qualified distribution from your retirement account prior to retirement, those assets could be subject to tax penalties. It might be better to keep your overall wealth strategy intact by keeping those assets invested to achieve your previously defined objectives.

Investors should consider keeping their emergency fund separate from cash in their investment portfolio. Cash in your investment portfolio can be used to take advantage of new opportunities without having to sell in a down market or potentially create a taxable event.

If you're a business owner or your income is dependent on bonus or incentive compensation, you may want to consider larger emergency fund savings or liquid allocation in your portfolio. If your cash flow varies throughout the year, you have to be much more thoughtful about planning for—and budgeting—your expenses.

CONSIDER YOUR PERSONAL BORROWING OPTIONS.

Before you begin the borrowing process to help you manage the expenses, check out your credit score and payment history. Take advantage of your annual free credit report to avoid any surprises when applying for credit. Your credit score, debt to income ratio and available collateral are key to an effective and efficient liquidity plan.

Home Equity Loan / Home Equity Line of Credit (HELOC): If you have equity built up in your home, a home equity loan or HELOC is an attractive borrowing option that may offer tax benefits.[1] With a home equity loan, you can borrow against the value of your home, less any current mortgages. HELOCs operate much the same way. They are lending arrangements secured by the equity in your home, typically featuring lower interest rates. However, just like a credit card, you only pay interest on the money you borrow, and you can advance or repay the loan up to the predetermined credit limit.

Cash Out Refinance: With interest rates at historically low levels, another borrowing option is to refinance your primary residence or vacation home. This allows you to take advantage of a lower borrowing rate and pull excess liquidity out of your home to be used for another purpose. These funds can be used to support cash flow needs or for investment opportunities.

Securities-Based Line of Credit[2]: Borrowing against the value of your investment portfolio is another common and flexible borrowing option. Similar to a HELOC, the variable interest rate is typically tied to a percentage of the current Prime lending rate. The borrowing limit is set to a specific percentage of account value usually around 50% or 60% loan-to-value (LTV).

You should use extra caution with this borrowing option when market activity is volatile. Should the borrowed amount exceed the LTV limit, the lender will likely take the required steps to bring the account in compliance, including liquidation of securities to pay down or pay off the balance. However, this can be an attractive option because it allows investors to remain invested while borrowing when necessary.

Credit Cards: Occasionally, credit card companies offer no fees on balance transfers and 0% APR for a promotional period. If your current credit card debt carries a high interest rate, transferring the balance onto a card with these terms could be beneficial. If you don't have credit card debt and need short-term help, a 0% APR card could be a good solution; however, be extra diligent about making timely payments and paying off the balance before the promotional period ends.

SHARING YOUR FEARS AND CONCERNS IS KEY TO FINDING SOLUTIONS.

Deciding how to handle your unique financial circumstance depends on several factors. This is an important decision that should be weighed carefully in the context of your total financial profile. That's why it's important to get objective advice from someone who is knowledgeable, discreet and will hold your concerns in confidence.

With our team of professionals at Commerce Trust Company, you can feel comfortable bringing up topics ranging from cash flow management and payment scheduling to having access to your wealth in an emergency. You can feel safe asking for financial advice regarding sensitive family matters.

Don't let fear and emotion cloud your judgment. Contact us today for a candid, unbiased perspective—we will listen to your concerns, answer all your questions, and empower you to make educated financial decisions to help get your finances back on track to maintain your lifestyle.

1 Consult your tax advisor.

2 Securities-based borrowing exposes the borrower to some risks. If the value of the underlying investments decreases sharply, the borrower may need to expedite repayment or sell investments to meet the terms of the agreement. Selling investment securities may result in adverse tax obligations.

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Shelly is a relationship manager team leader with Commerce Trust Company. As a member of the private client team and an experienced, tenured private banker, she and her dedicated client support staff are responsible for ensuring each client's experience with Commerce Trust exceeds expectations. Shelly's specific responsibilities include management of our clients' day-to-day banking, cash management, and credit needs, while also helping them navigate the wide array of our financial services to find the solutions that best fit their needs. Shelly has more than 30 years of experience in the financial industry. Shelly attended the University of Missouri – St. Louis where she studied business administration. Shelly has been active in many child advocacy organizations such as Girls, Inc. and Kids in the Middle.