TheStreet.com

Even High-Income People Overspend

Financial planners have to fight 'lifestyle inflation' to keep well-paid clients on track.

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Updated Nov 11, 2018 10:00 AM EST Original: Nov 10, 2018

More Americans are living beyond their means than ever before, including those pulling down six-figure paychecks. Household debt in the U.S. hit a record $13.3 trillion in the second quarter. Of those earning $150,000 or more, nearly 30 percent have less than $1,000 saved, a 2016 GoBankingRates survey found.

Increasingly, financial planners find themselves on the front lines in the battle to get doctors, lawyers and other well-paid professionals to spend less, save more and live financially sound lives. That can mean working with clients to break bad spending habits and to rein in and pay off high-cost debt like credit cards. Some planners espouse a "tough-love" approach, which can sometimes even lead to "firing" a client who refuses to get with the program.

"Bad debt is a destroyer of wealth," says James White, founder of J.H. White Financial and a certified financial planner in Pottstown, Penn. "It has a domino effect on your cash flow. It takes away from the positive savings side of cash-flow. Less in your emergency fund, less in your retirement savings, less for the necessary living expenses."

How should financial planners respond? Let's check it out:

Step 1: Target spending

Bad spending habits are a major factor when it comes to the shaky finances of many Americans, including high-income professionals, planners say.

Simply earning, getting a raise, or climbing the income ladder can be futile if there is no attempt to curb spending, with expenses rising right alongside income, a phenomenon known as "lifestyle inflation," notes Kristin McFarland, a wealth advisor at Darrow Wealth Management and a certified financial planner, or CFP.

"Lifestyle inflation can get individuals at any income level into spending trouble," McFarland says, adding it "can be particularly damaging when fixed expenses are involved, such as a home."

Not surprisingly, planners say a big step towards getting clients onto a healthier financial track involves identifying bad spending habits and curbing them.

When faced with a client with a major spending problem, McFarland will run an analysis detailing just how all that extra spending is hurting efforts to achieve specific goals, such as hopes of being able to retire at a particular date.

Alexander Koury, a wealth advisor for Values Quest in Phoenix, notes he is working with a medical professional who spends almost all of his nearly half a million dollar income each year. On top of that, he has $900,000 in student loan and mortgage debt.

Koury, a CFP, has helped his client set up a savings plan and consolidate various loans at lower interest rates, but spending remains a problem.

"What troubles me most is people mistake income for wealth, and they spend every dollar and beyond in some cases," Koury said.

But it is not always just the big-ticket items that get clients into trouble.

White, the CFP from Pennsylvania, points out that while grabbing a cup of coffee or eating lunch out may not seem like budget busters, all these seemingly minor, routine purchases add up.

"Lunch or coffee every day, online orders, the small purchases that when viewed individually do not look like much but viewed in aggregate monthly add up to too much spending," White says.

Step 2: Pay Down Credit-Card Debt

Generally, credit-card debt is considered a higher priority to pay off than mortgage debt due to the higher interest rates this type of debt carries, planners say.

Rates on credit cards can run in the 15% to 25% range, with card companies targeting consumers who will keep a running balance and not pay down their debt, notes Byrke Sestok, president of Rightirement Wealth Partners in White Plains, NY. By contrast, mortgage debt can be refinanced.

"Credit-card debt concerns me far more than mortgage debt," says Sestok, adding, "credit-card debt is usually a result of spending more than one makes and that's a behavioral issue."

White tells clients they should only use a credit card when they can turn around and immediately pay it off. If you can't do that, then don't use a credit card, he says.

"I hear the excuse well it was unexpected," White says. "My reply is: 'That is what an emergency fund is for. It prevents the use of bad debt.'"

But mortgage debt doesn't get a free pass either in White's book, particularly if a client is planning to carry a mortgage into retirement.

White asks clients whether they really want to use their "hard earned savings" to make mortgage payments during their golden years.

As an alternative, it might be better off moving to a smaller house and getting rid of the mortgage, White suggests.

"A mortgage is a concern if they are going to be carrying it into retirement," White says.

Step 3: Tough Love for Spenders

Sometimes more drastic measures are needed, planners say

David Demming, president of Demming Financial Services Corp. in Aurora, Ohio, and a CFP, cites the case of a wealthy family who got into trouble loading up on houses and cars and spending on their children.

Demming consolidated their mortgage into a 10-year, fixed-rate loan at 3% and expanded their secured and unsecured lines of credit to pay off their credit-card debt.

"We have invoked the wrath of God to not add other debt until progress on [paying down the unsecured credit lines] occurs," Demming notes.

Ian Weinberg, chief executive officer of Family Wealth & Pension Management LLC in Woodbury, N.Y., says overspending is an even more serious concern once clients hit retirement.

He urges clients who have a fixed amount of money saved up for retirement to adjust to a "lighter standard of living" to protect against the steady creep of inflation and unforeseen costs and expenses.

If clients aren't serious about adjusting their expenses to a realistic level, Weinberg isn't shy about what he believes is the appropriate next step.

"Clients who have retired with a finite amount of critical capital that spend recklessly and haven't listened to our advice about adjusting their expenses in retirement keep us up at night," Weinberg says.

If we can't help them acquiesce to a lighter standard of living ... then we tell them we can't work with them," Weinberg says. "We don't want to be a party to their ultimate destruction of their finances."