



FINANCIAL PLANNING

Half are living on the financial edge

By ALI JAFFER

As the year-end approaches, many Canadians are gearing up for holiday spending and finding the means to pay for the many expenses they will be incurring. On a day-to-day basis, Canadians are struggling to meet the daily needs for their family and are looking for various options to achieve their financial freedom.

A recent survey conducted by the Canadian Payroll Association concluded that nearly half of all Canadians are living paycheck to paycheck. This means if there was a change in interest rates, job loss, severe illness or other life-changing event, many of those Canadians would be in severe financial difficulty.

Furthermore, at the beginning of 2016, Statistics Canada reported that the average Canadian had more than \$21,000 in debt. An ineffective financial strategy will result in the accumulation of lines of credit debt, credit card debt and the buildup of personal loans. This will be even more significant in the event that a paycheck is delayed or large one-time expenses are incurred. This snowballing effect could result in the inability to even afford minimum payments on debt.

In order to determine the impacts of various factors on the paycheck-to-paycheck syndrome, an examination of these issues must be made. Some of these factors are economic, such as interest rate fluctuations, inflation and real estate trends, which are out of an individual's control. There are also personal factors, such as social pressures, improper budgeting and the inability to control impulse purchasing.

Interest rates

The Bank of Canada has hinted that interest rates may be rising. The rise in debt levels can be "blamed" on low interest rates that make it very attractive to borrow at 2 per cent. If the Bank of Canada were to increase interest rates by a quarter of a per cent, it would cause serious cash-flow issues for Canadians living paycheck to paycheck.

For example, on a \$400,000 mortgage that small rise in lending rates would result in about a \$100 extra monthly expense, putting several thousand people at risk of defaulting on their mortgages. The flipside of the interest rate debate is there is no incentive to save as money on short-term investments does not earn anything like it used to.

Inflation

Rising costs of essential day-to-day needs or significant infla-



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tion would cause many Canadians to be in a severe financial situation. Most affected families are sensitive to rising prices given that they have stretched themselves on day-to-day living and they lack of emergency funds.

Real estate market

A common message often heard is "if I sell my home, where do I go?"

First, if a family cannot afford to own a home, they should not be buying in the first place. With the exceptionally high real estate market, especially in B.C. and Ontario, Canadians should explore the option of either downsizing, buying a smaller home as first-time home buyers or, perhaps, even renting. Typically, household budgets should be between 30-35 per cent of overall expenses.

If these expenses are higher than this threshold, it may be time to look at other options. Studies have shown that renting a home is cheaper in the long run. These savings can then be directed toward other forms of investing such as stocks, bonds or mutual funds.

Social circles

It is very common for families to feel obliged to commit to dinners, movies or vacations due to the social circles that they are a part of. Always saying "yes" to these gatherings and keeping up



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with the Joneses can lead to the paycheck-to-paycheck syndrome or, even worse, dipping into lines of credit or credit card debt.

Sticking to an entertainment budget is critical in these situations by learning to say "no."

Calendar holidays

Every season has occasions where the consumer is bombarded with marketing to purchase gifts, decorations and attend or prepare for dinners. The key is for families to budget and set a limit as to how much they will spend on each of these occasions.

Here are some solutions to assist with the paycheck-to-paycheck dilemma.

Savings

A simple savings strategy such as putting away \$50 to \$100 every month in a savings account or a TFSA (tax free savings account) will go a long way toward preparing for retirement or establishing emergency cash flows. These savings have many advantages including compound growth, which is tax-free growth if invested within a TFSA. Savings can also provide an emergency fund in the event of a job loss. Some experts have often used a 10 per cent of earnings saved threshold as a guide.

Cash flow planning

The preparation of a cash-flow budget for the year will ensure that the current expenses are being controlled and managed. The first step in this process is developing a system to track expenses. A number of apps, websites and bank tools are available to help manage monthly expenses. The budget must be reasonable, with all expense items listed by category.

Living within a budget

With rapid advances in technology resulting in new products and gadgets being introduced to the market daily, individuals need to be selective in choosing which new gadgets or fads they want to purchase. Having control of these purchases will go a long way toward managing a family budget.

For day-to-day expenses,

various coupon sites and apps can lead to significant savings. For other non-essential purchases, there are discounted vacation websites that will allow for families to plan their vacations within a reasonable budget. Tracking expenses, cutting unnecessary spending and planning annual expenses will help prevent the living paycheck-to-paycheck dilemma.

Tax planning

Sometimes cutting expenses or increasing income are not options for families. However, a taxpayer can request the employers' payroll department change the withholdings for individuals who typically receive refunds. This will allow for larger cash flows throughout the year rather than a large refund during tax filing time.

Opening up a small business in addition to full-time employment will allow certain tax deductions that are normally not available. Seeking assistance of a professional tax preparer can also assist in capturing some commonly omitted tax credits or deductions.

Enhancing financial education

Various government programs are available to help people with their cash-flow planning. These include government loans for small-business owners, tax return preparation clinics or general courses on cash-flow planning.

Financial planners, advisers and accountants can also play a key role in developing statements of net worth, budgets and, most of important of all, adding value to their clients by ensuring they are spending only what they can afford.

The key to solving the paycheck-to-paycheck dilemma is to start financial planning as soon as a full-time job is landed. Ensuring that three to six months of an income safety net is kept aside and not relying on the uncontrollable external economic factors are essential to meeting your financial needs.

Whether someone can save \$50 per month or only a few dollars per month, all these savings eventually add up. As long as families are able to control what they are able to control, this common syndrome will never become an issue, allowing families to seek their financial freedom.

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