Real World Financial Management Tools and Practices

The purpose of this research is to discover techniques used by families in the day-to-day management of their finances. This study uses a case study of seven average American families to explore their normal routines. The information fills a gap in the existing research. The study found managers have a system and that common practices existed including extensive use of mental processing, routines, visual clues, multiple accounts, and a short-term focus.

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Introduction

The financial management practices of individuals and families interest financial planners. Questions regarding the long term preparedness, growth in net worth, retirement planning, and use of recommended financial practices among today's families are common research questions. With increases in personal bankruptcies and a decrease in the savings rate, concern arises over the family's financial well-being. This suggests financial managers need money management skills more than ever. Existing research has shown the recommended management practices are not used but has left educators and practitioners with little knowledge of what people actually do. Such information is crucial if educators are to help individuals and families prepare for today's increased financial pressures and complicated financial matters (Godwin, 1990a, 1990b; Lown, 1986; Winter, 1986b).

The purpose of this article is to discover techniques used by families in the day-to-day management of their finances. This study uses a qualitative approach for data gathering. Qualitative methodology explores what people actually do. Questions are open-ended and probing with each question stemming from an earlier response.

The Setting

Godwin (1990b) defined family financial management as "the planning, implementation, and evaluating by family members that is involved in the allocation of their current flow of income and their stock of wealth toward the end of meeting the family's implicit or explicit financial goals" (p. 103). From the normative perspective, financial management includes: regular generation of financial statements; budgeting; control of spending; recording income and expenses; and tax, insurance, investment, retirement and estate planning (Garman & Forgue, 1997; Rettig & Mortenson, 1986). The purpose is to enhance the well-being of families. However, these same studies indicate that few families use the recommended practices (Beutler & Mason, 1987; Davis and Carr, 1992; Godwin, 1990b; Godwin & Carroll, 1986; Hira, 1987; Titus, Fanslow, & Hira, 1989).

There is no argument that the American family manages its financial affairs. Winter (1986a) notes that families are managing and offers proof by observing families have "food on the table,...clothes on their backs,...and [the] utility bills [are] paid on time" (p. 145) and that they, for the vast majority, avoid serious trouble such as bankruptcy, problems with creditors, etc. The question is what are families doing?

Some clues exist in family life case studies, such as that of Rainwater, Coleman and Handel (1959) who commented about the "tin can" economy. Money for each budget item is placed in tin cans. Money is then withdrawn for each purchase. When the tin can is empty, no more purchases for that item are made until the can is refilled. Other qualitative works offer scattered bits and pieces of information (e.g., Hochschild, 1989; Jackson, 1985; Newman, 1988; Rosenblatt, de Mik, Anderson and Johnson, 1985; Rubin, 1976).

The lack of understanding of actual practices caused Davis and Carr (1992) to ask about "the incentives that actually lead people to embrace the recommended process" (p. 14) as have others (Godwin, 1990b; Heck, Winter, & Stafford, 1992). Financial management instructors even recognize that they do not utilized the practices they teach (Godwin; 1990a; Prochaska-Cue, 1993). Lown (1986) wrote, "Do as I say, not as I do" (p. 5). So what are families doing to manage their finances? (Godwin, 1990a, 1990b, 1994; Varcoe, 1990; Winter, 1986a, 1986b)?

Method

Family financial management research has typically relied on quantitative methods. Studies have examined the prescribed list of practices and asked who used one or more of these practices? The results found little

consistent use of these practices. The lack of use has caused researchers to suggest that perhaps a qualitative approach might fill the gap (Godwin, 1990b; Winter, 1986a). Qualitative research allows us to learn about people in the context of their lives, in their natural surroundings, performing their normal routines, and surrounded by their normal social structures and contacts (Bogdan & Biklen, 1992; Denzen & Lincoln, 1994; Guba, 1987, 1990, 1992; Lincoln & Guba, 1985; Miles & Huberman, 1994; Wolcott, 1990). The results are "descriptive" (Bogdan & Biklen, 1992, p. 30) and gathered from "ordinary people with ordinary knowledge" (Spradley, 1979, p. 25).

For this study the intent was to match the American median family as defined by U.S. Census data: a couple related by marriage with both partners age 30 to 40, in a first marriage of eight or more years with one or two children, an income of $40,000 to $60,000 with both the male and female adults employed, and both adults having a BS degree or less (1994 Statistical Abstract, Table 714; U. S. 1990 Census of the Population and Housing-Social, Economic, and Housing Characteristics, Table 5; U. S. 1990 Census of Population-Social and Economic Characteristics, Table 16, 17 & 23).). Families fitting this average were selected and interviewed until "the responses began to become redundant" (Lincoln & Guba, 1985). Seven family money managers became the respondents for the study. All interviews were taped and transcribed interviews. Families were interviewed on a quarterly basis from 1992 through 1995 and were conducted by the same person.

To assist in offering reliable and valid data, the tools of: member/ respondent checking (respondent receive and comment on transcribed material's accuracy, meaning and clarity); peer debriefing; triangulation or supporting findings through multiple means or respondents; meetings with colleagues to discuss findings, reflections, key words and themes; and input from the researcher's major professor plus an additional faculty member were used (Guba, 1981; Guba & Lincoln, 1994; Lincoln & Guba, 1985: Miles & Huberman, 1994).

Introduction to the respondents

Seven families are the source of data for the study. All respondents live in purchased single family dwellings in small towns and cities, populations ranging from 6,000 to 60,000, in the central part of the United States. All of the families have from one to three children; all of the children are living at home.

Angie and Bob

Angie and Bob are both self-employed. They have two small children, a family income of $40,000 per year and little in savings. They are one of two families in the study utilizing a financial advisor's services. The family debts consist of a home mortgage, a vehicle loan, and some credit card debt. Angie and Bob, like the other families, have several credit cards. Although Angie tries "not to have a balance on the cards, I can't say I never have." Angie considers their bills "routine." She feels she knows what she can afford without any tools beyond the check register. She feels fortunate, as "there has rarely been a time where I couldn't buy something," but "I don't go out and buy a filet mignon."

Cindy and Greg

Cindy and Greg have three children. Greg is employed full-time; Cindy part-time "so I can be home with the family." Both have additional part-time jobs. Together their current income is "about $50,000 per year." Cindy and Greg have a "home loan, a car loan, a personal loan, and some credit card debt." About the personal loan Cindy said, "We usually have one of those. We get one paid off and something else will die or, you know how it is." They have three credit cards with two having revolving balances. Cindy said, "I don't know if it is a correct mind set, but I think most people have those." When asked to be a part of the study, Cindy commented, "I don't do what I am supposed to, but I am normal." Cindy feels they are keeping up but are "not saving." Her greatest financial management frustration is that she and Greg only receive a monthly paycheck from their full time jobs. To handle this, Cindy writes all of the checks "first of the month." This offers a financial picture for the month. She pays the credit card bills last giving each an amount she believes she can afford based on "experience."

Gary and Donna

Gary and Donna are in their early 30's with a five-year old daughter. They are both employed full-time. The family's income varies, with Gary on a salary-plus-commission basis, but averages around $60,000 per year. Gary and Donna are the only family to use a computerized financial package. Gary and Donna have a home loan, a personal loan, a vehicle lease, and, quite often, a credit card balance. Debt planning for Gary and Donna is determining if a new payment fits into their income flow. Bill paying cycles around "my [Gary's] commission check on the 10th." The amount paid on any bill depends on how they feel financially. If they do not feel they can pay a bill in full, their procedure is to pay everyone something.

Lorrie and Andy

Lorrie and Andy have two children and a current income of around $50,000 per year. Their debt consists of a house payment, two vehicle loans, and some credit card debt. She wishes they could "pay off some of this debt and not get back into it" but debt is a part of her generation, "We don't live like [our parents did]. We live 'life to the max,' spending most of what we make." Lorrie feels they could save first but "it takes longer. We are going to have it right now." Lorrie feels like they are financially on the edge but "doing okay" as "the bills are paid" and they have "a roof over their heads" but that they are "living from paycheck to paycheck like everyone else." She is more concerned about "making sure ends meet" than net worth. Savings are money "left over."

Nora and Don

Nora and Don both work full time plus Don has a second part-time job. They gross about $50,000 per year. They have three children. Nora questioned, "What could be learned from me?" when asked to be included in the study. Her husband acknowledged that she has a unique system, "Her system is a one of a kind." Don continued, "I know that we should do a budget and stuff" but to him financial management means "doing it by going by your gut." Nora said, "I don't budget," but uses a "tablet" to help track the incoming bills, and "the next two to three paychecks." The family debt consists of a home loan, credit card debt, and a home equity loan for a boat. The home equity loan allows them to "write off the interest" and "spread out the payments" over a 12 year period so they are not "stuck with those high payments." Nora limits their debt based on "guilt" and experience that says, "You get one thing paid off, then you know you can buy something else." Overall, Nora feels "overwhelmed" by their financial situation and that they are "losing ground."

Sam and Gail

Sam and Gail have been married for 20 years, have two children, work full time and gross approximately $50,000. Sam follows few recommended practices commenting, "There is no budget in this house, none whatsoever...I cannot tolerate it. There ain't nothing I have to live by." Sam's planning consists of "I scribble a whole bunch of things and then decide what to do from there." Sam said, "I can make payments but if you ask me to save, it ain't going to happen...If I don't have a car payment due, I am looking for something else to buy." Sam said that management occurs but that people have individual ideas of what management is, "People do plan ahead but we just don't realize we are doing it" or having difficulty accepting them "do[ing] it their own way." Sam and Gail find debt acceptable. Their current debt, a $1000 a month payment, is financed with an "open line of credit using our home equity." They have no other mortgage or consumer loans or any revolving credit card debt. Sam commented that debt levels are "experienced based...We...build to that [level of monthly payments]. I had the history of being able to make them, why can't I continue?"

Sandy and Carl

Sandy and Karl have two children, are both employed (Karl full-time and Sandy part-time), and make about $40,000 per year, an $8000 a year decrease because of Karl's recent job change. While the income drop is significant, Sandy considered it [the job change] "a good choice for the family," as the job is "less stressful," and "left Karl free on the weekends." Sandy said initially the change meant "less recreational shopping...sending smaller payments on my flexible [credit card] bills" and being "more cautious," but "now [I am] back to my old ways." The most significant issue is the uneven checks Karl receives as an hourly worker. Sandy's management philosophy is controlled by: (1) "safety" which she defined as "savings" ($1000 in the bank) and having cash available to pay current bills; and (2) experience "We have managed in the past and can do so again in the future." Sandy does not use a "budget," saying, "People don't have the time to do all of these things [meaning the recommended practices]," and "people don't want to know that they have over-spent." Their debts include a home loan, a home equity loan for an auto, a 22% personal loan for their big screen television and credit card debt.

Results

The purpose of the study is to discover techniques used by families in the day-to-day management of their financial affairs. The understanding of what people are doing is a basic building block for the development of a financial management system that money managers are more likely to use. In this study that understanding begins in three broad areas.

System

Each family manager has a system he or she has developed to take care of their finances. The system or process is formalized, done in a regular manner and on a regular basis. The system is mental, not in writing and focuses on short-term financial stability, "staying current on one's bills" and "not going in the hole."

Each system uses a significant amount of mental processing. Cindy noted having "a mental thing of what am I going to owe this month." Lorrie said, "mentally, I know what all of my bills are." Other references included Cindy's mental adjustments for the unexpected; Angie's "mind games;" Sandy's mental allocation of funds based on feel; respondents' paying bills by "feel;" Nora's "mental adjustments;" and Sam's "thinking about."

The use of mental processing however is quite demanding. To help balance or avoid using all of one's mental resources for financial planning, respondents establish routines. These routines include Nora's selecting an insurance company who will "bill every month;" Lorrie's paying the "same amount every month" on her credit card bills; respondents "spending the same on groceries each week;" and the anticipation that bills are "consistent" each month. Sandy discussed the importance of income consistency, "The most frustrating thing to me is that I'm used to [a situation]...where every paycheck was exactly the same....You could plan for it; [now] you never know." Ease and convenience are factors that also limit the use of mental resources and time. Both appear in bank selection, use of credit cards, automatic overdraft transfers, and Sam's keeping accounts open "[so] I can borrow...in a hurry."

The idea of routines also included the use of automatic bill payments. Nora, Cindy, Angie, Lorrie, and Gary all try to have as many bills as possible paid directly from their checking accounts. While companies working with banks may offer that service, Nora gave an example of other ways it make work. Her dentist "accepted a pad of signed checks...and when [the due]date comes, they just rip it out [the appropriate check] and deposit it."

Tools

Even though family financial managers did not use the recommended practices creating instead their "own" system, these systems showed similarity in the use of certain tools. As might be expected all managers used some form of a checkbook register. Another tool included the use of multiple accounts, checking, savings or a combination, for managing the financial affairs of the family. Multiple accounts help the financial manager physically allocate funds thus avoiding budgetary categories and provide early financial warning signals. Another common tool is the use of visual reminders such as due date "calendars" and leaving unpaid bills in visible sight.

Several respondents use written tools, similar but yet different from those recommended. Lorrie uses a "little piece of paper" and Nora a "tablet." Even Gary's use of Quicken varies significantly from the recommended practices. Even Sam, whose system is the most unstructured, admitted to "scribble[ing] a whole bunch of things and then decide[ing] what to do from there. It doesn't include dollars, though, in detail, just ideas."

Underlying motivators

Three motivators were common among the managers and may offer the greatest understanding into the managers' reasoning. Short term safety is the first. This meant "having the funds available to cover current bills," "provid[ing] protection if funding gets tight" and "avoid[ing] an overdraft." Cindy, as well as Lorrie, Nora, and Angie, use a "false balance" or an additional amount of money that remains in an account even it showed a zero balance. "Then I know I am not going to hopefully overdraw," Cindy said. Other facets of short term safety meant the respondents' understanding and use of the "float" period, the leeway companies allow to receive payments.

Another motivator is current comfort. Lorrie commented that, "We have a different [idea]....People were married a lot longer [in her parents' generation] before they got their things....We don't live like that. We live 'life to the max'....We are going to have it right now." Sam said, "I will enjoy it now" and Sandy noted, "money was for...fun." What the respondents typically bought are wants, debt for "toys" is a perfectly logical thing," said Sam.

Acceptance of debt is a third motivator. All of the respondents openly accepted debt and recognized its significant impact in family financial management efforts. Each family has an acceptable level of debt that "grew" as they "became adjusted to higher levels." Experience told them that debt was best if continuous. "Finish one loan, get another" was common in all of the families. Financial managers commented that if they would ever quit making debt payments the money would just "disappear" and they would get no visible and tangible reward for their efforts. Debt went for home improvements, vehicles, clothing, eating out, gas, emergencies, vacations, etc. It was financed with mortgages, credit cards, constant personal loans, and home equity loans.

Discussion and Implications

So what are families doing? Families are managing and do so in a manner ranging from Sam's "Oh, I think about" and "people do plan ahead, but we just don't realize we are doing it," to Gary's use of Quicken to Sandy's use of a hierarchy of accounts or Nora's belief that "everything will work out, it always has in the past." Management is consistent, formalized, and focused. Families manage for stability, to keep the family out of "the hole," to smooth out the "bumps" and "dips," and to allow families to enjoy today. Management is not however the recommended practices.

Some of the commonalties found included financial managers focused on short term financial viability, defined as "paying our bills" and "keeping a roof over our heads." Internally generated savings were typically very small accounts. Most of the investment and savings that the families had were in company sponsored retirement accounts. Families accepted debt for today's wants of recreational items, modern conveniences, multiple vehicles, and electronic wizardry. Debt allowed the family to "live for today" and provided a means to increase their stock off goods. To handle their system, managers placed limits on the mental and time resources they would use making ease, convenience and routines important. For all of the similarities that existed in the various systems, a large amount of individuality was also noted. Tools were individualized. All managers desire the same end, short term financial viability, but their paths to reach that end differ. Experience plays an important role in each manager's system and its development. Three managers indicated that their earlier system were more formalized and more often in writing. Finally managers wanted to feel normal, that their system is typical of what others were doing.

Understanding what people do is the first step to developing a more accepted set of practices. This set must meet the respondents short term safety goal and the professionals' goal of long term well-being. What are the implications for teaching financial management? First the profession must recognize the focus on short term financial viability or "keeping the bills paid." Second is to accept people's individuality. One size does not seem to fit all. Third, financial management teaching must address the mental processing being done. Fourth, teaching financial management means recognizing the objectives of safety, control and comfort of the financial manager. Systems must offer tools such as those seen: putting unpaid bills in plain sight; jotting due dates on the calendar; and using aids such as automatic payments and developing others such as Goetting's and Ward's check register (1994), having due date stickers included with a bill; having perpetual calendar pages with due dates already marked; or financial calendars that allow dollar amounts of bills to be noted at a glance.

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