

These Expenses Are Ruining Your Financial Plan

Christmas comes every December 25th. You are required to have auto insurance. Every summer your electric bill goes up. Yet the expenses associated with these surprise us....always.

If you find yourself struggling to pay for the expenses that you CAN anticipate then you will always be playing catch up.

I pay my auto insurance every 6 months to get a discount. So when I lived in Florida that bill was \$2,600. Of course every 6 months I was stunned when Geico sent me a bill notifying me I had to cough up the cash.

Even though the bill came like clockwork every 6 months I was never ready and I never had the money available. I would put the bill on my Discover card to delay the pain 30 days, but like an average person I couldn't come up with \$2,600 in one month. So I dug into my Emergency Fund and paid the bill from there.

I quickly realized that I wasn't preparing in advance for these types of payments. When my electric bill spiked during summer I wasn't ready. When I had to buy presents for birthdays, anniversaries, and the holidays I seemed stunned.

Every time one of these "surprise" bills came I went to my Emergency Fund for help. Before long it was clear a cycle had formed. By the time I had paid back my Emergency Fund it was time to use that money towards a new unanticipated yet expected payment.

What can you do though? What options do you have?

Preparing For Expected Expenses

Well I found a way to make sure I had the money for these and even make some money in the process.

I created an "Allocated Funds" savings account and an "Allocated Funds" line in my monthly budget. Now instead of spending money I think I have, I am putting it aside for when these expenses do come up.

In order to ensure you are properly prepared you need to first figure out how much money you need to set aside. For me, I plan for the following:

- Auto Insurance
- Jewelry Insurance
- Oil for Heat (It is cold in New England)
- Gifts
- Clothes
- Auto Repair/Maintenance
- Auto Registration/Inspection

Once you have your list in place you will realize that there are two types of expenses: those that are ongoing (clothes, gifts, etc.) and those that have a defined due date (insurance, summer electric bills, etc.).

For each type we figure out how much to set aside a little differently.

Ongoing Expenses

For ongoing expenses, calculate how much you spent last year. Now add 20% on to that number for buffer room. Once you have that number divide it by 12 and you now have how much you should be setting aside each month.

For example if you spent \$2,000 on gifts last year (birthdays, anniversaries, Christmas, Hanukkah, etc.):

$$2,000 * 1.2 = 2,400$$

$$2,400 / 12 = \$200 \text{ each month}$$

Defined Due Date Expenses

For a defined due date expense you treat it a little differently. If you don't have the bill then look how much you paid last time and add 20% for buffer room. If you have the bill already then just use the exact amount it says you owe.

Once you have the amount you will work with, take that and divide by the number of months until you have to pay.

For example if your last auto insurance payment was \$560 and your next payment isn't for 5 months:

$$560 * 1.2 = 672$$

$$672 / 5 = \$134.40 \text{ each month}$$

Once you have figured out how much you will need to set aside each month for all of these expenses, look to see if you can even afford to set that amount aside each month.

If not then this could be a big reason for your current financial situation and you will need to look to see what expenses you can minimize or cut altogether.

Now that you can afford the total amount each month this is your new "Allocated Funds" budget line.

Automate and Forget About It

Now that you know how much you need to set aside each month you need to find a place to store the money.

You cannot just simply leave the money in your checking account because you WILL spend it. We all think we have the willpower to not, but I can tell you it will get spent. I have been there and seen it numerous times.

Instead get it out of view and make it hard to spend. Just like your Emergency Fund the "Allocated Funds" should be stored at a bank separate from your everyday bank.

And since we aren't storing the money in our everyday checking account, why not put it in a high-interest savings account and have it make money while it waits to get spent.

I personally store our "Allocated Funds" in an Ally Online Savings account where I earn 1.5% interest on the funds. Since January our "Allocated Funds" account has earned \$20.44. Not a lot of money, but it certainly beats the \$0.34 I would have made in a traditional savings account.

Now that we have a place to put the money, we want to simplify getting it there. You can automate the transfer in one of two ways. You can either take it directly out of your paycheck via direct deposit or set up an automated transfer. Let's look at each:

Direct Deposit

Many employers offer the ability to deposit your paycheck into multiple accounts. If you want to go this route contact your HR department at work and find out how to modify your direct deposit setup.

On the form it generally allows you to specify an amount to be deposited into Account A and then the remaining amount to Account B.

From there you can set up however much you must allocated each month to go into your "Allocated Funds" and the remaining amount to go to your standard checking account.

Remember, that this dictates how much comes out of each check. If you are paid twice a month then divide the amount you need to transfer in half and if you are paid weekly then divide it by 4.

Automated Transfer

If you don't want to work with HR or are looking for the immediate and potentially easier route, you can set up an automated transfer. You can either do it from your current bank or from the bank with your "Allocated Funds" account.

In either case it is pretty simple. Go to the bank's online portal and find where you make a standard transfer request. From there you can typically create a recurring transfer that will occur every month.

If you cannot find this feature on your own account reach out to their support. If this functionality isn't offered, I know that an Ally Online Savings account does.

Keep in mind that depending on your current financial situation you might not be able to make the transfer all at once. If that is the case then create multiple automated transfers so that by the end of each month you have transferred the entire amount you needed to allocate.

Spending the Money

Now that we know how much we need to save and have automated it so that the money is being saved without us having to think about it, we now need to focus on spending the money.

If you are using a savings account for storing the money, then don't forget that federal law only allows 6 withdrawals each month, which might mean you need to do some planning.

With that in mind, I personally like to transfer the money back to my standard checking account. It allows me to avoid the 6 withdrawal penalties and makes it easier to track my expenses as they are all out of one account.

Don't overthink this step. When you map out your budget for the upcoming month, look at how much of your Allocated Funds you will be spending. Will you be buying back to school clothes? What about getting an oil change? Whatever the expense is plan for it.

Now at the beginning of the month do a single transfer of the amount you will need that month. This prevents any overdraft issues while also avoiding any 6 withdrawal penalties.

Bada bing bada boom! Now you can rest easy knowing that those expected expenses that have been throwing your budget out of whack are no more. A simple transfer at the beginning of the month and you can breathe easy.