DESCANT
FINANCIAL PARTNERS
An Independent Financial Planning Firm

Helping Your Kids Recover After a Major Money Mistake

The average college graduate is $20,000+ in debt, and today's young adults are clearly exposed to more opportunities for self-directed financial disaster than any group in history.

Despite the current credit crunch, credit cards are still a common way most young people afford their new adult lifestyle, and rising costs on everything from rent to gasoline presents deeper challenges.

So it happens. Your child gets in trouble with those credit cards, loses a job, or can't find a job to pay the sum total of the rising debt he or she has. What can you do?

Make sure you can afford to help: It's tough to say no to a financial bailout for your child, but depending on the level of trouble he or she is in and your own financial responsibilities, you may need to. Here are some ideas:

Both sides should come clean: Remember that this situation is as much about the relationship as about the money. The decision to help a family member with money problems requires understanding – lecturing tends to work not so well. But it's right to encourage your child to take a frank look at their financial situation and if they are in debt trouble of any kind, they should get help. It's also important that you show confidence that they will make it through this.

Let us help: We can look at your child's financial situation and your own and give you both a road map on how to work through your child's money problems and set up better money management techniques for after the crisis.

Should help be considered a gift? Actually, this is a good first question in any scenario where you offer help to a friend or family member. What happens if you don't get the money back? For the sake of the relationship involved, it might make sense to think through that possibility. Would the potential loss of money injure you, and worse, will it injure the relationship? This is why it might be a very good idea to present this solution as a one-time gift – and then stick to it.

But if it's a loan: You need to structure it professionally with clear consequences if it goes unpaid. Handled correctly, such a solution can offer benefits for the borrower and lender alike. Terms should be at arm's length to meet IRS rules but it can still be more attractive than the child could obtain in the current marketplace. But there's the potential for incredible downside. Unclear agreements can lead to missed payments or default. If the borrower dies suddenly, the lender's investment may be lost if the agreement isn't structured correctly. A properly executed promissory note is still an obligation of the estate, and may continue to be paid to an heir or other person or entity based on the terms as agreed. Conversely, if the lender dies, the agreement may be inherited by another family member who may not be as understanding if the borrower is slow with payments and may force an acceleration of payments if the agreement does not address this issue. It is advisable that the loan agreement be in writing and properly executed to meet IRS rules.

Work with them on budgeting: It's not going to be enough to solve the immediate problem. Set a clear financial course for your child going forward. They obviously have to have a stake in the planning, but you're going to have to provide guidance or seek our help.

Encourage them to start an Emergency Fund: Even if your child only has a few cents in their pocket after settling their troubles, encourage them to start an Emergency Fund. Optimally, they'll need to stash away three to six months' worth of living expenses, and even if it's just a small start, it's part of the recovery effort and should ALWAYS be a part of their overall financial planning. An Emergency Fund could be established in a Bank Savings account or a Money Market Account whereby they can access this without penalty to pay for those emergencies.