The Bank of Mom and Dad – a source of comfort for everyone

The BMO Wealth Institute provides insights and strategies around wealth planning and financial decisions to better prepare you for a confident financial future.

The perception of wealth influences how families use their financial resources to achieve personal and family goals. The Bank of Mom and Dad is seen as an important factor in helping meet these goals. These days, many parents feel they are on track to being financially comfortable, but worry that their children are not going to attain the same level of comfort on their own resources.

When asked what it takes to be considered wealthy, many families' self-portraits have changed dramatically over the last few years. Rather than just thinking about accumulated assets, families are also focusing on their lifestyles as an indicator of family wealth.[1] The emergence of the concept of the bucket list in popular culture and the sharing of these experiences through social media are examples of this change in focus.

Most families relate to the idea of being part of the middle class, and do not consider themselves wealthy. This view is supported by studies that show that as earnings increase, the amount of accumulated wealth required for families to consider themselves wealthy rises proportionately.[2] This tendency to either understate or overstate wealth is also highlighted in a report by the Organization for Economic Co-operation and Development (OECD) on comparative income that noted if we're rich, we think we're poorer than we are; if we're poor, we think we're richer.[3] This perception of wealth influences how families use their financial resources, including the so-called Bank of Mom and Dad, to achieve their personal and family goals.

Wealth that used to be simply thought of as assets in the Bank of Mom and Dad is now being seen as an important resource that allows people to be comfortable. How comfort is defined is unique to each person and family. A general definition of comfort is the freedom from financial worries and having the financial flexibility to do what you want, whenever you want or need to. For most, achieving comfort is seen as the result of hard work. Getting a good education, seeking financial independence, having strong values, and a little bit of luck along the way are all seen as important factors in achieving the desired level of comfort in life.[4]

> The perception of wealth influences how families use their financial resources, including the **Bank of Mom and Dad**, to achieve their personal and family goals.

Our children aren't as comfortable as we are

While many parents of young adults feel that they have either achieved or are on track to achieve their desired level of comfort, they worry that their children are not going to attain the same level just on their own resources. A survey was conducted for the BMO Wealth Institute to explore how parents of children 18 years or older felt about their children's future as they embark toward adulthood.[5] The survey found that 59% of parents felt their adult children have more opportunities and a better life than they did themselves in their twenties. Young adulthood is believed to be a period when anything is possible. But at the same time, young adults also feel that it is stressful (84%) and that their lives are full of uncertainty (65%).[6]

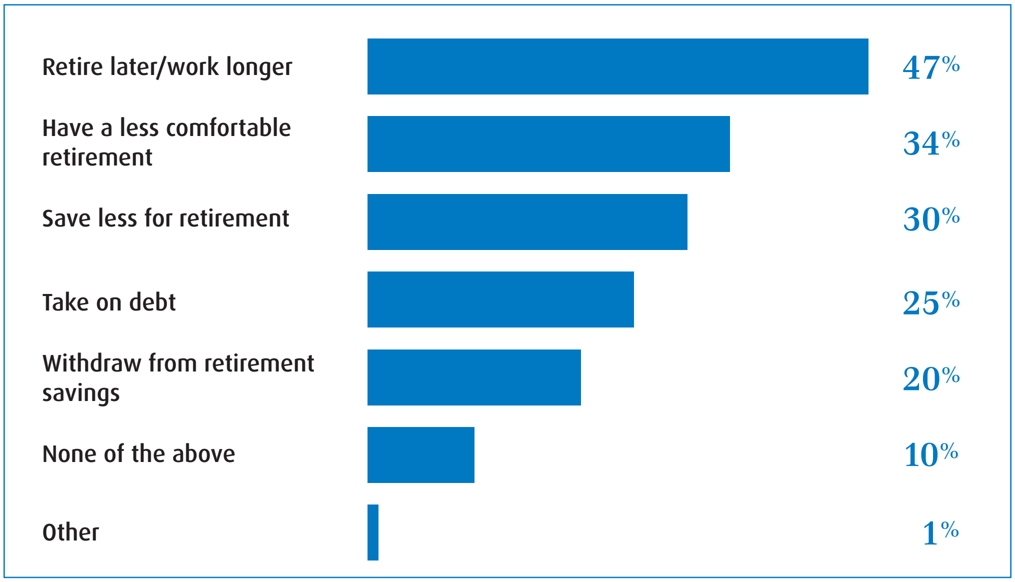
Much of this fear is driven by the economic environment young adults face today, with relatively high unemployment rates, difficulty in saving enough to buy a home, large student debt burdens, and underemployment due to being unable to find meaningful employment in fields related to their education.[7]

> **84%** of young adults **are stressed**, and **65%** **are uncertain** about their future.

Many parents realize that they got ahead partly because of the sacrifices that their parents made for them. These parents often believe it is their obligation to pay it forward by helping their adult children to also become successful. They will make many financial sacrifices for their adult children, with 47% prepared to retire later or work longer, 34% helping their adult children despite knowing it will result in a less comfortable retirement, and 30% saving less for their own retirement.

Parents are prepared to make retirement sacrifices to financially support their adult children.

Retirement sacrifices parents would make to financially support their adult children.



Source: BMO Wealth Institute survey by ValidateIt Technologies Inc., October 2015

Parents face a growing concern however, that there is a limit to the support they can provide. What effect will the decisions parents make today have on their own financial future, and on their desire to achieve and sustain financial comfort? Just how much money is available in the Bank of Mom and Dad to support the needs of every family member, never mind allowing parents to pursue items on their own bucket list?

When do children become adults?

Jeffrey Jensen Arnett, an experienced researcher on the topic of emerging adulthood, describes the journey toward adulthood as long and sometimes perilous.[8] When asked at what age someone reaches adulthood, more than half of parents (53%) and young adults (52%) agreed this happened between the ages of 22 and 25. By the age of 29, three-quarters of the parents (75%) and two-thirds of young adults (68%) regarded themselves as fully adult.[8]

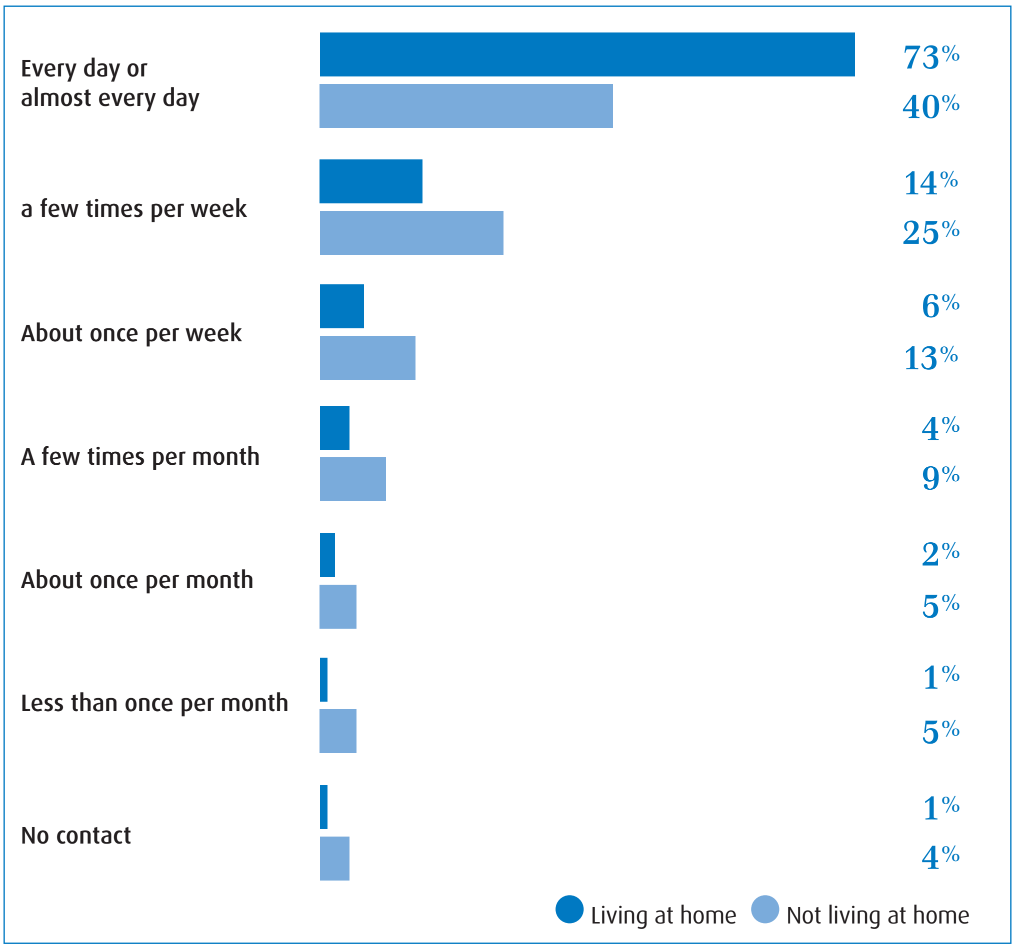
Parents and their children both agree on the behaviors that signify adulthood. Accepting responsibility for oneself was highlighted most often by parents (50%) and by adult children (36%), with becoming financially independent the next most selected behavior by parents (22%) and by adult children (30%).[6]

While these characteristics are important for every generation, parents believe that it takes longer to reach adulthood now than it did 30 or 40 years ago. Many more parents (43%) see this as a negative rather than a positive (13%).[6] The belief that it takes longer to become an adult today seems inconsistent with the fact that mothers and fathers of all income levels now spend more time engaged with and nurturing their children than parents did in prior generations.[9] However, this high level of parental involvement can extend well into adulthood, and is seen as lowering their children's degree of self-sufficiency.[10]

Despite concerns over the negative aspects of over-parenting – being helicopter parents – the frequency of contact between parents and their adult children is very high. Over half of the parents in the survey reported having contact with their adult child every day or almost every day (55%). Even for children that did not live with their parents, 40% of parents reported contact every day or almost every day, and 78% reported at least weekly contact with their children.

55%
of parents are **in contact with their adult children every day** or almost every day.

Frequency of contact based on where adult children live.

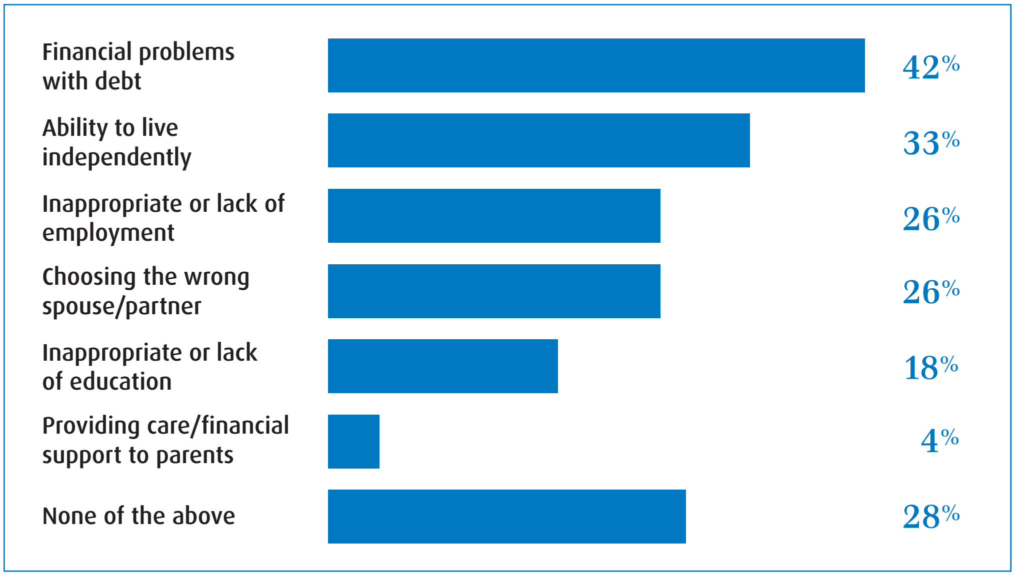


Source: BMO Wealth Institute survey by ValidateIt Technologies Inc., October 2015

When asked what concerns them most about their adult children, parents listed financial problems such as debts (42%), their children's ability to live independently (33%), and inappropriate or lack of employment (26%) as their top three answers.

Financial problems with debt is parents' greatest concern for their adult children.

Main concerns that parents have about their adult children.



Source: BMO Wealth Institute survey by ValidateIt Technologies Inc., October 2015

Considering all of this parental concern, their adult children were asked if they felt their parents had too much involvement in their lives. Surprisingly, only 30% suggested that their parents were too involved.[8] Giving their adult children more latitude may be difficult, as parents strongly value the relationships with their adult children – 78% reported that their relationship with their adult children was a source of enjoyment.[5] The ability of parents and adult children to achieve the levels of financial comfort they each aspire to depends in part on being on the same page when it comes to their goals and how they interact.

Helping our children

Many parents who pay it forward are providing more frequent and ongoing support for their children than they themselves received growing up. According to the BMO Wealth Institute survey, only 40% of parents received financial support from their parents as a young adult.[6] Conversely, 81% of parents reported providing financial support for their adult children. The table below shows that almost half of young adults receive occasional support when needed, while 36% receive frequent or ongoing support.

81% of parents have **provided financial support** to their adult children.

How much financial support is being provided by parents?

Source: BMO Wealth Institute survey by ValidateIt Technologies Inc., October 2015

Drawing from years of research, as well as clinical and field experience, therapist, international speaker and parenting consultant Alyson Schafer suggests that it may be well intentioned to offer help – financial and otherwise – but our grown children may come to expect their parents' support. Rather than seeing these financial contributions as generous but finite, they may feel they are simply their parents' responsibility. Frequently, relationships are strained when parents cut off support if attitudes of entitlement have developed over time.

While regular small amounts of financial support may not seem that much to a parent still in their prime working years, consider the financial impact of providing a child $500 per month to help them pay for their cell phone, internet and credit card bills. This adds up to $6,000 per year, an amount that could have a significant impact on the accumulation of retirement savings. For a parent, aged 50, contributing $6,000 instead to a traditional IRA each year could result in more than $220,000 of additional retirement savings by age 70½, assuming an annual growth rate of 6% for purposes of this illustration.

While helping our children is something we expect to do as parents, at least until they are financially independent, it is important to realize the long-term cost that this can have. This is especially important as the Bank of Mom and Dad is a limited resource that depends on the ability of parents to continue earning income to replace money withdrawn during their working years.

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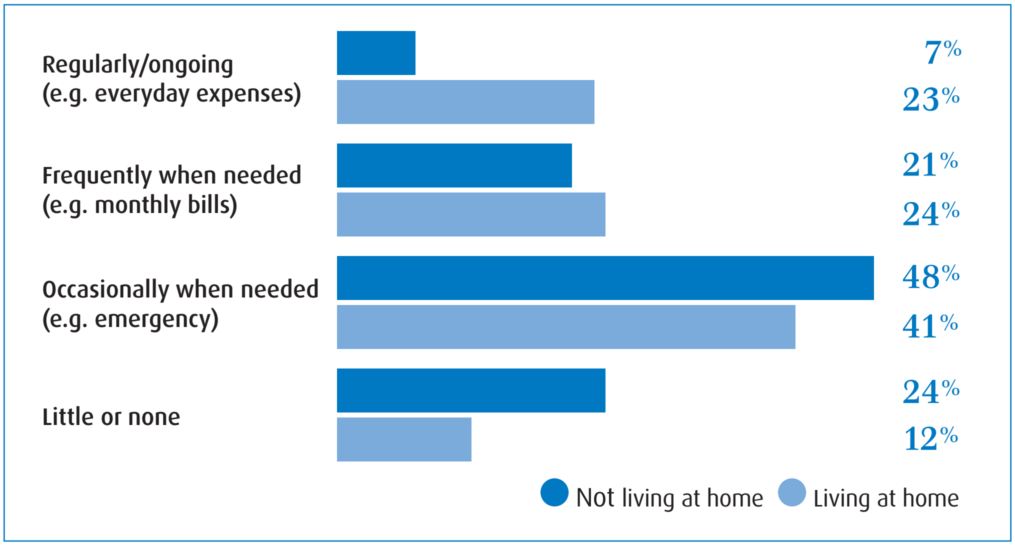
The amount of support provided

Parents today provide a significant amount of support for their adult children. According to the BMO Wealth Institute survey, almost 30% of parents with adult children that no longer live at home still provide frequent or ongoing financial support. A further 48% of parents reported providing occasional financial support to their adult children.

Percentage of parents who provided financial support based on where adult children live.



Source: BMO Wealth Institute survey by ValidateIt Technologies Inc., October 2015

Similarly to their parents years earlier, today's young adult children most commonly receive financial support for post-secondary education and by continuing to live at home. Interestingly, the most common reason cited for letting young adult children live at home is that they do not earn enough to live independently (66%). Other reasons include strong relationships between the parent and adult child (62%) and a desire to allow the young adult child to focus on their education (56%).[6]

Parents worry about their children finding appropriate employment, yet the majority of parents (78%) believe that their children have the same or greater opportunities than they did as young adults. This is despite the fact that youth unemployment is almost double the national headline rate, and jumps to almost four times the headline rate if youth underemployment is counted.[11]

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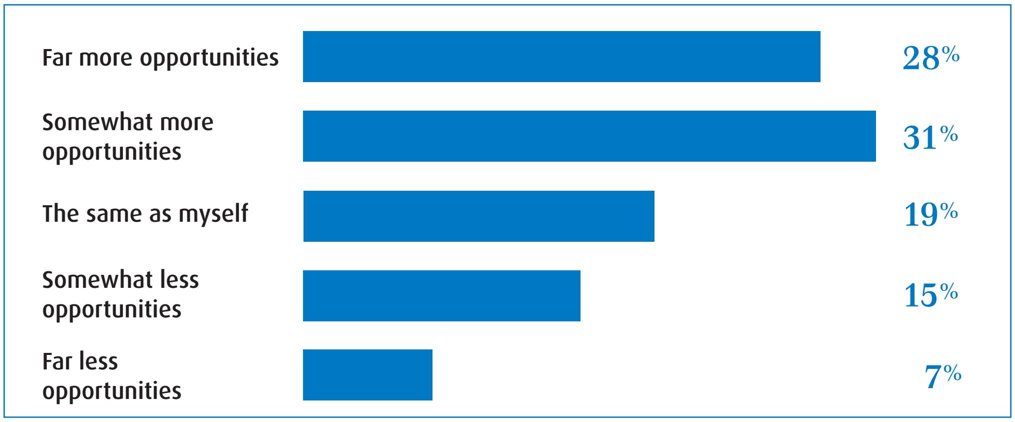
Percentage of parents who feel their adult children have more opportunity than they did in their twenties.



Source: BMO Wealth Institute survey by ValidateIt Technologies Inc., October 2015

With all these factors at play, it is hardly surprising that many adult children today are reluctant to leave behind the comfort their parents provide and move on with their own independent lives.

A better way to give to our children

The long-term financial implications of the ongoing support of adult children on the Bank of Mom and Dad and the challenges of helping adult children to achieve financial independence are concerns that have to be addressed.

According to Alyson Schafer, removing too many of the hurdles a child faces as they mature causes greater dependency in the long term. It would be better to provide children the opportunity to overcome some of the struggles they face, allowing them to emerge stronger. Further, she suggests that providing experiences from which a child can learn – both from their successes and from their failures – will build the emotional intelligence and the resiliency needed to adapt to this ever-changing world. It is far more valuable in the long run to provide learning experiences rather than ongoing financial support.

Help children build the mental muscle of resiliency to help equip them with the skills and strategies necessary to handle life's inevitable frustrations, challenges and setbacks.

Alyson Schafer

Discussions around financial planning

For adult children that have become accustomed to a level of financial support it is important not to cut them off all at once. Open communication is required, and may involve many conversations to set expectations for the future. It is important for all family members to understand that the Bank of Mom and Dad is a limited resource that was originally planned to be used primarily to support the parents and their financial goals.

Determining how much of the assets of the Bank of Mom and Dad is necessary for financial goals such as retirement will require a comprehensive wealth plan. The preparation of a financial plan that incorporates all available financial resources and includes all financial goals (including the bucket list) is an important first step that a financial professional can help with.

A **comprehensive wealth plan is required** to determine how much of the Bank of Mom and Dad is necessary for financial goals.

Once retirement needs have been met, then the competing interests of other family members like adult children and aging parents can be considered. Family members that have expectations of support need to understand the impact of these handouts on retirement plans if financial resources are tight; open discussions will provide a new perspective. A mutual understanding between young adults and their parents can help reduce expectations of ongoing financial support. This discussion is especially important if prolonged financial support will deplete retirement savings to the extent that parents will need financial support from their adult children in the future.

The advantage of starting early

A reliance on the Bank of Mom and Dad may arise simply because the kids have not learned enough about money from their parents. An understanding of personal finances involves learning how to budget, and establishing a saving and investing before spending habit. This will help children learn to live within their means, rather than always looking for a financial top-up to support an extravagant lifestyle. Parents who model good financial behaviors may have more success teaching their kids about finances because they will be practicing what they preach.

Parents who model good financial behaviors **will have more success teaching their kids** about finances.

When today's parents of young adults were young adults themselves, the household savings rate was more than 10%. This has fallen to less than 5% currently.[12] Today's young adults are not seeing their parents saving for the future at anywhere near the same rate that their parents saw at the same stage in life.

Putting money aside on a regular basis for specific purposes, such as for a college education for children through a 529 plan, is a good way to reinforce the message of budgeting for the future. Typically operated by a state or an educational institution, the purpose of a 529 Plan is to save for future educational costs. Named for Section 529 of the U.S. Internal Revenue Code that created it, one of the benefits of a 529 Plan is that earnings within the plan are generally not subject to federal taxes – and in many cases, state taxes – which may allow the college fund to grow faster. Along with their financial advisor, parents should work closely with their tax professional when discussing tax-advantaged accounts*.

As paper money becomes less and less prevalent, the idea of only so many dollars in your pocket to spend at a time is disappearing. To reinforce this concept, give younger children gift cards with set pre-loaded balances for special occasions that they can use at their favorite retailers. As long as the value is small and parents ensure that the card is not forgotten, this can help to reinforce the message of budgeting and spending only up to an available limit (including sales taxes) from an early age.

Benefit from a Roth IRA*

A Roth IRA can be a great way to make savings more tax efficient and extend the parent's ability to use the resources in the Bank of Mom and Dad to meet financial goals. Although the amount that can be contributed annually to a Roth IRA is limited by IRS guidelines, income earned in the account is generally not subject to any federal or state taxation. Roth IRA distributions are tax free after 59½ as long as you have had the Roth for 5 years. Also you can always withdraw your original contributions tax free, and there are specific rules that pertain to those with disabilities.

A Roth IRA **can be a tax efficient strategy** that could extend the ability of the resources in the Bank of Mom and Dad to meet financial goals.

Use Gift Tax* rule exceptions

If the Bank of Mom and Dad does have the financial resources to provide for the goals of the whole family, taking advantage of exceptions in Gift Tax rules can help to increase the benefit available for children and dependent parents. Gifts made for tuition purposes or to pay medical expenses are not subject to Gift Tax, making more of the resources of the Bank of Mom and Dad available, over and above the current $14,000 annual exclusion amount.

Leaving a legacy of financial comfort

Some parents don't realize how much their children depend on them financially, and consequently don't provide for them adequately in their wills. This can make it difficult for a surviving spouse to manage their own needs as well as providing financial support for their children (or children from a previous relationship). Wills can be planned to provide support for dependents. An insurance policy is one way to make additional funds available to help the Bank of Mom and Dad provide for both a surviving spouse and adult children. A joint insurance policy on both spouses that pays out a lump sum tax-free to the surviving spouse to supplement income or to support children who may be struggling financially is a good option.

Some parents **don't realize how much their children depend on them financially**, and consequently don't provide adequately for them in their wills.

Now or later

Even if the Bank of Mom and Dad is well funded and can afford to provide ongoing support for adult children, it is important to realize that this will reduce the amount available for undetermined but likely expenses associated with aging, such as health care and long-term care.

As an example, many parents are choosing to help their adult children with their home purchase by providing large lump sum amounts to help with the down payment. For the majority of parents (68%) these transfers represent a form of early inheritance that can help many young adults enter the real estate market – something that may not be possible without their parents' help. Most young adults, however, view this help as a loan (79%).[13]

Funds withdrawn from the Bank of Mom and Dad today **will no longer be available for undetermined but likely expenses** associated with aging, such as health care and long-term care.

Moving forward to achieving financial comfort

It is important to discuss your unique situation with your financial professional, who will be able to work with you and other professionals to develop a personalized financial plan. By working together with your BMO financial professional it will be possible to achieve greater peace of mind as you work toward building the financial comfort that you desire for yourself and your family.

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