

## The Income-Draw System

If you are paid on commission, or work seasonally, you probably have wondered if there was any way to get off the financial rollercoaster such jobs bring and have a stable, consistent income. One financial expert and author, Bernard Poduska<sup>1</sup>, suggests a system that will do just that. It's called the income-draw system.

**1. To begin, set up two separate bank accounts**—Account A and Account B. The income-draw system is based on a predetermined monthly transfer from one account to another. You may or may not find it to your advantage to use an account that earns a fairly good interest rate, such as an online savings account. *Kiplinger's Personal Finance* magazine indicates that EmigrantDirect, ING Direct, and HSBC Direct<sup>\*</sup>, have often paid “between 4.35% and 5.05%” annual interest<sup>2</sup> (check with each company for current rates). Many local banks, credit unions, and other online banks may also offer online savings accounts with competitive interest rates. Regardless of the bank or credit union you choose, and if the account is online or not, the important thing is to make sure that you are comfortable with the institution and that they are either FDIC or NCUA insured.

**2. The next step is to deposit all of your income into Account A.** Regardless of the source of income and how much money you earn from one month to the next, commit to deposit all of your income each month into Account A. If possible have your income directly deposited into Account A. If taxes are not automatically deducted from your paycheck, be sure to set aside an appropriate amount (in a separate account) to meet your tax obligations.

**3. Next decide on a monthly “salary.”** You can figure your “salary” in a variety of ways. If your job has not changed all that much, the easiest way to figure your salary is to take your income from last year and divide it by twelve. To be conservative, you might decide to have your monthly “salary” be slightly less than this amount.

**4. Arrange for a monthly transfer of your “salary” from Account A to Account B.** Choose a day each month that will be your “pay day.” This day should be the same day every month. This is the day that you will transfer your “salary” from Account A to Account B. The easiest way to facilitate this transfer is to ask your bank to automatically transfer your “salary” from Account A to Account B each month.

**5. Pay all your expenses from Account B.** Once you've set up the system, only pay expenses from Account B. Commit yourself to not spending more than your monthly “salary.”

**A note about charitable contributions.** Some people may pay a certain percentage of their income to a religious organization or charitable cause. If this is the case, you may find it helpful to pay charitable contributions directly out of Account A. In this way it would seem as if your contributions were deducted out of your paycheck before you received it.

Another option would be to pay the set percentage out of your Account B “salary.” If you arrive at the end of the year and have funds in Account A, you can then pay the same percentage of those funds toward your religious organization or charitable cause. By doing this your percentage donated over the course of the year will be the same as if you had paid that percentage on your Account A income.

Try to forget that Account A even exists. As you live within your monthly “salary,” you will find that your life is less stressful. As Bernard Poduska says:

The income-draw system enables you to enjoy a steady income without worrying about good and bad months. As a consequence, you can get off the financial yo-yo that most people with irregular incomes tend to experience—having money to burn one month and buying food on credit the next. (p. 147)

**Getting Started.** Poduska notes that “unless you happen to be having a good month at the time you start your income-draw system, you may have to take a reduced ‘salary’ until your reserves build up.” He also suggests that “you may wish to put aside small amounts each month until you accumulate enough to cover normal monthly draws” (p. 147). If you have money left in Account B at the end of the month, either transfer it to Account A, or leave it there to use the next month. Try not to spend it just because you have it.

**Ongoing Adjustment.** Poduska notes that ongoing adjustment is necessary: “At the end of the year, if you have money left over in your Account A reserves, you can consider increasing your ‘salary’ for the upcoming year” or consider putting the extra money in savings. Conversely, “If you find your reserves frequently being depleted, you may consider decreasing your draw during the next year” (p. 147).

**An Example.** To illustrate how the income-draw system works, Poduska shares an example:

The amount you actually deposit in Account A will vary from month to month, but it should accumulate enough of a reserve to ensure continuous availability of funds in excess of the monthly “salary.” For example, assume that after you've set aside the funds necessary to meet tax obligations your January income is \$2500 and you withdraw only \$2000. Your reserve will be \$500. February's income is \$3500 (only \$2000 is withdrawn, leaving \$2000 in the reserve); March's income is only \$1500 (you can still withdrawal your \$2000 “salary,” leaving a reserve of \$1500); April's income turns out to be only \$1000 (nevertheless, you are able to withdraw \$2000, leaving \$500 in the reserve). (p. 147)

<sup>1</sup> Poduska, B. E. (1993). *For Love and Money: A Guide to Finances and Relationships*. Pacific Grove, California: Brooks/Cole Publishing Company, p. 142, 147.

See also Poduska, B. E. (2000). *Till Debt Do Us Part: Balancing finances, feelings, and family*. Salt Lake City, Utah: Shadow Mountain, p. 117-118.

<sup>2</sup> Where should I put short-term savings? (2006, September). *Kiplinger's Personal Finance*, 60, p. 80.

<sup>\*</sup> Utah State University Extension does not endorse any financial institution.