Learning Objectives

1. Understand the importance of beginning your financial planning early.
2. Recognize the “10 Financial Life Events” and strategies to deal with them.
3. Understand and manage the keys to financial success.

Remember the movie *The Wedding Singer*, in which Adam Sandler plays Robby, a lovable love song crooner? At the start of the movie Robby is left at the altar. When he discovers that the reason is his lack of money, Robby laments, “Geeze, you know that information might have been a little more useful to me yesterday.”

Later, Robby falls in love with Julia, played by Drew Barrymore, who is already engaged to Glenn, a Wall Street bond broker.

“Hey, you know why she’s marrying him, don’t you?” Julia’s roommate asks Robby.

“The money thing, the security, the nice house, I guess. That’s important to some people,” is Robby’s reply.

“No, it’s not important to some people. It’s important to all people.”

“Hey, then I guess I’m in big trouble.”

In the end, true love reigns, and it turns out that to Julia, money doesn’t really matter after all.

But let’s face it, in movies as well as in real life, money not only determines whether you meet your goals, but how people relate to you. In fact, money problems are the
number one cause of divorce. The bottom line is that money does matter.

Most of us already know this, but most of us never learn how to truly manage money. But you’re ahead of the game: You’ve been introduced to the basics of financial planning. In this chapter, we recap much of what you’ve already learned, and we put it together in the form of an action plan. We also look at some of the special problems you may face in the near future—focusing on life events that could throw a monkey wrench into your financial plan. We examine the keys to financial success and ruin. Finally, we talk about getting started—that is, putting your financial plan into action. Following the advice in this chapter sets the stage for a sound financial future.

Your financial future starts now. The challenges you will face may include student loans and credit card debt; budgeting, spending, and saving; and the financial shocks of marriage and children. But it is time to make a choice: You can take control now, or put it off and make financial management a heck of a lot tougher in the future. Money does matter, even to Adam Sandler’s Robby, who said: “I’m a big fan of money. I like it. I keep it in a jar on top of my refrigerator. I’d like to put more in that jar.”

We’d all like to put more money in our jars, wouldn’t we? So, let’s get started.

The Ingredients of Success

It is simply impossible to succeed financially unless you:

- Evaluate your financial health.
- Plan and budget.
- Manage your cash and credit.
- Control your debt.
- Make knowledgeable consumer decisions.
- Have adequate health, life, property, and liability insurance.
Understand investing principles.
Make investment decisions that reflect your goals.
Plan for retirement.
Plan for what happens to your accumulated wealth and your dependents after you die.

Everything in personal finance starts with the budgeting and planning process first outlined in Chapter 1. You must periodically review your financial progress and reexamine your financial plan. In other words, personal finance is an ongoing process, with no financial plan being fixed for life. But even though financial plans don’t last forever, without them, goals are a mere fantasy.

There isn’t a topic covered in this book that is not essential to your personal financial health. As such, you’ll want to keep revisiting all these topics to make sure that your financial plan reflects your current financial health and what’s going on in your life.

Let’s now try to put all this together. First, let’s take a look at your place in the financial life cycle. Then let’s look at 10 financial life events—events that will change your goals, impact your financial resources, and create new financial obligations for you. Then we will examine 12 decisions that you will be making that will determine whether you succeed financially. Finally, we will end with a call to action—to begin your financial plan today.

The Financial Life Cycle

Let’s look at where the typical recent college grad is in the financial life cycle we outlined in Chapter 1. Recent graduates make a lot of financial decisions in their first decade out of college. They may purchase their first car and possibly their first home, they will be establishing credit and paying taxes, and they may even get married and begin families. If you’re a recent graduate, you will want to set up an emergency fund, start saving for your goals, and begin putting money in an IRA and a retirement account. Savings-wise, these are an exceedingly important 10 years. The financial decisions you make now will affect the rest of your life.

If, beginning when you turn 19, you put away $2,000 at the end of each year for 7 years in an IRA that earns 11 percent per year, and then nothing thereafter, at age 65 you will have more than $1.2 million! If you wait until you are 25 to start that IRA and make payments every year for 40 years, you still won’t catch up—you’d only end up with $1.164 million. Moreover, if you wait until you’re 30 to start that IRA and make 35 payments, you’ll end up with $683,179! There’s simply no substitute for starting early. It’s without doubt the simplest strategy: to recognize your financial future starts now and just do it.

Financial Life Events

In the course of your lifetime you will experience many events that will change your goals, affect your financial resources, and create new financial obligations or opportunities for you. While there is an almost unlimited number of these type of life events, we will focus on ten of the most common.

Life Event 1: Getting Started
Life Event 2: Marriage
Life Event 1: Getting Started

There is a beginning for everything, even for your financial future. For most of us, getting started begins with graduation from school, or with the realization that we have to get our financial life on track. Let’s take a look at some of the steps involved in “Getting Started.”

Step 1: Lay the Groundwork Before you can make financial progress and plant the seeds for your future financial success, you need an understanding of investments and personal finance. This course will take you a long way toward that goal, but it will also be important to keep up with all the changes that occur in the financial world by making a habit of reading periodicals such as *Money, Smart Money,* and *Kiplinger’s Personal Finance,* and newspapers such as the *Wall Street Journal.* Laying the groundwork involves more than just gaining an understanding of personal finance; it also involves an assessment of your current finances, a plan for both the expected and unexpected events of the future, as well as a realization as to how you view money—your financial personality.

- Expenses and a Budget. Know how much money you make. Know how and where you spend it. Probably the easiest way to get started and actually be successful is through the use of an online budget, and of those out there, Mint.com is one of the best. If you check out Figure 2.8 earlier in the book, you’ll find a short write-up on all the features of Mint.com and also of Geezeo, which is another online budgeting tool.
- Control Your Debt. Eliminate any high-interest debt you have and control your credit card purchases. You might want to take another look at the section at the end of Chapter 8 titled “Tying Things Together: Debt and the Real World.”
- Establish an Emergency Fund. Remember Principle 5: Stuff Happens, or the Importance of Liquidity.
- Insure Yourself. Make sure you have the kind of insurance that you need (i.e., disability), but only consider life insurance if you really need it.
- Control Your Credit Score. A high credit score will have quite a few financial benefits. If you’re having trouble controlling your credit score, check back to Chapter 6 for some help.

Step 2: Identify Your Goals Nothing happens without a plan. Identifying your goals is the first step in setting up your financial plan.
**Identify and Prioritize Financial Goals.** Remember **Principle 2: Nothing Happens Without a Plan.**

**Set a Time Frame.** When would you like to reach these goals? One year or ten?

**Identify the Costs of Your Goals.** How much in the way of capital will it take to reach these goals?

**Revisit Your Goals Annually.** Set a time every year—or if you are married set up an annual meeting with your spouse—to review your financial health. Put together a personal balance sheet and a personal cash flow statement for the past year. This may sound like a good deal of work, but if you’re using Mint.com, all the work is done for you. Check out the progress you’re making toward your goals, make the necessary adjustments, and make sure your retirement goals are part of your discussion.

**Step 3: Begin Saving for Your Goals**  When you have so many years to meet your goals it may be difficult to realize the need for immediacy, but starting to save today will make it much easier to realize those financial goals later. Not only does Mint.com provide you with help in setting up goals, but it also provides help in putting together a savings plan to meet those goals. Whether you’re saving to buy a home, for retirement, to pay down your student loans, or to pay off your credit cards, Mint.com provides a structure to meet those goals. Not only that, but Mint.com also gives you updates on your progress toward your goals, which reinforces your saving efforts.

**Save More Than You Think You Can.** Don’t let your expenses determine how much you save—decide to save and do it.

**Make Saving Automatic.** Have money taken directly out of your paycheck and put into savings. Remember **Principle 10: Just Do It!**

**Avoid Expenses Whenever You Can.** Look closely at no-load, low-expense mutual funds when investing in stocks.

**Don’t Procrastinate.** Don’t put off saving because “I’ll have more money to invest later”—that can be a recipe for financial ruin. For many, this is the biggest financial challenge they will face.

**Catch Your Matches.** Take advantage of any matching contributions that your employer offers. If your employer matches 401(k) contributions, max them out.

**Roth.** If you anticipate being in a higher tax bracket when you retire, consider a Roth IRA where the earnings that accumulate are tax-exempt.

**How Much Risk Can You Tolerate?** Gain a good understanding of your risk tolerance. If you’re not quite sure of your risk tolerance, you might want to check out one of the Web sites mentioned in Figure 11.4. For example, there is an excellent risk tolerance quiz located at njaes.rutgers.edu/money/riskquiz/default.asp.

**Asset Allocation.** Understand the importance of asset allocation and diversification.

**Put Together a Strategy.** Base your investment strategy on when you need your money, your risk tolerance, and your asset allocation.

**Control Your Spending.** Just because you earn it, doesn’t mean you have to spend it. That probably means you don’t want to buy a brand new car that depreciates as soon as you drive it off the lot. Just knowing how much you are spending and how those spending decisions impact the amount of money you’ll have at the end of the month helps control spending. Once again, Mint.com does exactly that, and also has the ability to e-mail you or text you when you go over budget.
Step 4: Manage Your Portfolio  Once your plan is in place, make sure that it changes to reflect changing goals and the progress made toward those goals. This means monitoring progress and periodically rebalancing investments.

- **Monitor Your Portfolio.** Make it an annual event to review your investment performance and make appropriate adjustments to your savings and investment strategy. When it comes to managing your portfolio, the easiest way to do it is online through your broker’s Web site, or if you have investments at a number of different financial institutions you might try Smart Money’s Web site (www.smartmoney.com) or Mint.com.
- **Stay Current.** Stay abreast of any changes in the tax laws that might impact your investment portfolio.
- **Adjust to Changes.** When necessary, change your investment goals to match changes in your life.

Life Event 2: Marriage

Most married couples plan their wedding down to the smallest detail but spend little time talking about money and planning their financial lives together. That’s probably not a great idea, given the fact that money problems are the top reason people get divorced. Managing your money when you’re single is tough enough. But when you’re married, you not only have to plan for your own expenses, but also those of your partner.

Your partner may bring student loans, credit card debt, a past bankruptcy, or other financial problems to the marriage. And let’s face it, you’re marrying this person’s money, too. On top of all this is the fact that opposites tend to attract. That means if you’re a saver, you might end up married to a spender, and if you’re a spender, there might be a saver in your future. In either case, if you don’t do some financial planning from the beginning, there will also be some arguments in your future.

The place to start is with a discussion about money. The aim is to find out your partner’s financial history, habits, and goals. Checklist 18.1 offers guidelines for this very important discussion.

Once you have an understanding of each other’s financial personality and views on money, it’s time to see how this translates into spending habits. You’ll want to track your expenses carefully for a month. When you do this, it’s important to keep track of all your expenses, including money you spend on books at Barnes & Noble or on lattes at Starbucks. This should provide fuel for more discussion as you see how financial views translate into action. You will now have enough background to make a budget. Set out your goals and make plans to attain them using what you’ve learned in this book. Just as important as setting up a budget is identifying expenses that you can eliminate. Tracking your spending will also let you plan savings, which you’ll want to make automatic.

Once you’re married, review and revise your plan annually, or whenever there is a significant change in your life—for example, the birth of a child. If you can’t get your financial plans settled by yourself, be sure to contact a financial planner. A planner will help you set up a plan that works and will guide you through any conflicts you might have. If you’re still having problems, you can seek the help of a financial counselor, a financial planner who specializes in counseling couples about money.
Two of the many financial decisions you face when you get married are whether to have joint or separate checking accounts and credit cards. Clearly, one checking account is easiest for most couples, but if you have incompatible money management styles, consider two accounts. That’s kind of the financial equivalent of two bathrooms. It makes record keeping more tedious, and you may not get as good a deal on your checking account from the bank, but if your money management styles are dramatically different, it may be the best choice.

With respect to credit cards, you not only want to control credit card spending but also to use your credit card to establish a strong credit history. If you’ve ever heard stories of a divorced, widowed, or separated stay-at-home spouse unable to get credit, you know how difficult this can be. The way to avoid this potential problem is for each spouse to have his or her own credit card.

When you are first married, it is time to reexamine your goals and begin planning for any children you might expect in the future as well as for your eventual retirement.

**Step 1: Get Organized** You now have a new financial partner and new considerations to work with, so the first step is to review and reorganize your finances.

- **Get Talking.** Discuss your approaches to handling money, as it comes in and goes out, and create rules to handle differences.
- **Update All Your Financial Records.** Make sure your driver’s license, passport, Social Security identification, bills, and any financial accounts reflect any name and address changes that might have occurred. Consider making your new spouse the beneficiary on your financial accounts, for example, investment accounts, workplace retirement savings accounts, or employer stock plan accounts you might have.
- **Decide What’s Common and What’s Separate.** Decide whether to keep separate bank accounts, merge everything, or a bit of both.
- **Gain Control of Your Debt and Your Credit Score.** Life will be much easier if you can work together to gain control of any credit card or other type of debt that one partner may bring to the marriage. Once your debt is under control, your credit score should rise and it will be much easier to successfully apply for a home mortgage. When dealing with debt that you or your partner brings into the marriage, you should begin with a discussion detailing all the debt each of you may have. Next, determine how to pay it off. Will both spouses chip in, or will each spouse pay down his or her own loans? Also, in order to control debt, you should create a strategy to save for one-time expenses—like a vacation or a new piece of furniture—without incurring debt.
• **Consolidate Your Credit Cards.** Avoid having twice the number of cards needed.

• **Merge Your Finances to Make Good Decisions.** If you don’t consolidate your finances, allowing you to see the big picture—that is, your combined income and savings—you won’t be able to make good joint decisions. Once again, Mint.com is a great tool to tie things together and create a budget that works for the whole family.

• **Set Up a Plan to Pay Household Expenses.** If it’s not realistic to merge all finances, one alternative is to create a joint checking account, with each spouse contributing money to pay for household expenses like the mortgage, utilities, and groceries.

• **Set Aside an Area Dedicated to Your Financial Paperwork.** It will be much easier for you to keep track of your finances, pay bills, monitor your budget, and plan for the future if there is a central, dedicated location for dealing with personal finances.

**Step 2: Revisit Your Financial Goals**

A new financial partner means new financial goals. This is a good time to revisit your financial goals, both short- and long-term, and set in place what is necessary to accomplish these goals. It is also a time to make decisions on how to manage your finances. Remember **Principle 2: Nothing Happens Without a Plan.**

• **Reexamine Your Financial Goals.** Have you changed your mind or time frame with respect to purchasing a home? Are children now a consideration?

• **Begin Saving for Your Goals.** Even if you don’t have children, but are planning to have them, begin saving for their education. Combining your incomes should allow you to save more. This is also the time to get serious about saving for your future. You’ll find that your expenses will only grow as you get older, which means you need to start saving now.

• **Make Your Saving Automatically.** Have money automatically deducted from your payroll.

• **Make Sure You Have an Emergency Fund.** Be prepared for the unexpected. The importance of an emergency fund cannot be overstated when it comes to marriage. Financial emergencies put enormous stress on a marriage. An emergency fund will not only help in the time of need, but will also provide a level of financial security that is important—you may not be able to avoid the emergency, but you can avoid the stress. Put a plan in place to have 3 to 6 months of living expenses set aside in a savings account or money market account and make sure to keep it strictly off limits until there’s a real emergency.

• **Begin Working Toward Retirement.** Make sure you have begun to save for retirement and, if you are both working, you might want to do it separately.

**Step 3: Reexamine Your Insurance and Benefits**

With a new partner in life, you may want to change your insurance beneficiaries, consider purchasing additional insurance, and make sure your benefits are coordinated.

• **Review Your Beneficiaries.** Make sure you review all insurance beneficiary designations.

• **Include All Family Members.** Are all family members covered?

• **Review Your Insurance.** Review your health insurance coverage. Does it cover maternal and prenatal care if this is a possibility? Also, review your homeowner’s and auto insurance.

• **Disability Insurance.** If you don’t already have it, make sure you have adequate disability insurance.

• **Coordinate Your Benefits.** If you both work, study your benefit options to identify the best and cheapest protection. Then, coordinate your benefits; perhaps you can drop a benefit that is covered in your spouse’s plan.
Step 4: Reexamine Your Taxes  Your tax status and the tax-advantaged benefits and opportunities afforded you by your employer may change as a result of your marriage.

- Update your W-4 Forms. W-4 forms should reflect your new tax status as a couple.
- Take Advantage of Tax Breaks. One spouse may receive tax breaks; make sure you shift savings from one spouse to the other to take full advantage of any tax breaks offered by employers.

Step 5: Make a Will  You must be concerned about providing for your spouse and possible children in the event of your death.

- Make a Will. Make or update your will to include your spouse and possible children.
- Review Your Beneficiaries. Review all beneficiary designations on your retirement accounts.

Step 6: Make It Work  Money is a major cause of friction in marriage, and while a good dose of financial planning will help, there are also things you should avoid doing.

- Don’t Keep Money Secrets. If you or your spouse overspend, don’t hide it from the other half. There is no good outcome from financial secrets.
- Don’t Let One Partner Take All the Financial Responsibility. While only one of you may be in charge of paying the bills, that doesn’t mean your partner should live in ignorance and spend without consequence.
- Avoid Bad Debt. Think twice before taking out a loan for something that will decline in value over time, like a car, keeping in mind that eventually you could owe more than your purchase is worth.

Life Event 3: Buying a Home

Your home is your biggest investment, so it shouldn’t come as a surprise that purchasing it has financial implications. Let’s look at some of the things to consider when buying a home.

Step 1: The Purchase Fits Your Financial Plan  Make sure that your purchase falls within the limits of your financial goals and budget.

- Keep Track of Your Credit Score. Many things affect your credit score (i.e., number of credit cards, debt level, and late payments). Knowing your score might affect your purchase decision and the ease in making that purchase.

Step 2: Consider Tax Implications

- Take Advantage of the Tax Benefits. When your major purchase is the renovation of your home, you might consider using a home equity loan, with tax deductible interest, to fund it. Or, use a home equity line to purchase your car or pay tuition; the interest, with some restrictions, will be tax deductible.
- Build the Tax Benefits into Your Budget. Include the tax savings, which your home mortgage interest and real estate tax payments have on your taxes, into your budget.
- Reexamine Your Investments. If you invest in municipal bonds and you’ve moved to a new state, consider moving your investments to municipal bonds from your new state to take the full tax advantage.
- Update Your Employer Records. Meet with the new employee benefits coordinator to update your W-2 with your new address and possible changes in deductions.
Know Your State. If you are moving to a new state, visit its tax Web site. These sites generally provide great information—from the cost of registering your auto to your new income tax rate—check them out. Higher or lower taxes mean less or more money for meeting your goals—either way, don’t be surprised.

Step 3: Take care of the Details

Update Your Address. Provide your credit card companies, bank, and other financial institutions with your new address.

Update Your Insurance Policies. Update your insurance policies to reflect the value of your new home as well as its contents. Note that your auto insurance rate may be impacted by the location of your new home.

Life Event 4: Having a Child

As we saw in Chapter 1, the cost of raising a child from birth to age 18 runs about $222,360 and the cost is rising. When you add in the cost of a college education and lost wages resulting from child-rearing duties, U.S. News and World Reports estimates that for a medium income family, a child requires an investment in excess of $1.45 million over 22 years. Yikes!

Certainly, there is more to life than money, and you just can’t quantify the joys and satisfaction of raising children. But you want to make sure you take the financial pain out of having children by planning ahead.

Step 1: Survey Your Finances Reassess where you are in light of your growing family and develop a financial plan for both the expected and unexpected costs of your new child as well as your short- and long-term goals. Make sure that you and your spouse are in agreement over your spending priorities.

Assess Your Current Financial Situation. Before you begin putting together a new financial plan, you’ve got to know where you are right now. As you develop your plan, make sure that you have an adequate emergency fund.

Reexamine Your Financial Goals. With a new child, your financial goals, both short- and long-term, may also change. A new short-term goal might be to find a bigger place to live, whereas planning for your child’s college tuition might be among your long-term goals.

Revise Your Budget. Revise your budget to reflect the new goals and expenses associated with a new child. You or your spouse might be taking some time off from work or even quitting a job. That should be factored into your budget. Make sure that you continue your contributions toward your retirement.

Step 2: Plan for College As we saw earlier, now is the time to start saving if you plan on funding your child’s college education. The sooner you start to save, the easier it will be to reach that goal—this is a perfect example of Principle 3: The Time Value of Money.

Estimate the Costs. Fortunately, there are a number of college tuition planning calculators on the Web, for example, the College Planner (www.offtocollege.com/calculate/) and www.dinkytown.net/java/CollegeSavings.html. Open a 529—and encourage contributions from family and friends—to maximize the benefits.
offered by the tax-advantaged plan. Keep in mind that you don’t necessarily have to use the plan sponsored by your state.

◆ **Automate Your Savings.** Have savings withdrawn directly from your salary.

**Step 3: Reconsider Your Insurance Needs** Your insurance coverage needs will change when you have a child. When it comes to providing protection for a child, remember Principle 7: **Protect Yourself Against Major Catastrophes.**

◆ **Review and Update Life, Health, and Disability Insurance Coverage.** For many individuals, the arrival of a child signals a need for life insurance—take a serious look at term life insurance. Is your health and disability insurance adequate? Make sure your new child is covered under your health insurance policy.

**TABLE 18.1 What You Can Do with Just Some of the Money if You Decided to Pass on Parenthood**

<table>
<thead>
<tr>
<th>Age</th>
<th>Some of What You Spent on Your Child</th>
<th>How You Might Have Spent That Money on Yourself</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Expense</td>
<td>Cost</td>
</tr>
<tr>
<td>0</td>
<td>Average cost of delivery</td>
<td>$6,400</td>
</tr>
<tr>
<td>1</td>
<td>An au pair (live-in nanny)</td>
<td>$30,000</td>
</tr>
<tr>
<td>3</td>
<td>Montessori preschool</td>
<td>$4,000</td>
</tr>
<tr>
<td>5</td>
<td>The “must-have” toy: the (very rare) 1959 Blond Ponytail Barbie</td>
<td>$1,800</td>
</tr>
<tr>
<td>7</td>
<td>After-school program for the gifted</td>
<td>$3,564</td>
</tr>
<tr>
<td>8–9</td>
<td>Private school</td>
<td>$19,770</td>
</tr>
<tr>
<td>10</td>
<td>Violin and lessons (3 times per week)</td>
<td>$4,150</td>
</tr>
<tr>
<td>11</td>
<td>Self-defense lessons (3 times per week) after being beaten up when going to violin lessons after school</td>
<td>$3,750</td>
</tr>
<tr>
<td>12</td>
<td>Therapy to improve self-esteem (once a week)</td>
<td>$5,000</td>
</tr>
<tr>
<td>13</td>
<td>Clothes from Abercrombie &amp; Fitch (to help with self-image)</td>
<td>$5,500</td>
</tr>
<tr>
<td>14</td>
<td>Transportation to and from community sentencing for using fake ID</td>
<td>$299</td>
</tr>
<tr>
<td>15</td>
<td>Bill from Mystic Tattoos</td>
<td>$239</td>
</tr>
<tr>
<td>16</td>
<td>Laser tattoo removal</td>
<td>$2,796</td>
</tr>
<tr>
<td>16.5</td>
<td>Increased automobile insurance premiums</td>
<td>$1,345</td>
</tr>
<tr>
<td>16.5</td>
<td>Increase in auto insurance after two tickets and one accident (including lawyer fees)</td>
<td>$2,250</td>
</tr>
<tr>
<td>17</td>
<td>SAT prep course</td>
<td>$600</td>
</tr>
<tr>
<td>Total (not including college)</td>
<td>$93,202</td>
<td>Total (not including college savings)</td>
</tr>
</tbody>
</table>

Now add in 5 years of college for your child or a Mercedes-Benz CL-Class CL63 AMG at $154,580 for you!
**Step 4: Update Your Wills and Trusts** Now is the time to consider estate planning. At a minimum you’ll want to designate a guardian for your children in the event something happens to you and your spouse.

- **Update or Make a Will.** If you don’t already have a will, make one now. Designate a guardian to raise your child and specify how your child will be provided for in the event something happens to you and your spouse.
- **Update Your Retirement Account Beneficiary Designations.** Contact the retirement and benefits department where you work and update your beneficiary designations.

**Step 5: Take Advantage of Tax Savings** Along with a child come some tax advantages.

- **Social Security Number.** Apply for a Social Security number for your child. It’s not that you expect your child to work, but you want the tax breaks that a child brings and the IRS requires both your child’s name and Social Security number.
- **Update Your W-4 Form.** Update your W-4 form to reflect the new exemption.
- **Update Your Flexible Spending Accounts (FSA).** There will be additional medical expenses. To keep the after-tax costs down, pay for them through your FSA.

**Life Event 5: Inheritances, Bonuses, or Unexpected Money**

An unexpected windfall can go a long way toward helping you reach your goals if you make it part of your financial plan.

**Step 1: Examine the Priority of Your Goals** This windfall affords you the opportunity to achieve goals that might have been out of reach.

**Step 2: Reexamine Your Goals** Take a look at your goals and determine which ones are most important. This extra money might mean that the timeline for achieving certain goals has changed. You might be able to move to a larger house, invest in retirement property, or pay off a certain debt now. Once you’ve done this it will become easier not to spend your windfall, but to save it instead.

**Step 3: Consider Estate Planning** If your estate is large, you may want control over how your assets are passed on to inheritors—that would be the job of estate planning.

- **Transfer of Your Estate.** Through careful estate planning you will be able to control the transfer of your estate. For example, you might have a child who has special needs, or you might not want your children to have access to their inheritance until they are a certain age.

**Step 4: Examine the Tax Implications** Depending upon how large your windfall is and how you obtain it, there may be tax implications. For example, a bonus or winning a prize on a TV show will generate taxes; however, an inheritance won’t.

- **Plan for Tax Implications.** If there are tax implications associated with your windfall, make sure they are incorporated into your budget.
- **Consider Estate Taxes.** While estate taxes are at present a moving target, if your estate is now of a size that it might be impacted by them, take steps to minimize them.

**Life Event 6: A Major Illness**

It can happen to anyone—in fact, most of us know someone who has had to face the news of a major illness. The impact is twofold—first, the devastating news, then the
financial impact. If you ever have to face such a tragedy, you’ll want to make sure the financial impact is as controlled as possible, thereby allowing you to focus on the healing aspect.

**Step 1: Reexamine Your Finances**  Reexamine your needs and goals in light of the future medical and rehabilitation costs, and changes in your future earning potential.

- *Assess Your Current Financial Situation.* Begin by taking a careful look at where you are now.
- *Emergency Fund—Adequate Liquidity.* This is the time to tap into your emergency fund. Make sure you have adequate liquid funds available.
- *Reexamine Financial Goals.* Depending upon the prospects and challenges you face, you may need to revise your financial goals to deal with the future.
- *Reexamine Your Investment Strategy.* Your working time horizon may be shortened—for example, you may now expect to work 5 instead of 15 years. Since you may be tapping into your retirement savings earlier than expected, you may need to change your asset allocation to reflect your shorter investment time horizon.
- *Revise Your Budget.* Your budget needs to reflect the new expenses you are experiencing and your redefined financial goals.

**Step 2: Take Advantage of Tax Breaks**  With an increase in medical expenses, there may be an accompanying increase in tax deductions. Make sure you take advantage of any tax breaks that might come your way.

- *Understand the Tax Implications.* Fortunately, there are tax deductions associated with medical expenses and co-pays. Get a copy of IRS Publication 502, which outlines what expenses qualify.
- *Explore Flexible Spending Accounts (FSAs).* Contact your employee benefits department at work and find out if your employer offers flexible spending accounts—if so, open one. Talk to your doctor to get an idea of what the out-of-pocket expenses might be.

**Step 3: Alternatives to Finance Your Illness**  Depending upon your diagnosis, you may want to consider tapping into your home equity or cash-value life insurance policy. If coming up with additional funds is a matter of life and death, it’s something you’ve got to do.

- *Reverse Mortgage.* To qualify for a reverse mortgage, you must be at least 62. With a reverse mortgage, you maintain ownership of your home, just as you would with a normal mortgage. You pay your real estate taxes and homeowner’s insurance and maintain your home just as before. Of course, you’ve got to remember that with a reverse mortgage you won’t be leaving the house to your kids—instead, it will be left to the bank.
- *Life Insurance.* If you are lucky enough to have a cash-value life insurance policy, you might consider taking a cash-surrender loan, which doesn’t have to be paid back. With a cash-value loan you are borrowing against the cash value of the policy, which is the dollar amount that you would be paid if you canceled the policy. Should the diagnosis be terminal, and your policy includes a living benefits clause, you can access part of the policy proceeds to supplement your budget, with the balance of the policy paid to your beneficiary.
Disability Insurance. Depending on your insurance coverage, short- or long-term disability benefits may be available should you be unable to return to work.

Life Event 7: Caring for an Elderly Parent

Complicated emotional and financial issues can arise as you reach out to help elderly parents. Finding the right solutions takes positive and clear thinking and, as with all of the areas we have looked at, works best with a plan.

Step 1: Health Care and Estate Planning Concerns

- **Initiate a Dialogue with Your Parents.** While this may be an uncomfortable discussion, it is one that can prevent a great deal of pain later, allowing family members to express their personal needs and wishes.

Step 2: Oversee Your Parents’ Financial Affairs

- **Make sure your parents’ financial affairs are managed in the same general way you are managing your own.** All of these actions are aimed at making sure your parents’ interests and desires become part of their financial plans.
- **Organize the Paperwork.** Know where financial documents are kept.
- **Gain an Understanding of Their Goals and Budget.** Discuss financial goals with your parents. Make sure they are receiving all the benefits in terms of pensions and Social Security to which they are entitled.
- **Develop a Budget.** Help your parents put together a budget.
- **Protect Your Parents.** Make sure your parents have their wishes expressed with a health care proxy. Also make sure they do not give out any financial information to anyone calling on the phone.
- **Durable Power of Attorney.** Try to have your parents look ahead to when they may no longer be able to manage their financial affairs.

Step 3: Discuss Long-Term Health Care Options

- **Make sure your parents are aware of the options and costs of long-term health care, although this may be prohibitively expensive, depending upon their age.**
- **Long-Term Health Care Insurance.** Depending upon their total assets, if they have more than $150,000 but less than $450,000 in retirement assets, including their home, they may want to purchase long-term health care insurance.

Step 4: Estate Planning

- **Discuss Estate Planning.** Depending upon the size of your parents’ estate, you may want to preserve their estate through estate planning.
- **Discuss Estate Planning.** Discuss any appropriate estate planning options with your parents. A good estate planning attorney will help them to preserve their assets by reducing estate taxes. If the estate is large enough, gifts of money or other assets may be recommended. To avoid future family conflicts, help them and other family members to resolve any questions about the gifting of personal property, such as furniture, china, tools, or jewelry.

Life Event 8: Retiring

While it may seem like it will never happen, there will be a time when you retire. Just as with everything else in life, the only way it will happen successfully is if
it is planned. Retirement means that you’ll be living off any income you continue to have, your personal savings, your pension (if you have one) or other employer-provided retirement plans, and Social Security (if available).

**Step 1: Develop a Retirement Income Plan** If you want retirement to be successful, you’ll need to prepare and plan.

- **Mental Preparation.** Retirement not only brings on the loss of a paycheck, it also brings on tremendous lifestyle changes. Your routine, your working identity, and your social relationships will all change as you leave your professional life. Being psychologically prepared for retirement can be just as important as being financially prepared.
- **Financial Preparation.** Make sure you have enough money saved to fund your retirement lifestyle and continue to monitor your asset allocation and earnings.
- **Plan How You Will Use Your Retirement Savings.** A well thought out plan will help you make decisions as to when to tap into different retirement plans, for example, any 401(k)s, 403(b)s, and 457(b)s that you might have, as well as your Roth or traditional IRA. Rules regarding distribution and taxation vary for different accounts, so use the rules to your advantage or seek professional help.

**Step 2: Manage Your Income in Retirement** Develop a plan for managing your money during retirement. Carefully consider the kind of lifestyle you currently have and the kind of lifestyle you wish to have during your retirement years.

- **Withdrawal Strategy.** Establish an appropriate withdrawal strategy to help ensure that your assets last your lifetime—and keep taxes to a minimum.
- **Monitoring Your Investments.** Develop an income management strategy to monitor your plan to stay on track for the retirement you envision.
- **Emergency Fund.** Always have an emergency fund—plan for the unexpected.

**Step 3: Review Your Insurance Coverage and Your Will** The loss or reduction of your retirement income could adversely affect your surviving spouse or family members. Life insurance can provide financial resources they will need during a difficult time.

- **Employer Retiree Health Care.** Contact your firm’s benefits office and investigate the retiree health care options.
- **Medicare.** Examine Medicare coverage and requirements and see how this fits in with your employer retiree health care coverage.
- **Medicare Supplemental Insurance.** Find out what is available in terms of coverage and costs from Medicare supplemental insurance.
- **Long-Term Health Care Insurance.** Investigate the costs and benefits of long-term health care insurance and make a decision. If you wait too long, the cost of long-term health care will become prohibitive.
- **Homeowner’s Insurance.** Many individuals ignore their homeowner’s insurance once it is purchased. Retirement provides a convenient time to revisit your policy and make sure that your coverage is adequate.
- **Review Your Will.** Regardless of your level of assets, ensure that they will be used to help the people and organizations that are most important to you.

**Step 4: Keep Track of Important Retirement Planning Dates** Financial milestones abound as you approach retirement. Keep a close watch on these dates:
Life Event 9: Death of a Spouse

The loss of a spouse has substantial financial effects. You need to review your financial plans and the financial plans of your spouse to make sure that the assets are distributed properly.

Step 1: Organize Financial Material  Organization is the key.

- Assemble the Papers. Collect the papers necessary to file for benefits and finalize the estate including at least ten certified death certificates, insurance policies, Social Security numbers, military discharge papers, marriage certificate, birth certificates of dependents, the will, and a list of assets.
- The Will. If there is a will, locate it. This will represent the first step in distributing the assets.

Step 2: Contact Sources of Survivor Benefits  Make sure you receive any benefits to which you are entitled.

- Insurers. Contact any insurers who have issued policies to the deceased.
- Social Security. Contact your local Social Security office to determine if the deceased was eligible for benefits, and keep in mind that there is both a death benefit and survivor’s benefits from Social Security. Also, contact the regional Department of Veterans’ Affairs if your loved one was a veteran.
- Past Employers. You may be entitled to employee benefits from the deceased’s employer or past employer—these may include a paycheck for vacation or sick pay, pension payments, or proceeds from an employer-issued life insurance policy.
Step 3: If You Are the Executor, Carry Out Your Responsibilities  If you are the executor, you are responsible for overseeing the estate and managing it through probate, making sure expenses and taxes are paid, and satisfying any financial obligations that might exist.

- **Distribution of Assets.** If your loved one dies without a will, state laws will dictate how his or her assets will be distributed. Contact an attorney or the probate court in the community for more information.

Step 4: Change Ownership or Title to Assets  Make sure that ownership or title to assets is changed.

- **Insurance Policies.** You may have to change beneficiaries.
- **Automobiles.** The titles may need to be changed.
- **Bank Accounts, Stocks, Bonds, and Safety Deposit Boxes.** To change the title on stocks or bonds, contact your broker (if applicable) or the company, mutual fund, or other financial services company that issued the product.
- **Credit Cards.** Notify the credit card company of the death and ask that the card be listed in your name only, or that the account be closed.

Step 5: Review Your Financial and Retirement Needs  With the loss of a spouse, your financial needs will change. You’ll want to:

- **Determine If Your Benefits Change.** If your spouse is covered by a pension, your future benefits may change as a result of his or her death.
- **Contact the Employer.** You should contact your spouse’s employer and find out whether you are due any benefits.
- **Review Your Insurance.** You may no longer need to have the same level of insurance if you do not have dependents.
- **Review Your Medical Insurance.** If your medical insurance was through your spouse, you will need to make sure you continue to be covered. You may want to continue coverage under COBRA or you may find it better to purchase your own insurance.

Life Event 10: Divorce

With over 40 percent of all first marriages ending in divorce, this is a life event that affects many of us. Not only are money problems the major cause of divorce, but divorce usually leads to reduced income and the burden of expenses that were formerly shared. Moreover, the financial impact of divorce is many times compounded by the cost of the divorce itself. If you have to experience this life event, there are a number of steps you can take to lessen its financial impact.

Step 1: Prepare for Divorce  The best way to lessen the financial impact of a divorce is to prepare for it.

- **Pay Down Debt.** Dividing assets is tough enough, try not to have much debt to divide.
- **Keep the Costs Down.** The nastier the divorce, the more the cost—keep things as civil as possible.
- **Remember Principle 1: The Best Protection Is Knowledge.** Protect yourself—seek help from a financial planner specializing in divorce if you need advice.
Step 2: Avoid Credit Damage  Many times credit scores go down during a divorce; you’ll want to avoid this if possible. Starting over financially is difficult enough without adding to it.

- **Joint Accounts.** Having the divorce finalized isn’t enough to separate accounts that remain open in both names; you’ll have to take care of that. You may not feel financially responsible for these accounts, but monitoring them to make sure payments are made will be in your best interest. Consider options for paying the balance on accounts and opening new individual accounts. Recognize that joint accounts will still be reported on your credit history, so getting them closed will protect your future score and access to credit.

- **Late Payments and Your Credit Report.** If late payments occur, add a note to your credit report explaining why it occurred—all three credit bureaus allow you to add a 100 word note at the end of your credit report.

- **Late Payments? Have Your Accounts “Re-Aged.”** Once you have your finances under control, contact your creditors to see if they would be willing to “re-age” your accounts, listing your accounts as current and erasing late payments from your file.

Step 3: Revisit Your Financial Goals  Divorce may alter your financial goals and your ability to reach them. Take another look at your financial goals and put a new plan in place.

- **Reevaluate Your Goals.** Take another look at your financial goals and put together a new plan to reach them.

- **Social Security and Your Ex-Spouse’s Earnings History.** If your marriage lasted 10 years and you didn’t remarry, you may be entitled to Social Security benefits based upon your ex-spouse’s earnings, even including earnings after the divorce. Make sure you get the benefits to which you’re entitled.

Step 4: Reexamine Your Insurance Coverage  Make sure you have adequate insurance coverage—health, life, auto, and property insurance.

- **Insurance Coverage.** If you have been covered under your ex-spouse’s policy, make sure coverage continues for you and your children. Either get coverage on your own, or keep your coverage under COBRA.

- **Child Support or Alimony—Check Out Life Insurance.** You might want a policy in your ex-spouse’s name to cover these costs in case your ex-spouse dies. And don’t forget the tax implications of paying or receiving alimony.

- **Your Life Insurance Policy.** Carefully review your life insurance policy (i.e., name, beneficiaries, and amounts). There may be changes you should make.

Step 5: Rework Your Budget  A new budget should accompany your new lifestyle.

- **Your Budget.** Rework your budget to reflect your new income and the burden of expenses that were formerly shared.

- **Retirement Savings.** With divorce, many individuals put retirement savings on the back burner and focus on taking care of more immediate needs—try not to fall into this trap. Retirement is going to come someday, like it or not.

- **Reexamine Your Expenses.** For example, don’t keep the house if you can’t afford it.
**Emergency Fund.** When you’re on your own, you no longer have a partner to rely on if you run into financial trouble, which makes having an emergency fund even more important.

**Tax Breaks.** Your loss of income may qualify you for tax breaks to which you weren’t previously entitled. Your filing status and standard deduction will change, as may your right to claim your child as an exemption, depending on the divorce decree—so plan accordingly.

---

### The Keys to Success: A Dozen Decisions

In building wealth you’ll face a number of different hurdles and decisions—some of them financial and some of them lifestyle. Even worse, you’ll make some of these decisions without even knowing it. What we’ll do now is take a look at them and try to understand their ramifications.

**Number 1: Become Knowledgeable**

Armed with an understanding of the basics of personal finance, it becomes much easier to avoid financial pitfalls and bad advice—remember **Principle 1: The Best Protection Is Knowledge.** In fact, you’ll find the ability to evaluate financial advice and make good financial decisions invaluable. Unfortunately, managing their personal finances is one of the few things people seem willing to do without an understanding of what they’re doing. Certainly, no one would attempt a heart bypass if they didn’t know what they were facing, but when it comes to personal finance and investing, too many people are willing to take a stab at it even though they don’t have the slightest idea what they’re doing. The results are generally sad: Often that lack of knowledge attracts the unethical and incompetent characters who loiter wherever money is present.

Knowledge will keep you from falling prey to those who are always willing to help you with (or help themselves to) your money. In addition, knowledge will spur on your commitment to personal finance. When you understand the concepts of the time value of money and stock valuation, you gain an appreciation for starting your financial plan early in life, and that appreciation leads to action. An understanding of personal finance also gives you the ability to handle those unwanted financial surprises that are all too frequent in life. In short, knowledge will keep you out of financial trouble because, as we all know, it’s a lot easier to do things right if you understand what you’re doing.

**Number 2: Don’t Procrastinate**

Remember **Principle 9: Mind Games, Your Financial Personality, and Your Money;** the biggest threat to your financial future comes from within. Although bad advice can slow your financial progress, procrastination stops it. Unfortunately, very few things are more natural than procrastination. In fact, you’re probably pretty good at it already. Postponing that term paper really didn’t hurt you; after all, as long as you handed it in on time, it didn’t matter. As you should know by now, it’s not the same with personal finance: There’s a big difference in whether you invest $2,000 for retirement now or the day before you retire.

Still, it’s awfully easy to put off facing your financial future. If you aren’t married, you may be keeping your life on hold, waiting for that special person to make financial sacrifices with. Or when you graduate you may think you deserve a break from “student poverty.” Or you may just think there’s no sense saving now, when in the future you’ll earn a lot more and saving will be a lot easier.
Unfortunately, there’s always a reason to put it off. But while you may feel you aren’t earning enough money right now, wait until you get married and have kids. How about adding those home mortgage payments into the mix? And just when you think you’ve made it out of the woods, paying for college will be staring you in the face.

The bottom line is that your financial future starts now. You know enough about the time value of money to realize that procrastination will only make your future work a lot harder. As the Rolling Stones sang, “Time is on my side.” With personal finance, there is no truer statement. Remember Principle 10: Just Do It!

Number 3: Live Below Your Means

You always hear people saying, “We don’t spend money on anything extravagant, but we just can’t seem to get ahead.” The answer to their problem is uncomfortably simple: You can’t save money unless you spend less than you earn. The problem is that people tend to spend to their level of earning, and in many cases, beyond. Unfortunately, our culture makes that natural. For many people, “you are what you buy.” Their image comes from the car they drive, the labels on their clothes, and the wine they drink. It seems many people think if they earn a certain amount of money, they should live and look a certain way. Even worse, shopping has gone from a chore to a hobby for some, and to a lifestyle for others. The result is regardless of how much you make, it all goes toward the necessities of life—the more you make, the more necessities there are.

How do you get out of this trap? The answer is you’ve got to change your attitude toward spending. You’ve got to be realistic with respect to what you can really afford. This all flows from a basic truth: You can’t have it all; you have to make choices. The place to start is to track your spending. Once you see what you’re spending, you’ll also see what you can cut. For example, that morning USA Today, cinnamon scone, and large cappuccino that you pick up on the way to work may cost you $6.75 a day. If there are 22 work days in a month, say goodbye to $148.50 each month and $1,782.00 over the year. And even worse, before you spent it, there were taxes. If you’re in the 25 percent marginal tax bracket, that means you needed to earn $2,376 (that is, $1,782/(1 – 0.25]) to cover your morning fix on the way to work. Cutting out the nonnecessities will allow you to make savings automatic.

Number 4: Realize You Aren’t Indestructible

You’re young, you’re healthy, and the mere fact you can eat dorm food and live means you’re indestructible. That doesn’t mean your TV might not fail you, or your car might not meet an untimely death. So make sure you have an emergency fund.

Now let’s look at insurance. If you’re single and don’t have any dependents, you probably don’t need any life insurance. In fact, you can take a look at Table 9.1 to see whether or not you need any. If you need it, keep your costs down by shopping for term insurance on the Internet, and when there’s a major change in your life, such as the birth of children, review your coverage. As for health insurance, let’s face it, you need it, and let’s face it, it’s

FACTS of LIFE

If you aren’t making the financial progress you want, challenge yourself to understand why.

STOP THINK

If you ever saw the movie Willie Wonka and the Chocolate Factory, or read the book Charlie and the Chocolate Factory, on which the movie is based, you’ll remember a little girl named Veruca Salt. She was a nasty piece of work. She constantly demanded things, screaming “I WANT IT NOW!” Her desires and the way she acted were clearly out of control. She didn’t make it through the story—but if she had, with that attitude her financial future would not have been very bright. There’s no easier way to foil a financial plan than with a lack of control and impulse buying. Control is crucial. Can you think of any impulse purchases you’ve made?
expensive. Hopefully, your job will provide you with adequate coverage. In fact, when you’re job hunting, make sure you look very closely at the health care benefits.

OK, you’ve got your life and health insurance, are you ready for action? The answer is no. Consider this fact: If you’re under 35, there is a 65 percent chance that an accident or long-term illness will keep you out of work for a minimum of 6 months. Moreover, about half of all mortgage foreclosures come as a result of insufficient disability insurance. That’s because while you’re down, your bills won’t stop, and Social Security won’t kick in unless the illness is terminal or you’re disabled for at least a year. In fact, Social Security’s rules are so restrictive that you might not get any help from it. That means you’ve got to protect yourself. Where do you start? Check your company’s disability coverage. If your company provides it, make sure it’s enough. If not, find a personal policy and get covered.

Is that it? Heck no! The most important thing you can do is recognize that you aren’t indestructible. Lead a healthy lifestyle. That means have regular checkups, don’t smoke, exercise regularly, eat healthy, keep your stress level down, become a defensive driver, and avoid excessive alcohol consumption. The bottom line is that a healthy lifestyle will save you a good deal of money.

Number 5: Protect Your Stuff (and Look Out for Lawyers)

Having home and auto insurance is something of a no-brainer: You need it, assuming you have a home and a car. Fortunately, there are ways to keep the cost down. The key is to keep your deductibles as high as you can afford. After that, go for as many discounts as you can. Keep in mind, insurance isn’t a maintenance plan, it’s protection against major financial disasters.

As you look at your auto insurance policy, take a good look at the level of liability insurance. Given the level of jury awards given to auto fatalities, you’re probably underinsured. If you’re driving and someone is injured, you could be facing financial ruin. Remember, the liability coverage on your auto liability insurance generally is only $50,000, while the median jury award for traffic fatalities runs above $500,000.

What happens if you’re driving and your cute little dog Pooksie jumps on your lap and you lose control of your car and hit someone? Your insurance company will pay the cost to defend you and Pooksie in court and pay damage awards, but only up to the policy limit. All this means that going for “the minimum I need” may set you up for a financial disaster. You need more than the minimum level of coverage, and one way to afford it is to raise your deductible. That also means you may need a larger emergency fund in the case of an accident. An alternative approach is to give some serious thought to a personal umbrella policy. The bottom line here is to make sure your insurance actually protects you from financial ruin.

Number 6: Embrace the “B” Word (Budget)

When most people think of a budget they think of a financial strait jacket, something that takes all the spontaneity out of life. After all, your “20-something” years are supposed to be a “live for the moment” time. In reality, a budget is a means to reach your goals. If it makes you feel too much like your folks to think about sticking to a budget, think of it as a “cash flow plan.”

Unfortunately, the thought of a budget doesn’t excite many people, so the best thing to do is make it as easy on yourself as possible. Probably the easiest way to do this and actually make the budgeting process successful is through the use of an online budget, and Mint.com is one of the best. Mint.com calculates your average spending in different categories that you can use to create a budget based on your historical spending patterns. In addition, it shows you how your spending decisions impact how much you have left at the end of the month. You can also get a free app for Mint.com that allows you to check your budget in addition to sending you e-mail
or text alerts when you go over budget. If you check out Figure 2.8 you’ll find a short write-up on all the features of Mint.com and also of Geezeo, which is also an online budgeting tool.

What does a budget (or cash flow plan) do for you? It forces you to use restraint, to think about what you spend money on, to live below your means, and (yes) to be frugal. For example, if you’ve already spent this month’s budgeted amount on restaurants, you’ll have to save up money, perhaps from passing on that new Led Zeppelin reunion CD, if you want to eat out. Unfortunately, self-restraint is tough, especially given all those advertisers with their sights on your money bombarding you from TV, the Internet, the radio, newspapers, and magazines.

Without a budget, your financial future is bleak at best. Sticking with a budget, you’ll avoid the nightmares financial chaos brings and be able to save.

Before you can put a budget or cash flow plan in place, you’ve got to find out where your money is going. To do that, you’ll want to track your expenses carefully for a month. To help you with this, take a look at Worksheet 7, “The Budget Tracker.” You’ll also want to go back to Chapter 2 and review the sections titled “Developing a Cash Budget” and “Implementing the Cash Budget.” You’ll find that while you’re setting up your budget, you’ll be able to identify expenses you can eliminate. Also, make sure your savings are automatically deposited in a mutual fund or other investment so you don’t have a chance to get to that money.

Number 7: Reinvent and Upgrade Your Skills

There was a time when the first job you took would be your job for life. You’d stick with that company for 30 or 40 years, collect a gold watch, and retire. Welcome to the new world—the world of downsizing, restructuring, reorganizing—all words that mean you’re gone. In today’s world it doesn’t matter that you’ve been a loyal employee for 20 years and it doesn’t matter that you come in early and leave late. What matters are your skills: Are they needed? What do they bring to the company? Your history with the company is irrelevant; the real question is, what do you add to the company today? Sounds pretty cold, doesn’t it? Well, it is, but that’s how the business world works today. Nothing is long-term. If a company needs your skills and talents, you’re in good shape. If not, you’re out.

The question is, how do you prepare for this kind of job insecurity? The answer is to make sure your skills and talents are needed. That means you’ll want skills that are both valuable and that can’t be acquired with little or no effort. You’ll also want to take some care in picking a career. You want to have a skill businesses are willing to pay for. Maybe that skill is being a CPA, or having a unique computer skill, or more advanced building construction skills. How do you keep your skill level both valuable and unique? The answer is to continuously reinvent and upgrade your skills through education. The education you’re getting right now will prepare you for a job when you graduate, but it won’t be enough to keep that job for life. Given the pace of innovation, no one can stand still and expect to survive. Let there be no doubt, education is the best investment you’ll ever make.

Number 8: Hide Your Plastic

There probably isn’t a more dangerous threat to your financial well-being than credit cards. The real problem is that there’s no real problem with credit cards, just with credit card debt. Unfortunately, for most people these two go hand in hand, especially if you’re a student with lots of needs but no real income. It would seem that

FACTS of LIFE
In 2011, the average family with a high school student attending the prom will spend $807. Interestingly, the amount of money spent on the prom varies by region, with southern families spending the least, only $542, and those in western states spending the most, $1,073.
college students would be the last people credit card issuers would want to tap—after all, given their income they can’t be great credit risks.

But that is far from the case. Credit card companies set up tables on campus and bribe students into filling out an application with offers of free Frisbees, calling cards, and other goodies. And it works. In fact, one-fifth of all college students have four or more cards. With credit cards in hand, it simply becomes too easy to spend money—that pizza late at night, or those “must-have” tickets to the Rolling Stones 50th Anniversary Tour. People simply spend more with credit cards—about 30 percent more—than they do with cash. For students, it’s particularly tempting to use credit cards. After all, you’ll be earning the big bucks in a few years, so paying them off shouldn’t be any problem . . . should it? The average undergraduate accumulates about $2,169 in credit card debt by the time he or she leaves school; and for those 27 percent of undergrads who use credit cards to help finance part of their education costs the median balance is around $3,400. Even worse, 21 percent of undergraduates have credit card debt between $3,000 and $7,000.

The only real answer is restraint. Don’t use credit cards except for emergencies, and then use them with the utmost restraint. Your goal should be to make it into the next stage of your financial life (that stage where you make money) with as little debt as possible. When you get there, credit cards are great, but make sure you pay them off every month. If not, take the scissors to them.

**Number 9: Stocks Are Risky, but Not as Risky as Not Investing in Them**

Stocks are risky. If you didn’t learn that in Chapter 13, you probably learned it by listening to stories on the nightly news describing the recent wild market gyrations. Should you put your money in these risky investments? If your investment horizon is long, the answer is yes, but you’ll want to eliminate as much risk as you can through diversification. One easy way to do this is through a stock index mutual fund. If all this talk of investing in stocks gives you heart palpitations, go back to Chapter 11 and take another look at the section called “The Time Dimension of Investing and Asset Allocation.” As long as your investment time horizon is long, stocks are prudent.

If the risk of stock price fluctuations is not your biggest fear, what is? The fear of not keeping up with inflation and taxes. In effect, it is the fear that you won’t earn enough on your investments to meet your goals. Just look at a 3 percent rate of inflation. After 23 years you’ve lost half your purchasing power, and if the inflation rate is 4 percent, it will take less than 18 years. In fact, as shown in Figure 18.1, over the last 60 years from 1951 to the beginning of 2011 the annual rate of inflation has been over 3.7 percent. Given the very low average annual return on Treasury bills, only 4.75 percent, you can see that most of those returns are taken up by inflation. Throw in taxes and things get even worse. What does all this mean? If you don’t take some prudent risks, you don’t have a chance of meeting your goals.

**Number 10: Exploit Tax-Favored Retirement Plans to the Fullest**

If you’re lucky, you’ll get a chance to participate in the best investment (aside from education) around. What is it? It’s a tax-deductible contribution to an employer’s retirement saving plan with a matching contribution from the employer. Why is it so great? Because your contributions aren’t taxed, that means you can contribute money that would have otherwise gone to the IRS. In addition, because the investment earnings aren’t taxed until they’re withdrawn, you earn money on earnings that the IRS would have collected. While you’re doing all this, don’t forget to take full advantage of a Roth or traditional IRA.
What should be your strategy? When you get out in the real world, max out on these tax-favored retirement plans. If you aren’t sure this is the right approach, go back to Chapter 16 and reread the section called “What Plan Is Best for You?” If that doesn’t convince you, read it again until you are convinced.

**Number 11: Plan for the Number of Children You Want**

Children can be wonderful, but they are expensive. At one time, children were money in the bank. When they were young, they worked the farms or in the family business, and when you got old, your children were there to take care of you. In short, a great deal. Times have changed, to say the least. This doesn’t mean you shouldn’t have as many children as you want, but you should be aware of the costs involved.

**Number 12: Stay Married**

Divorce is expensive, really expensive. An amicable divorce runs in excess of $1,000 while an unfriendly one can easily hit $10,000 and up with no limit. But it isn’t just the cost of divorce that makes it in your best financial interests to stay married, it’s also the fact that married people tend to earn more money and accumulate more wealth than single people living separately or together. The statistics are convincing: Married men earn 26 percent more than unmarried men, and married couples earn 61 percent more than families headed by single men. For divorced women with children, the tale is the saddest: Their income is only about 40 percent of that of a married couple. Clearly, for women with children, divorce opens the doors to poverty.

Why do married couples do better financially? One reason is that the cooperation learned in a successful marriage can translate into a career advantage. In addition, a successful marriage requires money management and budgeting. Unnecessary expenditures are eliminated, and you now have someone to answer to when you spend $1,400 for an autographed picture of the Three Stooges on eBay. On top of all this, being single is expensive. Most people spend a lot of time and money searching for that right person. What does all this mean? You should take real care in picking a spouse, and once you’re married, put serious effort into making your marriage work. It also

**FACTS of LIFE**

Divorce is expensive! Just look at the Paul McCartney–Heather Mills divorce—after 5 years of marriage, he paid her $49 million. If you look at this cost on a per day basis, it runs to $26,849 per day, not counting attorney’s fees and court costs—that’s a mighty expensive divorce.

---

**FIGURE 18.1 Average Annual Returns Before and After Inflation from 1951 to the Beginning of 2011**

<table>
<thead>
<tr>
<th></th>
<th>Average Annual Return Before Inflation</th>
<th>Average Annual Return After Inflation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stocks</td>
<td>12.3%</td>
<td>8.6%</td>
</tr>
<tr>
<td>Long-Term Bonds</td>
<td>6.6%</td>
<td>2.9%</td>
</tr>
<tr>
<td>T-Bills</td>
<td>4.8%</td>
<td>1.0%</td>
</tr>
</tbody>
</table>

**Average Annual Returns**

- **Before Inflation:**
  - Stocks: 12.3%
  - Long-Term Bonds: 6.6%
  - T-Bills: 4.8%

- **After Inflation:**
  - Stocks: 8.6%
  - Long-Term Bonds: 2.9%
  - T-Bills: 1.0%

**Average Annual Returns from 1951 to the Beginning of 2011**
Part 5 • Life Cycle Issues

**Getting Started: Just Do It**

It’s now time to put things together and begin to build your financial future. Let’s put some of the concepts we’ve examined in the previous chapters to work. And if all this has made your head spin, this section will give you enough direction to get going.

If you’re having second thoughts about starting, just look back a bit in this chapter at the section titled “Number 2: Don’t Procrastinate.” Starting your plan today may be the most important financial decision you’ll ever make.

Begin with budgeting and planning. Figure 1.1 gives an outline of this process. Find out where you stand, define your goals, develop a plan, and revise the plan as your life changes. This means putting together a balance sheet, income statement, ratio analysis, record-keeping system, and a budget. You’ll want to rely heavily on Chapter 2 for this.

You’ll also want to pay close attention to managing your cash—things like controlling banking fees and ATM charges. It also means making sure you have the necessary emergency funds. Chapter 5 should help here.

---

**MONEY MATTERS**

Tips from Marcy Furney, ChFC, Certified Financial Planner™

**TAKE MY ADVICE**

I have borrowed some advice from *The Parenting Handbook* (there must be one because all parents say the same thing), which surprisingly may be applicable to our financial world. Though we may wish to consider personal finance a deep and intricate subject, handling money may be as simple as living life like a kid who actually listened to his or her parents.

“Here’s your allowance. When it’s gone, you will have to live without until next week.” Because it’s pretty hard to get a loan or credit card as a kid, “learning to live without” is a brutal reality. Identifying needs versus wants, prioritizing them, and living below your means are the keys.

“I guess if Patty jumped off a cliff, you would, too.” Following the pack can lead to disastrous investment decisions, tremendous debt, low self-esteem, and generally poor financial health. Making informed decisions and focusing on personal goals, rather than trying to buy status and happiness or conform to the ideal of the hour, are the ingredients of good personal finance.

“Do your homework before you go out to play.” You should investigate and be informed before you make any major financial decision. Also, you’ve got to do the things without a lot of glamour, such as saving for that distant retirement or “doing homework,” before you spend time and money on the things that bring immediate gratification.

“If you keep crossing your eyes, they’ll stay that way.” Successful money management is a habit. If you develop a habit of using credit as a safety net for overspending, there is no quick fix. Just proclaiming your goals won’t make them happen. The continuous positive movement toward them with tried and proven methods results in accomplishment.

“Wear clean underwear in case you have a wreck.” Though I could never exactly reconcile this one, I take poetic license here to interpret it as a warning to be prepared. A financially sound lifestyle includes purchasing insurance to handle those catastrophes you can’t just cover with savings. Of course, Mom didn’t say to “wear your best underwear,” so I’ll stretch it even further to mean you shouldn’t waste money by overinsuring or covering things you can handle on your own.

“Do it by yourself.” Especially with women, the development of financial autonomy is important. If you are married, knowledge and input from both parties are essential. If you are single, cut the apron strings, and learn to make decisions on your own. Depending on a parent or spouse to handle your finances can result in you being without a resource at the very time you need it most—at the death of a parent or departure of a spouse.

means you shouldn’t have children if you aren’t married—no two ways about it. Things don’t always turn out as planned, but if you don’t plan, they never turn out.
Rid yourself of "bad" debt. If you’ve got it, get rid of it. If you don’t have it, avoid it. You might want to review the section on “Tying Things Together: Debt and the Real World” in Chapter 8, along with the material in Chapters 6 and 7.

Your safety net—your life, health, disability, property, and liability insurance—should be in order. Chapters 9 and 10 should help you with this.

It’s also time to start investing. Try stocks and mutual funds. You’ll find that success breeds an enthusiasm for investing (and saving) that simply cannot be explained in a text. You’ll want to keep your attention focused on taxes—take advantage of any tax-favored plans like IRAs and 401(k)s available to you. You’ll want to begin thinking about, and planning for, retirement—it simply is never too soon, at least if you want to enjoy retirement. You’ll find help with this in Chapters 3 and 4, and Chapter 11 through Chapter 18. You don’t have to know everything about investing to get started. In fact, right now, if you’ve gotten this far in this class, you’re well ahead of most people when they begin investing.

Still, nothing in this book will be of help to you if you procrastinate. That means follow Principle 10: Just Do It!

Summary

1. Understand the importance of beginning your financial planning early.
   There is no substitute for starting early when it comes to financial planning and saving.

2. Recognize the “10 Financial Life Events” and strategies to deal with them.
   Marriage and children further complicate planning for your financial future. The key to controlling financial problems before you marry is an open and frank discussion about money with your partner. The goal is to find out your partner’s financial history, habits, and goals. You can also take the financial pain out of having children by planning ahead of time.

3. Understand and manage the keys to financial success.
   As for becoming rich, the one common trait seems to be frugality. Several key decisions in life will determine how your financial future turns out. You’ll want to gain an understanding of personal finance; avoid procrastination; live below your means; have adequate life, health, property, and liability insurance; become an active budgeter; keep your skills fresh; avoid credit card debt; take some prudent risks with your long-term investments; max out on tax-favored retirement plans; understand that children are expensive and plan accordingly; and stay married.

Review Questions

1. Name ten critical strategies for personal finance success.
2. Why are the financial decisions during the first 10 years of getting started so important? Name five financial decisions that are typically made during this period.
3. List the four steps critical to financial success when planning for the life event “getting started.” Explain how the warning “don’t procrastinate” applies to each step. In your answer include how often your financial goals should be reviewed.
4. What factors should a married couple consider when choosing to have one or more checking accounts? Credit card accounts?
5. Most of the financial life events represent the “typical” progression through the life cycle. Other events, such as receiving unexpected money, or experiencing a major illness or divorce, occur more randomly. For one of these three, review the planning steps for coping with this life event.
6. List five financial planning issues that parents should address when they are expecting a child. Briefly explain why each issue is important.
7. Caring for an elderly parent, retiring, or the death of spouse can have a major impact on an individual’s daily life as well as on his or her finances. For one of these three events, review the planning steps for coping with it.
8. Financial preparation for at least five of the life events mentions establishing an emergency fund. List the five. In your opinion, an emergency fund would be critical for which of the remaining life events? Why?
9. List and briefly describe the 12 basic decisions you must make in order to achieve real wealth.
10. Name five strategies to help you compensate for one reality of life—“no one is indestructible.” How does this life reality relate to Principle 7: Protect Yourself Against Major Catastrophes?
11. Identify four ways a simple budget, or cash flow plan, can help you achieve wealth.
12. Why are equities a prudent investment strategy for accomplishing future goals? Be sure to consider the effects of taxes and inflation.
13. What might be described as the “best” investment (aside from education)? Explain why you should take full advantage of any tax-favored investment alternatives available to you.
14. Name two social trends that reflect the role of debt in American society. What factors contribute to these trends?
15. Why does financial planning require a “call to action”?

Develop Your Skills—Problems and Activities

These problems are available in MyFinanceLab.

1. Calculate the future value of an account after you’ve contributed $1,000 at the end of each year for 40 years assuming you can earn 9 percent compounded annually, and that you don’t make a withdrawal during the 40-year period. Now calculate the value of the same account if you stop making contributions after 30 years. What does this tell you about the power of time when trying to accumulate wealth? (Hint: This problem can be solved using a financial calculator as discussed in Chapter 3 or the Money in Motion calculator, which is available in MyFinanceLab.)
2. Why do insurance products play such a critical role when planning for financial life events? Do any of the life events not prompt an insurance review? What insurance products do you consider essential for yourself after graduation when you are “getting started”? What coverage might your employer provide? What insurance products will you need to purchase?
3. Why should you continue to upgrade your skills even after graduation? Name a few methods for upgrading and reinventing your skills in your career field. Estimate the costs associated with these strategies. Will you, or your employer, likely be responsible for the cost of these investments in yourself? Have these issues come up in job interviews?
4. This chapter asserts that “building wealth is part of a satisfying life” that is built on a balance between (a) a personal life that reflects your values and goals and (b) financial decisions that direct your spending. Reflect on this statement and Table 18.1 to describe your plans for having children.

5. Review the 12 keys to financial success, noting how many mention financial restraint. How can an understanding of living below your means and financial planning give you the freedom to spend while still accomplishing your goals?

6. Review the 10 financial life events and identify the ones that mention an emergency fund. Why is an emergency fund of 3 to 6 months of expenses recommended for everyone? Why is it particularly important when planning for some financial life events?

7. As inflation and taxes increase, why is it more important for investors to take prudent risks with equity investments? How is this principle affected by the investment time horizon?

Learn by Doing—Suggested Projects

1. To learn more about “cheap” living, do an Internet search to generate a list of the “top ten tips” for living frugally or saving money. How do the suggested spending and saving practices vary over the financial life cycle? Which ones might be most acceptable to young professionals getting started?

2. Develop a detailed budget for yourself using Worksheet 7. Next month record all expenditures, regardless of how small, that you make. Calculate the variances between the budgeted and actual amounts. Write a brief narrative of your budgeting experience.

3. Visit the Internet sites www.ed.gov, www.salliemae.com, www.loanconsolidation.ed.gov, www2.ed.gov/offices/OSFAP/DirectLoan/cancellation.html, or www1.salliemae.com/apps/SMCalcs/RCW/content/index.aspx to learn more about student loan repayment and consolidation. Review the repayment calculators and determine the monthly repayment for your loans, if applicable, or a hypothetical loan amount. Calculate your debt limit ratio from Chapter 7 based on your projected take-home pay. Assuming you can take on more consumer debt, what is the maximum payment you can add and still have a debt limit ratio below 15 percent?

4. As a group project, ask everyone in your class (or other classes) to estimate how much total debt they will have upon graduation using the categories of (a) student loans, (b) credit cards, and (c) other consumer debt (e.g., auto or electronics loans). Ask everyone to record their information, without including names, and submit it to your group. Summarize your findings, noting trends and averages. Is most of the debt good or bad debt? Are your classmates in danger of financial troubles after graduation? If so, what intervention strategies would your group recommend?

5. Make a list of typical items paid for through borrowing. Share your list with friends and relatives and ask them to quickly categorize the debts as good or bad. Record their reactions. Then explain the characteristics of good and bad debt and ask them to review the list again. Did their classifications change? How does the average person view debt? Did your respondents consider the characteristics of good and bad debt when making borrowing decisions? Summarize your results.

6. To learn about the services offered to households experiencing debt problems, contact the National Foundation for Consumer Credit (800-388-2227 or on the Web at www.nfcc.org). This nonprofit organization has offices across the nation and can refer you to a credit counselor in your area. Other for-profit services also may be available, but be sure to shop around before committing to any service. What educational or debt counseling services are available? What is the profile...
of the typical client they serve? What strategies do they typically use to assist clients? What are the expectations of clients seeking assistance? What costs, if any, do these services charge? What is the percentage of clients who successfully complete the debt management program?

7. “The more you make, the more necessities there are.” Discuss this quote with friends or relatives representing different stages of the life cycle and income levels. Can they recall specific goods or services that became necessities as their income increased? Can they recall specific goods or services that became necessities after specific life events? What do you and your classmates consider as necessities for getting started following college? Prepare a written or oral report of your findings.

8. Schedule some time to candidly discuss money and financial management with your best friend, partner, significant other, or spouse. Use Checklist 18.1, “Marriage, Money, and Financial Personality” as a guide. Don’t assume that you know the answers—regardless of how well you think you know the person. Prepare a written or oral report to describe your experience and summarize your observations, recognizing that some information may be confidential. What did you learn?

Be a Financial Planner—Discussion Case 1

This case is available in MyFinanceLab.

Your sister Chris and her boyfriend Doug recently announced plans to be married after graduation in May. Although you are fond of them both and want their relationship to succeed, you are concerned about their financial future. Neither Chris nor Doug completed a personal finance course while in college. Chris is a spender who has known few limits on her wants since she was a teenager. Doug, on the other hand, has worked, saved, and invested since he was a teenager to help provide for college costs. He will complete college with approximately $12,600 in student loans. But their income in their first year out of college will total $90,000, due in large part to Doug’s choice of major and practical work experience during college. Chris, who admits having no financial skill or interest, is content to let Doug handle all those matters, since he seems to be good at it and will likely earn more than she does.

Questions

1. The discussion of money issues is the first of a four-step process to help couples successfully manage their finances. The process might be summarized as (a) talk, (b) track, (c) plan and act, and (d) review and revise. Describe the steps and the objective of each.

2. Doug and Chris, similar to many young couples, are combining two life events: getting started and getting married. Integrate the planning steps and create a new list to ensure that Doug and Chris don’t overlook anything.

3. Explain to Chris why it is important that she become informed and involved in her financial future—regardless of how well Doug fulfills the role he hopes to have of husband and provider. What dangerous myth should she avoid? (Hint: In answering this question, go back to the section “Women and Personal Finance” that closed Chapter 1.)

4. Chris and Doug’s ideal is for Chris to work for a few years and then be a “stay-at-home mom.” If she invested $4,000 for eight consecutive years in a Roth IRA that earned 9 percent annually, how much would she have after 35 years? (Note: The first 8 years are an annuity, after which the balance will continue to grow, without deposits, for the remaining 27 years.) (Hint: This problem can be solved using a financial calculator, as discussed in Chapter 3, or the Money in Motion calculator, which is available in MyFinanceLab.)

5. Identify three essential actions that Chris should take to ensure her financial future.

6. Help Chris and Doug consider the issues of joint or separate checking accounts and credit cards. Why are these important issues to resolve prior to marriage?
7. What financial issues should Chris and Doug review, and perhaps take action on, prior to the birth of a child?
8. Aside from the obvious pain and emotional turmoil to Chris, Doug, and their extended family that would be caused by a divorce, why is it financially sound advice to stay married?
9. Doug is anxious to repay his student loan debt quickly but he also wants to take advantage of the matching contribution on his employer-provided retirement account. Assuming his student loans are bank loans at a rate of 8.25 percent, determine his monthly loan payments over a 5-year term (60 monthly payments), using the time value of money tools you learned in Chapter 3.
10. If Chris and Doug lose 30 percent of their gross salary to taxes and benefits, determine their debt limit ratio (from Chapter 7) based on the student loan payment. How much additional debt repayment could they add and not exceed the 15 percent safety margin?
11. Advise Doug on the priorities of repaying student loans or other debts as well as including retirement savings in their budget. Assuming he has a choice of equity and fixed-income investment products, which category would you recommend for his retirement savings? Defend your answers.
12. Why should insurance protection be a critical component of the financial plan developed by Chris and Doug? What strategies can help keep insurance costs down?

Be a Financial Planner—Discussion Case 2

This case is available in MyFinanceLab.

Jena has been so excited about what she has learned in her personal finance management class that she has been telling everyone, “You should take this class.” Now her dormitory hall monitor has asked her to prepare a talk on “credit and the young professional.” She has decided to use a question-and-answer format. Help her answer the following questions.

Questions

1. Why is it easy for college students to get and use credit cards? Aside from the obvious impact of “forgoing future consumption” to repay the debt, how can students’ credit practices affect their financial future?
2. What are three debt and credit trends that suggest few people are practicing frugality?
3. What does it mean to determine your own borrowing capacity and stick to it? Why is this strategy necessary when “choosing wealth”?
4. What is the relationship between borrowing capacity and an emergency account? What is the advantage or disadvantage of using less liquid accounts for emergency savings and, in the event of an emergency, immediately relying on credit?
5. What financial ratios are useful in monitoring your borrowing capacity? How are these ratios calculated and interpreted?
6. Review the 12 “keys to success.” Which strategies could you utilize to avoid bad debt?
7. According to the Nellie Mae study of college students, the average outstanding credit card balance reported by undergraduate and graduate students was $2,169 and $8,612, respectively. Jena decided to use the time value of money tools from Chapter 3 to calculate the size of the monthly payments that a typical undergraduate would need to pay off his or her $2,169 of credit card debt over 1 year (12 monthly payments), assuming an annual interest rate of 17.5 percent. She will also calculate the monthly payments that a typical graduate student would need to pay off his or her $8,612 of credit card debt over a 5-year period (60 monthly payments), again assuming a 17.5 percent annual rate of interest (in both calculations, assume no annual fee and no additional charges).