Developing Your Spending Plan

WELCOME AND INTRODUCTION 1

Welcome to Developing Your Spending Plan. In this program you will
learn about the importance of developing financial goals and having a 2
written plan to help you make your goals a reality. Using the Financial Planning Worksheet, a comprehensive financial planning tool, you will learn how to measure your wealth by calculating net worth, account for all of your income, document living expenses, and detail your indebtedness. You will also learn easy ways to improve your cash flow, reduce unnecessary living expenses and pay off debt, and know where to go for help.

FINANCIAL GOALS 3

Successful people have goals. They take control of their money and plan its use. It's important to commit your financial goals to writing. Take a moment to write down one financial goal that you would like to achieve. It can be a short-term goal, meaning you could achieve it within the next five years, or it can be a long-term goal, meaning it will probably take you more than five years to achieve it.

Goal setting forces you to decide what you want to accomplish with your money and clearly defines the steps to take. A well-written goal is a "SMART" goal. SMART means:

- Specific.
- Measurable.
- Action-oriented.
- Realistic.
- Timely (start and stop dates).

Goals will likely change over the years and that's fine. Adapt your plan to meet changes.

A typical financial goal is something like this: *"I want to be rich."* 4

Many people want to be rich, but this goal does not have a specific plan.

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How will you get rich, by what age, starting when?

Written using the SMART technique, the goal states, "I plan to have $1M in assets by age 65. To achieve my goal I will invest $250 per month in mutual funds with an average earning of 10%." Excellent goal! It is specific as to how much to save, has an end point and identifies what will be done to make it happen.

Here is one additional example of a SMART goal:

"I will buy a house within the next five years."

To achieve this goal I will:

- Get a copy of my credit report within 30 days.
- Pay off my car loan one year early by making double payments each month.
- Double my current savings to equal $500 per month to be able to have $30,000 for closing costs, down payment and other expenses.

Comprehensive, accurate and effective spending plans are developed with the ultimate goal of building wealth, not debt. Start this process by envisioning what you would like to achieve with your money and then writing your goals down in black and white using the "SMART" process.

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The Financial Planning Pyramid

THE FINANCIAL PLANNING PYRAMID

After doing some "vision" work through goal-setting, what do you do next? The Financial Planning Pyramid gives us a visual picture of the steps involved in successful management of personal finances.

1. The Management Level includes the most basic elements of planning and is the first step in building wealth. This level includes:
   - Adequate income: Using all of your pays, allowances and benefits offered by your employer.
   - Controlled spending: Using some type of a written plan.
   - Adequate insurance: Using appropriate insurance to protect against financial loss.

2. The second level of the Pyramid is the Savings Level. This level includes:

   Reserve Fund: A Reserve Fund is for expenses that don't occur monthly, such as car insurance, school tuition, birthdays and anniversaries, and holiday shopping.

   Emergency Fund: An Emergency Fund is for unexpected, emergency expenses such as emergency leave, unexpected auto repairs, or things like sick pets. It is recommended that an emergency fund consists of one to three months of your net pay.

   Goal-Getter Fund: The Goal-Getter Fund is for your short-term goals – financial goals for which the money is needed in the next five years or less. Money is kept in liquid accounts such as savings accounts or short-term CDs, where it is easily accessed.

   Note that these three funds don't necessarily have to be three separate accounts, but they need to be accounted for separately.

3. The remaining level of the Financial Planning Pyramid is the Investing Level. This level includes all of the tools that can be used in an effective investment plan. Investing is different from savings – more gain is involved, but so is more risk. Investing is for long-term financial goals – financial goals for which the money is needed in more than five years. Don't invest money you may need in the short term.

   Before investing, it is critical to first give attention to the Management and Savings levels of the Financial Planning Pyramid. Once you have established your spending and savings plans, then move into the investment arena. Plan to attend a Saving and Investing or Retirement Planning class at your Fleet and Family Support Center, or ask your CFS to conduct the training so you can learn more.

DEVELOPING YOUR SPENDING PLAN 7

What is a spending plan? A spending plan is a written method to achieve your financial goals by measuring and managing the money that comes in and goes out of your "pocket." A common name for a spending plan is a budget.

An effective plan: 8

Is a guide and servant – not a master. Some people think of a budget or a spending plan much like a diet – I have to suffer through this, and it will be painful, but hopefully in the end I'll achieve my goals. But if your spending plan is well-crafted, it won't feel restrictive. In fact, it should free you from worry and meet your needs and wants.

Doesn't need to be down to the penny – That's not to say it can't be down to the penny, and some people like to be that specific with their money. However, if you aren't much of an accountant, don't worry. The spending plan process will help you build up to accurate and effective numbers.

Is easy to understand – A spending plan or budget, in its simplest form, is a list of money in and money out. It shouldn't be any more complex than it needs to be for your situation. Although this program will introduce you to an eight-page tool, if your financial situation isn't complex, you may not need to use the complete form or a simpler form may work. Keep the process as simple as you can.

Is a reflection of your needs, wants, values and goals – The spending plan is YOUR spending plan. It should reflect the way you actually spend your money. Anyone who spends the money should be involved in the budgeting process. For example, if you are married, your spouse should be included.

9 *Is based on current income and expenses* – If you don't know what your current income and expenses are, you'll need to find out. Service members can usually list their income easily, but listing expenses may take a little more effort, especially if the person putting the plan together doesn't spend all the money in the family. Again, include everyone who spends the money in the process, and if you need to, track spending for a pay period or two in order to get accurate numbers.

Is practical and realistic – An effective spending plan has to be based on reality. You may want to spend only $20.00 a month on gas for your car, but is that realistic? You may want to start riding your bike rather than driving, but is that practical? As you work through your spending plan, be sure to keep it real.

Is flexible – A spending plan should not be a straight jacket. Build in flexibility by adding in a cushion, or better yet, make sure and build up your emergency and reserve savings so you can be flexible when you need to be.

Provides for pleasures as well as necessities – Service members and their families work hard for their money and make sacrifices every day that most civilians don't. It bears repeating that your spending plan needn't be so restrictive that you don't have room for some of life's pleasures. There are times when everyone needs to cut back, but it is reasonable and expected that people will build into their spending plan some money for pleasures, as well as necessities.

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A written spending plan can help you:

- Live within your income: By putting everything down in black and white, planning and tracking spending.
- Realize personal goals: Part of developing a spending plan is setting your goals down on paper and listing the steps needed to achieve those goals.
- Maintain a good credit history: The first step in having good credit is to pay your bills on time. An effective, written spending plan provides the foundation for a great credit report. And since the ultimate goal of any spending plan is to help you build wealth, not debt, as your assets grow and your debt is kept to a minimum, your credit report looks better and better.
- Get more for your money: A spending plan is the single best way to help find "leaks" in your spending. By tracking your income and expenses, you may find money you didn't know you had. You could find that you've been spending money on things that you don't really need or value. Many people even find that there is money 'lost' … they don't know where some of their money goes. You should be able to account for 100% of your money and ensure it is going only where you want it to go.
- Reduce financial stress and arguments: Planning income and expenses, writing down goals, and working together with your spouse will greatly reduce financial stress and arguments. Money is a top reason service members experience stress on the job. It is also one of the top things couples fight about. Much of this can be avoided by planning your spending, and a written plan is the key.
- Achieve financial competence and confidence: Imagine how it would feel to have just achieved an important financial goal in your life – perhaps it was to buy a house, to finance a child's education, or to retire early. Imagine how it would feel to know that when you decide not to spend money on something you want, you're saving the money for something even more important, something you've planned for. Imagine what it would feel like to be fully in control of your money, with low debt, adequate savings, and an investment plan in place. A spending plan isn't the key to all happiness, but it will open the door to a sense of financial competence and confidence.

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The Financial Planning Worksheet

The Financial Planning Worksheet Checklist

THE FINANCIAL PLANNING WORKSHEET

The Financial Planning Worksheet (FPW) is the spending plan form used in the Navy's Personal Financial Management Program. You will see that this is much more than just a budget.

There are five major components to the FPW:

1. Net Worth Statement on page one.
2. Budget or Cash Flow plan on pages two through four.
3. Action Plan on page five.
4. Paycheck by paycheck Spending Plan on page six.
5. Expense tracking form on pages seven and eight.

The Financial Planning Worksheet Checklist provides a list of items needed to accurately complete the FPW. Gather up any and all of these items and use them to fill in the appropriate sections. Be sure to use a pencil and have a calculator handy.

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1. The Net Worth Section

The first page of the Worksheet has a variety of personal information on the top half and the bottom half is a "Net Worth Statement". On this form, you simply list the total value of everything you own on the left and the total balance due for everything you owe on the right. When you subtract one from the other you are left with a figure called your "Net worth."

Net worth is your assets minus your liabilities, what you own minus what you owe. This is a measure of your wealth, and if you are running your finances according to good financial principles, you should see this number go up year after year. Ideally, you should have a positive net worth, but for many people just starting out it is common to be negative.

It is important that you accurately estimate the value of what you own (items in the assets column). To find the value of savings bonds, go to www.savingsbond.gov. If you don't know your home's value you can get an estimate of it's value at www.homegain.com. And to find your car's value check www.kbb.com or www.nadaguides.com.

Since your Net Worth is a measure of your wealth, it is a number that you should track on a regular basis, year to year for example, in order to ensure that you are building wealth, not debt. Using sound financial principles in the way you manage your money will ensure that each year the "bottom line" increases, and you are indeed moving in the direction of building wealth.

2. The Cash Flow or Budget Section 13

The four primary elements of the budget portion of the Financial Planning Worksheet (pages two through four) are:

- Income.
- Savings.
- Expenses.
- Indebtedness.

The Income Section 14

The income section is on page two of the Worksheet. This information comes directly from your Leave and Earnings Statement (LES). There are different terms used for different combinations of pays and deductions:

- Gross Income – your total pay and allowances, everything you earn.
- Net Income – gross income less taxes.
- Take-Home Pay – net income less any other deductions or automatic allotments. This is what ends up in your account each payday.

To determine your income, copy all pays and allowances you are entitled to from your LES or use a current pay chart to calculate your gross pay on page two. Remember this figure could be different from your taxable pay. All taxable items will have an asterisk (*) next to them in the entitlements section on your Financial Planning Worksheet. Another way of knowing which of your entitlements is taxable is anything that ends in the word "pay" is taxable.

Next list all monies deducted from your pay. These could include:

- Taxes.
- SGLI.
- FSGLI.
- TSP.

- Dental.
- Advance pay.
- Overpayments.
- Armed Forces Retirement Home.
- Contributions or payments to military aid organizations like Navy-Marine Corps Relief Society.
- Allotments.

Subtract your total deductions (B) from your gross pay (A) to calculate Service member's take-home pay for the month (A-B on the worksheet). If you divide take-home pay by two, you should get the amount of your direct deposit.

It is important to know the amount of your total net monthly income, the final income calculation on this page. With all the automatic deductions most service members have, it is difficult to keep track. To calculate your total net monthly income, all deductions that were made in the deductions section need to be added back except taxes and the Armed Forces Retirement Home assessment. Then add any additional income that is coming into the family such as income from a part-time job, a spouse's income, rental property income, child support, etc. Copy this amount into the appropriate box in the Summary section at the bottom of page four.

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The Savings Section

Turn to page three of the FPW. On this page and the next, you will list all of the money you spend. Why do you think Savings is the first category? Do you think of Savings as an expense (as something you "spend" money on)? There is room in this section to list any monthly amounts put into savings funds, as well as lines for monthly amounts going to investments and/or the TSP. When you total the monthly savings and investment amounts, copy it into the appropriate box in the Summary section at the bottom of page four.

Most financial advisors suggest you save a total of 5-10% of net income. The average American saves less than 1% (Bureau of Economic Analysis, December 2006). However, the average millionaire saves 10%, and the Navy's Personal Financial Management program recommends setting 10% of net income as a monthly goal for this category.

Living Expenses Section 16

This section lists the most common living expenses. Work down the page filling in the “Actual” column. If you know you spend money on an item but don’t know how much, you may need to track your spending for one or two pay periods.

Tracking Expenses: How much do you spend every month on living expenses? The best way to find out is simply to track your expenses for a month. Most people who are building their first spending plan cannot account for 10% of their income – they simply don’t know where the money goes. 17

There are lots of ways to track expenses. There is a form on pages seven and eight you can use, or keep a small notebook in your wallet or purse and write everything you spend in it. Be sure to write everything down – the dollar for a Coke, the $4.00 for Girl Scout cookies, the $5.00 you loan to a coworker, etc. You can also try keeping receipts from every purchase you make and total them up at the end of the week. After you’ve written everything down for a month, group your expenditures into categories similar to those listed on page three of the FPW and enter them on the form.

Living expenses take up the majority of your income. Some expenses are fixed, such as rent and insurance. Others are variable, such as entertainment, food and clothing. You can control variable expenses and adjust the amounts you spend in these categories in order to have more to use somewhere else.

Tracking expenses will give you a more honest picture of your spending than trying to guess how much you spend in each category. If you can’t commit to tracking expenses for a whole month, try to do it for two weeks. Get family members involved. It can be a family project. After you calculate your total monthly living expenses, copy the amount into the appropriate box in the Summary at the bottom of page four.

The Indebtedness Section 18

Page four includes the indebtedness section. This is where you list all of your outstanding debt along with the minimum payment required and the annual percentage rate (APR) charged. Include:

- Credit cards (bank, department store, gas, etc.).
- Car loans.
- Personal loans.

- Consolidation loans.
- Student loans.
- Advanced payments.
- Overpayments.
- Indebtedness to NMCRS, NEX, family and friends.

DO NOT include your mortgage. For our purposes, your mortgage is a living expense. DO include any rental property you have that is not your primary residence. When you total your minimum monthly debt payments, copy the amount into the appropriate box in the Summary at the bottom of the page.

19 The Summary

With the numbers input into the Summary at the bottom of page four, you can determine whether you have a surplus (money left over) or a deficit (a negative amount) at the end of the month. Income minus savings minus living expenses determines what you have left to pay debts. This number minus debt payments is what you have at the end of the month (this is also lost money or money that is unaccounted for, otherwise it would be listed somewhere on pages 3 or 4 already!). The Summary information can also be used to calculate what percentage of your net income goes to expenses, to indebtedness, and to savings. The ideal distribution of your net income is:

- 70% to living expenses.
- 20% to debt payments.
- 10% to savings.

Percentages will vary in different households based on different life-styles – but these guidelines still prove very effective in helping build wealth and keeping debt to a reasonable level.

20 Debt-to-Income Ratio

Monitoring your debt-to-income ratio is a good way to get a quick check of your financial health. In the 70-20-10 guidelines, the “20” is the debt-to-income ratio. Calculate your debt-to-income ratio as a means of measuring whether or not additional credit is affordable.

- First determine your net monthly income by identifying everything you make in one month minus only what is being withheld for taxes.
- Then total all monthly payments. Remember not to include mortgage payments.
- Divide the minimum monthly payments by the total net monthly income to determine your debt-to-income ratio.
- Minimum payments divided by net income multiplied by 100 is your ratio.

The formula is written below the Summary at the bottom of page four, and here is an example to help you calculate your own ratio:

An E-4 with dependents has a net income (after taxes) of $2980. Total minimum monthly payments are $545 a month. The debt-to-income ratio 21
formula=

545/2980= .1829

.1829*100= 18.29

Debt-to-income ratio is 18.29%

Credit use guidelines are:

- Less than 15% - use caution.
- 15% - 20% - fully extended.
- 21% - 30% - overextended.
- Greater than 30% - seek help.

In this example the E-4 is in the "fully extended" category and should refrain from taking on further debt payments. The use of credit has evolved from a luxury to almost a necessity. It all depends on how you use it. Credit cards are often used for wants rather than emergencies or planned needs. This, along with impulse spending, gets many people into the 'overextended' debt range. If you find yourself with too much debt, there are resources available to you. These resources are identified and will be discussed at the end of the module.

Surplus or Deficit 22

Is your bottom line positive or negative? If it's positive, great, but what are you doing with that extra money? If you are accounting for all your money there should be no surplus or deficit. If there is a surplus, put it away into savings or use it to pay off debts. If there is a deficit, you need to make some adjustments. Double check all your numbers and math to ensure there are no mistakes.

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Creative Savings Strategies

3. The Action Plan

Page six shows three ways to improve your spending plan, which means create a more positive cash flow. You can:

- Increase income.
- Decrease living expenses.
- Decrease indebtedness.

Decreasing living expenses produces the most immediate results. A well-managed budget that decreases living expenses can see results within days.

What are some ways to reduce expenses?

- Cut back to basic cable.
- Get all-in-one packages for cable, internet and cell phone.
- Eliminate telephone land line if you have a cell phone.
- Check books out from library rather than buying.
- Use public transportation or carpool rather than drive.
- Turn off lights when not in a room.
- Ask for military and other discounts.
- Send email rather than calling.
- Trade child care duty or meal duties with another couple.
- Cook at home and pack your lunch.
- Shop at thrift stores.

What are some ways to increase income?

- Spouse gets a job.

- Active duty person gets a part-time civilian job.
- Review and change tax filing status and exemptions.
- Enroll in any federal or state programs you may qualify for such as Women, Infant and Children (WIC) or Supplemental Security Income (SSI).

What are some ways to decrease indebtedness?

- Pay off debts.
- Stop using credit cards.
- Pay down debt using a power pay plan.
- Shop for the lowest interest rates.
- Consider consolidating.
- Seek help if in serious debt. Interest accrual and late fees may be waived by some creditors if in a non-profit debt management program.

When you construct your budget for the first time, use the "Actual" column. After you have decided what changes and improvements to make on page five, go back and recalculate your surplus or deficit by using the "Projected" column on pages two through four.

4. The Spending Plan

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Page six of the FPW is a paycheck-by-paycheck spending plan. All of the details you have worked out can be put together on one page to provide you with a specific amount to spend in each category.

You can use either your take home pay amount or total net income. Check the box for the amount you will base the Spending Plan on. If you use take home pay, list only what is deposited into your account each pay day and then note all other expenses as indicated. If you have allotments coming out of your salary, do not include them again on this page. If you use the net income amount, include all expenses whether paid by allotment or directly by you.

Note the (P) for "planning". This is where you list what you plan on paying with each paycheck. The (A) is the "actual" amount you spent or paid for the items. The spending plan allows a forecast of four months so you don't forget quarterly payments.

When used as a working document, your spending plan forces you to make deliberate spending decisions. If you consider buying an item not on the plan, then you must make a choice, take on more debt or spend money allotted to something else.

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THE AUTOMATED FINANCIAL PLANNING WORKSHEET

An automated version of the Financial Planning Worksheet is available on line or through your Command Financial Specialist. This Excel version automatically does calculations and fills in the Spending Plan. It is available at the websites noted in the "Sources of Help" handout.

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SOURCES OF HELP

A business would bring in a consultant if it started to run into financial problems. If you're having financial difficulties or need assistance creating a spending plan, get help. Sources of help include:

- Your Command Financial Specialist.
- Fleet and Family Support Center Financial Educators.
- Navy-Marine Corps Relief Society.
- Debt Management Programs at Credit Unions (both on and off the installation).
- Consumer Credit Counseling Services or other non-profit financial education organizations.

Some of these services are available on line or by telephone.

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SUMMARY

Understanding the fundamentals of the Financial Planning Worksheet provides you with a broad understanding of financial planning and the road to financial security. To review the five components of the FPW:

1. The "net worth" section on page one helps you measure your current wealth by subtracting everything you owe (debts) from everything you own (assets). This number should go up every year.

2. The “cash flow” or budget section on pages two through four allows you to calculate net monthly income, total monthly savings and living expense amounts, total monthly debt payments, surplus or deficit, and debt-to-income ratios. A great goal for your cash flow is to have 70% of your money going to living expenses, no more than 20% to debt payments, and at least 10% to savings and investments.

3. The “action plan” section helps you plan ways to cut expenses and debt payments and increase income, and provides a place to write down financial goals as well as space for referrals and additional education/training. Commit your intentions to writing and make the necessary changes in your cash flow.

4. The “spending plan” section on page six provides a paycheck-by-paycheck plan to ensure your actual day-to-day spending is in line with the amounts you have budgeted. Carry this plan with you at all times and refer to it when you are faced with an unplanned expense. Look at your spending plan and ask yourself, “Of all the things I’ve already thought about and planned for, which am I willing to give up in order to spend the money on something else?” Update your spending plan as income and expenses change.

5. Two expense tracking pages are provided for your convenience on pages seven and eight. Everyone benefits from tracking expenses for a month or two. It isn’t as hard as it seems, since you really only have to track out-of-pocket expenses. Everything else is usually paid for with a check, automatic deductions, or a credit card, so you’ll have a written record of them already.

These aren’t just the components of the Financial Planning Worksheet; they are the critical components of any well-crafted and effective financial plan. Once you understand and use these components, you are well on your way to building wealth and financial security.