G93-1162 Financial Planning

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Financial Planning

This NebGuide discusses the importance of financial planning, the results of not planning finances, and the important steps to take in making a financial plan.

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Achieving financial security in today's rapidly changing world requires more than earning an adequate income. Making sound decisions about managing financial resources is essential if financial success and security is to be attained. Financial planning refers to this decision making process.

Financial planning is the continuing process of decision making about obtaining, protecting, and using financial resources throughout life. Financial planning means developing and implementing plans to meet defined financial goals and objectives.

Financial goals are general, broad ideas of what you want to achieve with financial resources. An example of a financial goal is to send a child to college.

Financial objectives are more specific statements and stated for a shorter time period. An example of a financial objective is to put $1,000 in XYZ Mutual Fund for Junior's college education.

The financial planning process involves identifying both short and long term goals, and financial objectives; anticipating life changes and the costs associated with those changes analyzing your current situation relative to specific goals, objectives, and future needs; and developing plans that will help you meet financial objectives and goals.

Financial planning is not a one-time endeavor or piecemeal approach to financial decision making. It is an ongoing, continuous process that looks at the total financial situation, and makes adjustments that are appropriate for the changes in life.

In summary, *Best's Review*, the noted insurance industry publication, says financial planning is a "real, consumer-oriented, defined process, not a new way to sell financial services and products."

Importance of Planning

Why is financial planning important? Just as businesses need strong financial plans to thrive, people can use a similar systematic approach to managing personal and household financial affairs.

A. Planning financial resources puts ***you more in control*** of your financial situation. Look at your plan as a blueprint or guide for action that will give you more control over financial resources. It will also increase your ability to get what you want out of life. Planning is an indication that you accept **responsibility** for your own financial future. Although there are times when you will need to seek information and advice from other sources, the ultimate decisions are yours.

B. ***Building savings reserves.*** Without such a plan, you are more likely to put whatever is left the day before you receive income into your savings. For most people, savings accumulated in this manner will grow very slowly, or not at all, unless there is a definite plan. Financial experts recommend saving at least 10 percent of gross income for most people.

C. ***Prepares you for change.*** In today's world, change is inevitable. By recognizing that changes will require adjustments in your finances and by providing for those possibilities in the financial plan, the financial burden of the unexpected can be lessened. Having a plan can reduce anxiety and uncertainty as well since you will have the feeling of security that comes in knowing you have done your best to prepare for your future.

D. ***Improves communication and family relationships.*** The financial planning process requires that household members discuss individual and group goals, determine priorities, and consider consequences of various courses of action. Working together can enhance group unity and lead to more stable relationships.

Results of Not Planning

Results of not planning are:

1. Dependents and possessions inadequately protected against risk.

2. Financial goals and objectives not reached since money is not routinely set aside for them or a lack of financial objectives which make long-term goals seem unattainable.

3. Wasted resources since no plan means day-to-day decision making may not be done with an eye to the future.

4. Higher income and estate taxes paid which might have been avoided with a financial plan.

Financial Planning Goals

While financial goals will depend upon what you and others in your household believe are important, there are certain general areas around which to organize specific financial objectives.

One general goal is ***protection against risk***. Risks to consider include income loss and expense of premature death and disability, medical care expenses, property and liability losses, and unemployment.

Asset accumulation is another general goal. Consider the importance of an emergency fund in this category. An emergency fund can be an important buffer when those unexpected expenses occur. Any future expenses might also be included under this category of financial goals. For example, will there be education expenses for household members? Is the purchase of a home or starting a business in the works? Or, perhaps you are building assets for general investment purposes to receive a greater financial goal. Again, decide on your own particular reasons for building assets.

Providing for retirement income will be another goal. Because of the uncertainties associated with retirement, planning needs to begin at an early age. And, financial planning cannot stop at retirement.

Longer lives and even moderate inflation cause the need to provide for increasing income in a retirement plan.

Tax reduction is another area for planning. The goal for tax planning should be to pay what is legally owed, but not a penny more. In addition, estate planning or determining how to best distribute assets at death with minimal losses to the estate can be part of a financial plan.

Steps to Financial Planning

How can a financial plan be developed which will meet specific needs?

First, gather all pertinent information relating to finances. Gather information about income, expenditures, insurance coverages, employee benefits, investments, wills -- any document or information that relates to your individual situation. Complete a net worth statement and an income/expense statement at this time to better understand the current financial position.

Second, identify financial goals and objectives. Clearly define what it is you are striving toward. Look to the financial planning goal categories above and determine what your specific financial goals and objectives are. Communication with others in the household is an important part of this planning phase. While reaching a consensus is sometimes difficult, identifying goals, objectives and priorities is crucial.

Then, analyze your present situation. What is your current financial position? Are goals and objectives consistent with situation? Are there areas of deficiency that will need to be resolved?

Nonfinancial factors such as age and health of household members; number of dependents and their anticipated length of financial dependency; amount and stability of income, both present and future; and the financial temperament of household members, especially of adults, need to be considered.

Next, consider alternatives. During this phase, seek information to determine what consequences there are for the various alternatives you have. Getting information from financial advisers will be an important part of this step.

Develop the plan which includes specific strategies for meeting goals and objectives such as budgeting, automatic payroll deductions for savings or retirement, or developing an investment strategy. Look at the plan and ask if it allows you to meet your specific financial objectives. More importantly, is it a plan you can live with? Then put the plan into action.

Finally, review and revise. No plan should ever be considered final. As circumstances change, adjust the plan. Remember that the basic purpose of a financial plan is to help you reach the financial goals you have set.

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