

# You Need A Budget.



## 10-Day Course

*"You Haven't Budgeted Like This."*

## Day 1: How to Become Financially Secure

First off, thanks for taking part in this free e-course! I'm excited to be able to share some information with you about what is possibly the most boring topic imaginable: budgeting.

On a personal note though, this is right up my alley. When I started attending college there was one major that kept calling my name-accounting. They accepted me before I had my charisma bypass surgery. I was a natural from the start!

With that said, I warn you that this course is written by an accountant. What's more is that it's written about budgeting. Even more astonishing, I actually take the idea of budgeting extremely seriously. When you have no personality, these types of things become very important to you.

This course is broken up into 10 days. Over the course of ten days we'll discuss everything from spontaneity to boxing, and marriage to dollar unemployment. I hope to keep this quite personal, and have written it in such a manner. You'll hear my experiences and those of others with whom I've worked. My hope is to have you so consumed with resolve to get your financial house in order that you'll be absolutely, positively dying to get on a budget. You do need a budget, after all.

### **Your Budget - Your ROCK**

If you have read any personal finance books you may not have realized this, but the vast majority of them are doing you a huge disservice.

Read carefully and you'll notice that every "guru" mentions the need for a budget. Every one of them stresses its importance for...oh, about three sentences. Then they move on to catchier, more popular, more saleable things.

That's the biggest problem people have with budgeting-it doesn't sell. It's not sexy. It's not complicated. As a matter of fact, a lot of times an author sells a book on the illogical premise of over-complicating something that was simple to begin with. Not so with a budget - it's just too straight-forward.

Sorry Mr. Guru, you don't have a chance with this one. You'd best write about intelligent portfolio allocation or super-mega-rapid-debt-repayment-strategy optimizers.

I am, of course, being sarcastic. But the fact still remains that the budget is not given the attention it deserves. Again, it's boring.

BUT, it is the ROCK upon which your entire financial life is built. It is your foundation. All other financial decisions are appendages to the budget. The budget is the tree. Your retirement plan is the fruit. The budget is the massive trunk, rooted deep into the ground, immovable by any force. The new car you want is the fruit. The house you want-the fruit. The college savings you're dying to put away for your kids is, you guessed it...the fruit.

If the tree isn't there, neither is the fruit.

Advice from a Guru: "Make sure you're putting away at least 15 percent of your retirement into no-load mutual funds with solid track records."

But you still need to find the 15 percent.

Advice from a Guru: "You can utilize many options to save for your kids' college: 529 plans, ESAs, etc. It's an absolute must that you begin putting money away today."

But you still need to find the money.

Most financial books focus on the fruit. During this course, we're going to focus on the tree. The fruit needs to come from somewhere, and that's ALL we're going to talk about (well, almost).

Tomorrow we'll discuss the bad rap the budget has received and expose those dirty lies for what they are. In two days we'll hit the First Rule of Cash Flow in depth.

Grab a pencil and paper and write down the "fruit" you would like to grow from your financial tree. What will you do?

- Get out of debt?
- Pay off your home?
- Invest more earnestly for retirement?
- Put away money for a fancy vacation?
- Buy that flat-screen plasma HDTV?

Write down your financial goals. As we move through this course you'll have your eyes opened to the reality of those goals-they are a reality. You just need to plant your tree, help it take root, and watch it grow.

**Action Steps:**

- ✓ Write down your short- and long-term financial goals.

## Day 2: Dirty, Rotten, Lousy Lies

Alright, You're 1/10 finished.

Yesterday we talked about how a budget is the ROCK of your financial plan. It must be the first of all things financial. If you're concerned about your retirement nest egg, you must first be concerned with the chicken. And, as we talked about yesterday, if you want to grow some fruit (retirement, debt freedom, college funding), you need a budget - err, tree. Whatever.

I'm sure it was as true in your neighborhood as it was in mine. There was a house somewhere nearby that the neighborhood kids decided was haunted. It was probably occupied by some scary lady who would peer through her curtains and scare the living daylights out of any kids that dared set foot on her lawn. You probably stayed awake with your friends during sleepovers daring each other to knock on the door and bolt.

Little did you know how absolutely wrong you all were! The scary lady was the sweetest lady you ever could have met. She peered out of her window in hopes that you would come and knock on her door so she could show you pictures of her grandkids that lived thousands of miles away. She also wanted to feed you the most delicious chocolate chip cookies you ever would have tasted. She was hoping above hope for some company. You never heard her talk (because you wouldn't dare go near her house), but if you had, you would have heard the sweetest grandmotherly voice EVER.

See what I'm getting at? A functioning budget is like a sweet grandmother who bakes to-die-for chocolate chip cookies but is shunned by the neighborhood for no good reason! (I'll see if I can't use some sort of analogy with each day. By the end, I imagine we'll all be good and confused!)

Let's talk about these dirty rotten lousy lies (aka: excuses).

### ***Lie #1: I'm spontaneous.***

Budgeting destroys spontaneity. Wrong. Budgeting promotes planned spontaneity. Yes, I'll admit that for something to be spontaneous it can't be planned. But won't

you also admit that you can acknowledge the fact that you will be spontaneous (without knowing exactly what it will be) and plan for that a bit? A concrete example: if, at the drop of a hat, you like to go buy shoes, and you've done it consistently, and you can't stop, you either need to take drastic measures to keep yourself out of shoe stores or you need to acknowledge reality and budget for it. You still won't know which shoes you're going to buy (brown, white, black? Who knows!? That's the unpredictable spontaneous part), but you're acknowledging the fact that you WILL do something unplanned. Plan for the unplanned and you'll level out the ups and downs of your financial roller coaster.

***Lie #2: I'm not heavily in debt.***

I don't need a budget. If you make any money whatsoever, you would be well-served to live on a budget. The budget makes money work harder, last longer, go stronger, think faster, and move quicker. Whether you make \$100,000 a year, or \$24,000 per year, you need a budget.

***Lie #3: I don't have time to budget.***

Oh don't even go there girlfriend! You don't have time NOT to budget. Allow me to let you in on a little secret: Throughout this course you are going to learn the most effective, efficient way to manage your money. This most effective, efficient way to manage your money takes one to two hours per month. (My wife and I have been clocked at as low as 38 minutes for the entire month). Put another way, you're saying you DO have time for: talking with creditors, going to the bank to take out a loan, financing the purchase of a couch, settling for a new job that you don't want because you can't make it one month without a paycheck, etc. Sorry if that maybe sounded a bit harsh but that is reality. If you don't face reality, well, reality will eventually grab you by the shoulders and whip you around so fast you won't know what hit you. You WILL face reality eventually - make it happen on your own terms.

***Lie #4: Budgeting means lots of paperwork.***

Nope. How the heck could my wife and I have done ALL money management tasks for the entire month in 38 minutes if there was a ton of paperwork involved? There are a few receipts. There's an internet connection. There's a piece of software (the

software is the key, actually). That's about it. Sometimes there's some hot chocolate or another goody to eat while we're doing our budgeting meeting, but I'll talk about that on Day Six.

***Lie #5: Budgeting is for nerds, geeks, and penny pinchers.***

May I take the liberty to alter the above lie into a truth? Budgeting is for RICH nerds, geeks, and penny pinchers. Thank you.

***Lie #6: Budgeting causes inexplicable pain and suffering.***

Just the opposite my friend! The budget removes inexplicable pain and suffering. It helps you cope with financial problems. It is your straight-to-the-point doctor that never misses a diagnosis and tells you like it is. The budget will make your life easier. Truly.

Take a moment to write down what has kept you from actively budgeting. Do you not know how? Is the tracking too daunting? Is the software too overwhelming? Have you used the TIME excuse? Write those all down, then address each one of them. Debate yourself. Are your excuses also just dirty rotten lousy lies about a sweet, lonely grandmother?

Well, based on my experience working with others, these lies do seem to pop up most often. They're dirty rotten lousy lies. Pay no heed to them. Remember: the budget wants to give you fresh, hot, gooey chocolate chip cookies - and just chat in a sweet, grandmotherly voice for an hour or so each month. Tomorrow we're going to get into the mechanics of the budget, starting with the First Rule of Cash Flow. Hey, it only gets better, so hang on for the ride.

***Action Steps:***

- ✓ There are no action steps for Day Two. Just stop believing all the lies about budgeting.

## Day 3: The Ins and Outs of Inflows and Outflows

Today we'll discuss the actual mechanics of doing a budget.

Money is like breathing:

- In
- Out

With fancy marketing and pushy salesman, many times more money goes out than comes in. As a matter of fact, according to a report from a few years back in the Associated Press (January 2006), Americans' saving rate has fallen below zero, the likes of which hasn't happened since the Great Depression.

When you're operating on a budget, the pattern changes just slightly:

- In
- Assigned
- Out

We'll talk about each aspect of a budget, why it's there, and what you need to do to make it work.

### **Inflows**

Typically, when you think of money coming into your pocket, you think of your employment (or self-employment). Whether it is social security, child support, or welfare, the first type of inflow can be thought of as your Primary Income. Your paycheck most likely comes to mind. Some people are paid twice per month; others are paid every two weeks. Some are paid just once a month. None of that really matters though because you always follow the same three steps. If you earn income, you budget it, then you track your spending against your budget.

You want to make sure you record every single inflow. NO dollar should escape accountability.

## Outflows

Outflows are really pretty basic. Any time money flows out of your pocket (or you charge something on a credit card - meaning you incur the obligation to pay money out of your pocket), it is an outflow.

How big does an outflow have to be for it to really "count" as an outflow? It need not be very big at all. Perhaps an example would suffice. Did you stick a penny in the gumball machine at the oil & lube station while you were waiting for your car to be serviced? Congratulations, you just created an outflow! (How'd that gumball taste, by the way?)

While the one-penny charge is a bit of an exaggeration, I do it to illustrate a point. Too often we talk ourselves into little purchases that we think won't really add up. One penny plus one penny is two pennies. Five dollars plus five dollars is ten dollars. Thirty dollars plus thirty dollars is sixty dollars.

Personally, my wife and I have decided to record every single outflow. I encourage you to do the same.

I should probably mention that people place WAY too much weight on the notion of having to record everything you spend. Remember the other day when I said that my wife and I had been clocked at doing the ENTIRE budgeting process in 38 minutes? That included recording every single outflow for the month - manually. If it's a big receipt that needs to go to lots of different categories, save the receipt. If you make most of your purchases on a debit card, the bank already "wrote it down" for you. You just need to login to your bank, look at the register, and record what you've spent. We usually enter our outflows as they happen on our phones and then do a "check up" once a week. It takes five minutes - tops.

Also, there is a psychological advantage in writing things down. It keeps you closer to your money. This is a good thing. As you begin writing down EVERYTHING you spend, you'll notice your spending decline. It's an instant raise!

Begin recording every single purchase you make-and stop whining!

There you have it: the ins and outs of inflows and outflows. Pretty basic stuff huh? I think so too. For Day Four we'll talk about the First Rule of Cash Flow, that crucial - essential, extremely important - middle step of the budgeting process. We'll see you tomorrow!

**Action Steps:**

- ✓ Begin recording every single purchase you make. Without exception. It doesn't matter how you record it (pencil, iPhone or Android, spreadsheet, etc.), just make sure you do it consistently beginning today.

## Day 4: Who's the Boss? You, or Your Money?

We've covered the basics of a budget. You have your inflows, and your outflows. Right in there, sandwiched between the two pieces of rye, is Rule One: Give Every Dollar a Job. YOU are the boss.

Imagine a business where there are no defined job descriptions. Everyone just kind of comes and goes as they please. Some days you might find an engineer working on a marketing plan. The next day he could be over in finance figuring out how to account for a lease. The marketing employees love spending time on the factory floor because of all the big, shiny machinery. The accountants (with all their personality) enjoy spending their time trying to sell the product to customers (imagine how well that's going). Occasionally you might find a purchasing agent in discussion with the product design team about a cheaper, stronger material he read about on the internet...

I think you get the picture. This is not a company that has mastered cross-functional team theory. This is a company with no defined employee responsibilities. You wouldn't want to work there - and your job wouldn't last long if you did. It is only a matter of time before a company without properly defined roles is going under.

A household, where the dollars' roles are not properly defined is similarly destined to fail financially.

In the old days, devoted budgeters used envelopes to assign jobs to their dollars. That was pretty straight-forward; the dollar, sitting in the "groceries" envelope, knew exactly what to do, and when to do it.

In our much-more-modernized society (that, ironically, has not improved so much on the budgeting front), we don't seem to manage well with a lot of cash. I personally have tried the envelope system with a few select spending categories (groceries was the big one) and failed miserably. I would forget the envelope. Have I ever forgotten my debit card? Not one time.

But does that mean our dollars can just go about their business doing whatever they please?

Not even a little bit.

With spending apparently easier now than in the past (broader access to credit), it has become even more important that we consciously assign each dollar that comes into our hands a job to do for the month.

For instance, let's say that \$2,000 comes into your hands during the month. You must assign each and every single, solitary dollar a job. Some will go toward rent, and do their job during that very month. Other dollars will go to savings, where their job is to recruit new employees (read: interest) and train them to do the same. Some dollars have the job of just being "ready" for an emergency (much like firemen, right?). You'll have some dollars that sit around for six to twelve months before finally doing something (saving up in anticipation of car insurance premiums, and Christmas fund come to mind). Every dollar still does something. No dollar goes without a job.

Ever.

Well, almost never.

When my wife and I first started budgeting, we made the same mistake most beginning budgeters make. We didn't give ourselves any breathing room. I have to give credit to my wife though - she was much more dedicated than I was. I started to notice that I was stressed about money. I was stressed about spending it. I was stressed we wouldn't have enough of it. Frankly, it was getting to me a little bit at a time. I felt like I couldn't justify spending money on anything.

This is a dangerous situation. My wife handled it much better than I did. She's naturally much more frugal than I am...I was struggling!

We were assigning every single dollar a job. Every job appeared so important! I felt like I couldn't just go grab a candy bar if I wanted one. I felt constricted. After a month or two of working like this, I talked with my wife about it. I came to find out that she was also pretty stressed about our money situation. We decided then and there that each of us would get a little bit of "fun" money. Money we could just spend on whatever we wanted - without being accountable to the other person. In

sticking with our company metaphor, you could say that this fun money is unemployed.

The amazing part about this principle is that the amount does not need to be a lot - but it does need to be there! We settled on five dollars each per month. That was all I needed. Five lousy dollars and I felt like I could buy the world. The principle of assigning each dollar a job can work for or against you. Make sure you learn from mine and my wife's experience. Everyone needs a bit of breathing room!

You might consider a realistic unemployment rate for your personal economy. Is unemployment better? Certainly not. But it's realistic. And I've found too often that when people are unrealistic with their budgeting (as my wife and I were), they crash and burn. They give up. Why? You can't do unrealistic things for a significant amount of time when you're living in a brutally realistic world. So what exactly does an unemployed dollar do? Well, my wife gets a few of them, I get a few of them. And we can basically do whatever we want with them. They're unemployed. It really doesn't matter to me what she buys, and it doesn't matter to her what I buy (with the fun money). She doesn't tell me when she has bought anything. I don't tell her when I have. Unemployed dollars don't report to any boss except you.

The intentional lack of accountability to your spouse is key. It doesn't matter if one of you is the complete breadwinner of the family - it's the household money - not the breadwinner's money. Once it hits the budget, it belongs to the household. Only once you assign fun money to each other do you once again have your "own" money.

(Guys, a very romantic thing to do is to spend your fun money on your wife.)

Remember: when you're employing every dollar of your personal economy, make sure to un-employ a few too. It will more closely align your ideal world of money with the real world of money. Where do you eventually want most of your dollars working? In the Savings Department. In that department they're extremely useful. They find other dollars to employ on their own, and teach these new dollars the ropes (find more dollars, and teach them to find more dollars). The Savings Department is a beautiful thing. Where do you absolutely need dollars? In the

Emergency Department. These dollars aren't there to find other dollars. They're simply in charge of maintaining your Disaster Relief Plan. They shouldn't be employed in other departments. And they should never, ever be unemployed (used for "fun"). Because we're in this technologically progressive (and fiscally-irresponsible) society, you need to use something that will allow you to assign your dollars their jobs with ease. You can use a pencil and paper, some software, envelopes, a chalkboard - whatever. Just make sure your dollars are being assigned! When I created our software solution, it was imperative that it was easy to use. Keep that in mind as you choose your own solution. It needs to be user-friendly (and preferably cheap).

I can't stress enough how important it is to have your dollars working for you instead of just doing their own thing. As you implement Rule One, you'll notice that your dollars work harder, longer, and stronger for you. They're more efficient. They don't put up a fight. They do what they're told. They're basically the opposite of your teenager.

Now, we talked a lot about assigning your dollars jobs, but we didn't mention the process by which you do that. Tomorrow will be a special day because we're going to focus specifically on budgeting in a marriage. If you're single, well, tomorrow you'll learn what you'll do once you're married (or you can take a day off).

**Action Steps:**

- ✓ Create a list of your dollars' potential "jobs." These will be your spending categories.
- ✓ Write down what you'll buy with your "Fun" money. Your budget's longevity depends on it.

## Day 5: Money, Marriage, and Hot Chocolate

Yesterday we addressed a ton of issues regarding Rule One: Giving Every Dollar a Job. I purposely left one HUGE issue completely out; it deserves a day of its own.

When I was in graduate school I attended a Business Law course. One day, while sitting in class, I realized that the budgeting that happens between spouses is much like the consensus ad idem (meeting of the minds) we were discussing that very night.

I'll take the liberty of quoting Wikipedia to help me explain consensus ad idem:

"...a term in contract law used to describe the intentions of the parties forming the contract. In particular it refers to the situation where there is a common understanding in the formation of the contract...The reasoning is that a party should not be held to a contract that they were not even aware existed."

Basically, for a valid, enforceable contract to exist between two parties there needs to be this "meeting of the minds." That very same thing must happen when you're having your Budget Meeting at the beginning of the month!

It makes perfect sense that the monthly budgeting meeting can be seen as a contract between two parties: You and your spouse. Just as with contracts in business, there is usually a period of negotiation between the two parties prior to agreement. This same healthy negotiation pattern should happen when you're budgeting with your spouse. Healthy negotiation involves honesty, compromise, and respect. If those components are not present when you're forming multiple spending contracts with your spouse, it's best to work that out before you get so deep into negotiations that you're ready to tear your (or their) hair out.

We won't get into all the differences of men and women here, but let's just agree on the fact that there are innate differences between the two sexes. Respect and love that about your spouse. And then move on.

Honesty in negotiation means that if you agree to a spending amount, then you fully intend to live up to your side of the bargain. Guys: if you agree to spend \$50 on tools for February, then you aren't allowed to spend any more than \$50 unless

you can renegotiate the contract with your spouse (and this means taking the new money from some other place in the budget).

Honesty also implies that you're up front with your spouse about your concerns. If you feel like you're suffocating under the budget that you two have been working with for a while then you need to voice that concern!

When your spouse voices those concerns you need to be thinking about the "friendly" side of negotiations. Are you compromising if and when compromising is appropriate? Are you being respectful of your spouse's needs and wants?

The Budget Meeting should not be a dreaded 30 minutes (you don't really need more than 30-40 minutes for a month. As you get better at it, you'll knock it out in ten minutes). The more you budget, the quicker you'll recognize and anticipate what really needs to happen. Each spouse will be more realistic with their own expectations and compromising and respectful of the other's.

Sure, on paper this Budget Meeting may sound easy, but what if your spouse just really isn't the "financial type"? There are a few (million) of those. Some are in denial. Some are just really busy. Some are unbelievable earners and don't want to be bothered with the other side of the equation. Most just don't know what the heck you're talking about when you mention a Budget Meeting - so they're naturally, eh, petrified.

The word 'budget' tends to conjure fears in spouses. It has a pretty negative connotation attached to it.

You say: "Honey, I'd like to set up a budget with you."

They hear: "Honey, I'd like to control you when it comes to money."

You say: "Honey, we should probably budget for big expenses."

They hear: "You're spending too much money (but I'm not)."

You say: "Honey, let's try and keep to our budget this month."

They hear: "Honey, why don't you try and keep to my budget this month?"

That's just the way it goes. If you're the spouse that's on board and you're having trouble convincing your significant other of the importance of a budget...keep trying! Spell it out in very clear and friendly terms exactly what a budget entails. It is a 'meeting of the minds' between you and your spouse. That means that each one of you has to agree on how many dollars you've allocated to each of the spending categories.

Remember back to our definition of a meeting of the minds: "a party should not be held to a contract that they were not even aware existed." If you aren't sitting down with your spouse and agreeing together on how much to spend where, you can't really hold them to any type of budget per se.

I must say that if your spouse just outright refuses to sit down with you and manage the money for 30 minutes each month (you even agree to handle entering all of the transactions!), you have a deeper marriage issue than just budgeting. When you make it very clear to your spouse how absolutely important it is that you get a handle on your finances, that you actively budget together every month, and that it would mean the world to you if they would do it with you - they'd have to be a backward person to refuse. And you can tell them I said so!

A successful Budget Meeting should take place at the beginning of the month. Remember, keep it short. Make it fun. Have hot chocolate during the meeting. Go to a movie afterwards (budget for this, of course). Attach something positive to it. Just make sure you do it!

When you are successfully budgeting ("success" in budgeting does not mean you never go over your allocations) with your spouse each month, you will notice a few very positive changes in your money and your relationship. Your money matters will improve. Within your relationship you'll feel more teamwork, respect, and camaraderie with your spouse. Your communication skills will improve greatly.

The Budget Meeting cannot be ignored. It is the most powerful tool in solving money problems in a marriage - or improving the overall money situation in your marriage.

Have your spouse read this day's material. Talk it over with them. Spread the love!

Tomorrow we're going to get into Purchasing Power, and the Second Rule of Cash Flow.

**Action Steps:**

- ✓ Hold a budget meeting with your spouse. Talk about long- and short-term goals. If necessary, hold hands during the process.

## Day 6: It's Slightly Cloudy...

Congratulations on making it this far. I'm assuming, of course, that you've actually been reading, pondering, and ACTING on the principles taught in days one through six, not just hitting the delete key...

Wow. We've covered a lot. I hope you're beginning to feel the power of the budget. Maybe you're even developing a bit of respect for that six-letter word. You've also realized there is no truth to the lies surrounding budgeting. You've recognized the fact that your life, as you know it, will be improved immensely when you implement these principles. We've gone through the ins and outs of inflows and outflows. We talked about assigning every dollar a job. And just yesterday we stressed the importance of the Budget Meeting in your marriage. Did you talk with your spouse about it? Where can you improve? When will you start?

Today we're going to hit the Second Rule of Cash Flow Management: Save for a Rainy Day.

Rule Two can only happen when Rule One is happening. Remember how you're assigning your dollars to different jobs? Well, let's use the over-used example of car insurance. Let's say your \$360 car insurance premium is due every six months. That works out to be \$60 a month, right? I know, this is going to blow you away - all the complexity and stuff - but you'll want to budget \$60 into your car insurance category each month. When the sixth month rolls around, guess what your balance will be? \$360. You'll cut the check and pay the bill. No damage done.

But I'll bet you can remember back a few months ago when something big WAS due - maybe it was your property taxes, HOA dues, or...Christmas. How was it handled? I can't speak for everyone, but based on what I've experienced, if you don't plan for those high points with the bills, you're going to get leveled. You were apparently barely making it month to month and then you realized that a \$360 big-kahuna-type bill is coming down the pipeline. You probably had to charge it.

That's all going to change. It MUST change! If you're spending everything you make every month, you will eventually be carrying large amounts of debt around

your neck. You bring home \$3,000 - you budget and spend \$3,000 each month. When the insurance premium comes due you charge it. Again you bring home \$3,000 and then budget and spend \$3,000 again. This time though, you have a tiny minimum payment increase because of the \$360 charged onto your card. No matter, right? Well, repeat that cycle a few more times, with a few more similar situations and pretty soon you're sitting there with \$12,000 of credit card debt and no apparent way out.

There is a way out. You need to acknowledge the fact that some of your money, though it may not be going out this month, IS going to be doing a job for you. Its job is to sit there until the big bills come due.

What was once a roller coaster ride, is now a smooth highway. This principle, obvious as it may seem, truly works. It forces you to acknowledge in the "good" months (where nothing big is due) that you inevitably have a rainy day ahead. Instead of having eight good months, and four bad, you're going to have twelve normal months.

Trust me. It's much easier to handle twelve normal months.

This all appears quite easy when \$360 is a fixed payment. But what about something like car repairs? When's the transmission going to fail? When will the air conditioner stop working? When will your grandpa accidentally break the door handle off of your car while trying to get out, which causes you to have to roll down the window and reach for the outside handle whenever you want to get out of the passenger side (but forces you to show some chivalry when your wife is on the passenger side and you have to run around and get her out so she doesn't have to roll down the window and do it herself)?

I've digressed.

The fact of the matter is this: sometimes the forecasters know it's going to rain. Sometimes they can predict it with relative ease. Other times, everyone's surprised. We're talking about the surprises. You are not a statistical outlier. Neither is your house, your car, or your health. You are going to have some surprises.

These surprises do not constitute an emergency. You KNOW they're going to happen - you just don't know WHEN. So you need to start estimating. How much did you spend on car repairs last year? Was that a pretty normal year? Well then how much should you be putting into the car repairs category each month? It's as easy as that. You don't have the fixed amount, but you do have the experience that tells you something will come up. Something WILL come up.

Think about some rainy days in your life. I've talked about car insurance, Christmas, HOA dues, and property taxes. You may also have club membership dues, self-employment taxes (done quarterly), health insurance premiums, birthdays, anniversaries, relocation, etc. It's basically anything big that is happening that you can estimate and plan for financially.

My wife and I use the YNAB software that tracks these balance accumulations for us - but that is not totally necessary. You could just as easily use real envelopes, or write it down on a piece of paper on your fridge, or in your check register. You DO need to track it somehow or it won't work very well.

Setting aside money each month for rainy days will give you back your sanity and financial peace of mind. I can promise you from my own experience that the money really IS there when you're actively assigning your dollars to efficient, good jobs. Your money will go further, and you'll find that you have more than enough to save up while the sun shines for those rainy days ahead.

Tomorrow we're going to focus on the sport of boxing. Well, sort of.

### **Action Steps:**

- ✓ List all of your larger, non-monthly expenses (life insurance premiums, property taxes, Christmas, vacations, etc.)
- ✓ Divide the totals of those expenses by twelve to get your monthly funding requirement.

## Day 7: Staying on Track, No Matter What

We're going to hit Rule Three in major depth here. It is, by far, the most subtle of the Four Rules of Cash Flow, but it's my favorite.

You've probably heard the saying, "Just roll with the punches." It basically means take things as they come. Be adaptable - flexible. The original origin of the saying comes from the sport of boxing: "Said of a boxer: to move the body away from and in the same direction as an opponent's punches to reduce their impact."

If you ever watch boxing in slow motion you'll see the fighters doing this all the time. It truly does lessen the impact, and keeps them on their feet so they can continue the fight.

In budgeting, the same advice holds. So far, we haven't talked much about how people tend to get pretty depressed and down on themselves when their budget doesn't work for them. They usually throw in the towel (origin: "The traditional declaration of defeat in boxing, where a second, who feels his boxer cannot continue the bout, throws a towel into the ring to end it.") Okay. I'll get off the boxing thing...maybe.

So what happens when you go over budget? Well, nothing. You just roll with the punches. The key though, is to acknowledge the fact that you overspent, without throwing in the towel.

Rule Three is subtle, but here it is: If you budget \$200 into the groceries category for MARCH, and spend \$250, you overspent in groceries by \$50. In APRIL, your total available money that you have to budget is reduced by \$50. Your grocery category is zeroed out, and that's it. Let me stress that you don't pull the \$50 out of your grocery category - you pull it out of next month's TOTAL available money. If you wanted to, you could budget \$150 into groceries to try and make up for it, but there's no need. As soon as you take it out of that month's available money, that category overdraft is "paid back."

That's the gist of the rule: you pay yourself back for your mistakes by deducting it from next month's available money.

I'll tell you that the easiest solution to implement this is to have it done automatically with the YNAB software. But again, a pencil and paper will work fine. Some people are much more comfortable with the ol' no. 2 pencil anyway and that's fine.

I wish I could be standing there in front of you explaining this concept. I'd definitely be using some hand motions, and my voice would become more urgent as I dove further into the concept. I'd probably have to be standing to make it really come to life. I might even pace a little.

I love this Rule because it keeps people on their budget without punishing them in such a way that they never recover. This rule is in place so that you have a conservative rein on your money. As far as I know, it's completely unique. I haven't found it anywhere else.

Let's look at groceries a bit closer again. If you did overspend by \$50 - and DIDN'T zero your grocery balance at the end of the month, you would be living with that mistake of overspending by \$50 every single month. What if you budgeted \$200 for April and actually spent \$200? It'd still show that you had overspent by \$50 (even though you technically did what you planned to do that month). The cycle could continue again and again. BUT, if you zero the category and take the \$50 from the money available to budget for the next month, you start with a clean slate - each and every month.

Keep in mind that you're still paying yourself back for that mistake. It is not, by any stretch of the imagination, free money. You DO pay it back. And if you were to continue in your merry overspending ways, you'd eventually go under (we'll talk about that a bit more tomorrow). But you won't. You'll get better and better at staying within your budget and these overdrafts you experience will be less and less frequent.

I'll spill my guts here. My wife and I have been married almost eight years at the time of writing this - and we have operated using the YNAB Rules of Cash Flow the entire time. We have never, ever stayed within budget for our groceries. When we first married, we would budget \$120 and spend \$130. So we budgeted \$130 and spent \$140. We budgeted \$150 and spent \$160. We dropped it back to \$120 and

spent \$130. Heck, a few months ago we budgeted \$200 and spent \$215. Go figure huh? Does it bug me? Nah. Do I wonder what kind of gremlin we have in our grocery cart when we're shopping? Yeah.

The key is that we still just roll with the punches. What we overspend in one month, we pay back the next. Every category is zeroed that is overspent, and every category that has a surplus carries that surplus forward (Rule Two). It's masterfully simple. You don't really even feel what the budget is doing. It just takes you by the hand, makes a few corrections, and leads you gently down a more prudent path.

Alright, that's it for Rule Three, and Day Seven. Tomorrow we'll hit the final rule, then on Day Nine I'll be giving some words of caution regarding the rules. On Day Ten I'll share with you some closing thoughts, and my own story from rags to...nicer rags.

**Action Steps:**

✓ Take a break. There aren't any action steps for Day Seven.

## **Day 8: Learn to Live on Last Month's Income. (Say What?!)**

We're going to roll up our sleeves and get to work today.

It's been said that the definition of insanity is doing the same thing over and over while expecting different results. That seem like solid advice in my book, so we're going to springboard off that thought as we discuss the final Rule of Cash Flow.

When my wife and I first married (it's been a few years now), we worked part-time at the university where we were attending school full-time. Part-time work on a university campus equals, well, not a lot. I wasn't TOO worried about things, but the fact that our finances would be tight did inspire me to construct a spreadsheet to help us track our spending. Eventually I built it so it would also track our income.

The income was where the problems started arising though. Julie would work anywhere from 15-22 hours per week, depending on exams and homework. I would do my best to work between 18 and 24 hours, but again, that could change based on other uncontrollable factors. We were living on a variable income.

So how do you budget when you don't know what you're going to make? While a lot of financial gurus will suggest that you prioritize your expenses and always pay the top ones first, there is a better (initially harder, more fulfilling, and eventually easier) way.

You live on last month's income.

Now I'm going to spend the rest of the time trying to convince you that it IS a good idea.

Keep in mind though, that you can still use YNAB without having your one month's expenses saved. 90% of first-timers start using YNAB without having Rule Four in place. I DO want to encourage you to work toward living by Rule Four as fast as you can. It really is quite lovely - like a barbecue on a warm summer day...

If you've been on the site for more than five seconds you've seen this rule. You really should stop living paycheck to paycheck and begin living on last month's income.

How did we, two struggling college students do it? I'll admit, we had it kind of easy. Since our wedding had just happened a few months before, we had wedding money sitting in our savings account. I withdrew enough to get us through March without touching March's paychecks. That's exactly what I'm going to ask you to do. You need to make it through one month without using that month's paycheck(s). You may need to get a little intense to get it done.

Remember Albert Einstein. If you want to stop living paycheck to paycheck, and enjoy the benefits of MUCH more flexibility in your finances, if you want to be able to budget easily and accurately, you're going to have to start doing something different.

Again, the trick is to make it one entire month without touching your paychecks. If you've already done it, you're in like a dirty shirt.

How do you manage to get by for a month without touching that month's paychecks? Well, that's pretty much entirely up to you. I'll give you a few ideas to get you started. The key is INTENSITY. For the short-term, virtually ANYTHING is possible. Remember that!

- Work overtime if your job allows it. Put in as many hours as you possibly can.
- Get a part-time job. You can make a thousand bucks a month working 80 hours in a month at a part-time job. Think pizza delivery, UPS, painting, lawn care, house cleaning, etc.
- Start a small business. Some people laugh when I share this idea with them. I don't say it to be funny. I have a cousin that built up a lawn care business in one summer. It's been a couple of years since he's put anything into it, and it still makes him money every month. Imagine what it could be doing if he was actively going after it? If you mow 8 lawns for 8 weekends at \$20 a pop you'll have a nice stash. Don't forget car washing, window washing, dog walking, etc.
- Have a garage sale. That's right - get rid of the junk you don't need. Sell everything you forgot you had. People sometimes make enough from their garage sale to save some major money toward their #1 fund. Typically you make between \$500 and \$800.

- Negotiate your credit card rates down. Threaten to switch to other card providers. This can lower your minimum payment substantially - freeing up the extra right now for your buffer fund.
- Ask for a raise. Have you been an awesome employee? Do you truly deserve a raise? Then you should ask for one.
- Cut out your entertainment (keep thinking short-term here)
- Buy used (refrigerators, washers, dryers, cars, clothes, shoes, etc.)
- Freeze your credit cards in a very, very, very large container of water. If an emergency does strike where you absolutely need the card, then take the container out and let it melt at room temperature. By the time you can actually get to your cards, you'll have thought up a good solution for your emergency (that doesn't involve borrowing money).
- eBay. Like a garage sale, but with a wider audience. If you don't know how to eBay, ask the person next to you. They'll most likely know how and will be able to help you.
- Car pool. Gas prices are high right now. Sure it might be a bit inconvenient, but imagine if you could cut your gas bill in half!?
- Brown bag it. Don't eat out - at all. Remember, a short-term solution for long-lasting rewards. Sacrifice! (You'll probably trim down a bit too - I know I tend to trim UP if I eat out a lot). You may need to brown bag your dinner as well if you're working overtime!
- Cash in vacation. Sacrifice a few vacation days for your peace of mind. Many employers will allow you to 'cash out' of vacation. It's a great way to get some cash.
- Is your tax refund on its way?
- Save all windfalls. You do get windfalls. They happen. Stash 'em.

- Cut your phone bill. Consider cutting your phone down to the very basics. Do you have a cellphone where you could get out of the contract inexpensively? Remember, it's a short-term solution for long-lasting peace.
- Sell your car. Perhaps, you have a car that is way too expensive considering your current income. Sell it! Even if you owe more money on the car than it's worth, you can refinance the difference (provided your credit is decent), which frees up some extra dollars for your buffer. Remember, once your budgeting foundation is built, that debt will go away quickly.
- Don't buy bottled water. Seriously.
- Don't go to the mall. Seriously.
- Cancel cable, satellite, etc. Seriously.

It may take you several months to get to the point where you can live an entire month without touching any income. I've worked with some people that were truly so close to living paycheck to paycheck that they worked at it for FOURTEEN months. By and large, they are the exceptions (both in dedication and circumstance) to the rule.

Also, remember again that you can still use the YNAB system without your one month buffer saved. I just expect you to be working toward it - pronto.

The advantages to living one month behind your income are much further reaching than just eliminating the variable income problem of budgeting. When you are not living on the edge you are less stressed, healthier, sleep better, make wiser financial decisions, and enjoy a better relationship with your spouse. Life is better. You no longer have to time your bills with your paychecks, saving you hours of time each month! Keep those benefits in mind as you're scrimping by without cable, eating brown bag lunches, and throwing everything extra toward your buffer!

Take a moment to write down what you will do beginning NOW to get out of the paycheck to paycheck rut to be able to live on last month's income. Get crazy if you need to.

Rule Four is an important point, and absolutely vital if you want to have an easy, intuitive, cash flow management system.

Tomorrow we're going to talk about the danger lurking in these Rules: Overconfidence. See you then!

**Action Steps:**

- ✓ Write down three things you can do in the next 24 hours to begin building your buffer.
- ✓ Write down two more things you can do within the next 30 days to begin building your buffer.

## Day 9: You're Not Infallible, but You're Close

Seriously though, once you have these Four Rules implemented and running virtually on auto-pilot, you're going to feel invincible when it comes to your money. You'll be spending less time doing money things, thinking money things, and worrying about money things. Yet your money will be doing things you never thought possible. It'll be working harder for you. It will finally be productive. It'll be the employee you always wished you had.

But don't think you're infallible. Don't think it can't happen to you.

I'll share with you what happened to me and my wife. Now, keep in mind, I am especially prone to thinking we're invincible when it comes to money. And it's not because we make a lot (working with a part-time income while going to graduate school full-time does not equate to lots of money, quite the opposite actually). The reason I have felt so invincible in the past is because I trust the YNAB System to the core. I trust the Four Rules. I know that if we're recording what we're making, recording what we're spending, and having our budget meeting each month, we'll be fine.

But that's not quite right. Sometimes, you start to get a bit too comfortable with the rules. That's exactly what happened to us.

During my second to last semester of graduate school I cut back on the hours I worked at my job. I thought we could get by with me working about 20 hours per week. This happened mainly because I was kind of getting burned out - was extremely busy with school, and the website - and wanted to spend a bit more time with the family. So, we decided we could get by on me working 20 hours.

In October we overdrafted a bit in our budget. I figured we'd make it up in November. In November we overdrafted. With December coming though, I knew I'd be making more money because I could work full-time during the winter break. So I thought we'd make it up. Of course, Rule Four of YNAB states that you live on last month's income - so that December extra money wouldn't even come until January.

Well, December was more expensive than we had originally anticipated - and we overspent. Three consecutive months of overspending meant we had very little to work with come January. Well, January wasn't looking so hot. We actually used a cash infusion from our emergency fund to help pay for our health insurance premium (I had been putting off throwing that money into a Rainy Day fund for the few month's prior because we were just trying to catch up on the 'now' expenses). So that health insurance premium hit us big time (we had to pre-pay an entire semester's worth of insurance).

Health insurance is not a valid emergency fund expense.

So I started working at least 30 hours at my job - trucking through my last semester in graduate school. February was interesting because we started the month with only about \$1,000 of available money (all of these past overdrafts come back to haunt you if you don't make up the difference by either making more or spending less in succeeding months). I don't want to divulge too much personal information, but our rent amounted to more than half of that \$1,000.

So what happened? Why didn't we cut back our spending in the face of obvious looming problems ahead? We grew complacent with the budget.

As I mentioned above, I'm the author of the system for crying out loud. My wife understands it just as well as I do. What I'm saying here is this: we know how YNAB works better than anyone! We've seen how the principles force us to be conservative, assign dollars their jobs, and save for rainy days. The rules really work.

And we knew that Rule Three really works. We knew it so well in fact that we started virtually "borrowing against it" in a sense. Not literally borrowing money, but what we were doing was virtually the same thing. A non-YNAB credit card user unfamiliar with YNAB would use the following logic when charging a purchase and, thus overspending: "I'll spend less next month and be able to pay this off." We were doing virtually the same thing! "Well, we'll just buy it now because we need it now. YNAB will suck it out of next month's available money, so we'll just spend less and make up for it."

Amazing isn't it? Rule Three is so powerful, so graceful in how it guides you toward fiscal conservatism, that you can forget who truly controls the spending: You do...and you have to.

If you pick your favorite rule of YNAB, and only hold on to that one, without addressing the Four Rules as a whole, you'll start to go under. Which rule did we tend to ignore? Do you see the writing on the wall?

Rule One became second rate. We didn't pay it nearly the attention it truly deserves. Rule One of YNAB is the zero-based budget. You give every dollar a job. What that does is create spending limits in each of your categories. We were not paying enough attention to those limits! If the limit is there, then you stick to it no matter what. If you're out of milk for the month, you either take from another category in that month or you don't buy the milk! You should not begin to rely on Rule Three in such a way that you overspend in the month -make no adjustments for it - and expect to simply make it up in the next month. A pattern of such behavior will lead you to exactly where we ended up - needing to use our emergency fund money to pay for a non-emergency. Bleh.

Consider this a fair warning from the biggest YNAB fan of them all! You must abide by each rule of YNAB. Do not grow too comfortable with Rule Three's power to smooth out the bumps. I guess sometimes those bumps make for good reminders. We used YNAB for three years before I finally came to this realization: Regardless of how powerful the rules are, it is still up to you to exercise the discipline necessary to stick to every single rule. Don't play favorites!

I'm certain as you begin to implement the Rules of Cash Flow, you too will grow very comfortable with how the whole thing works. It's okay to become comfortable - just don't become complacent.

I'm especially excited for the final day tomorrow. I'll share with you quite a bit of our story - I hope you'll pardon the personal side of it and see it for what I truly intend it to be. See you tomorrow!

**Action Steps:**

- ✓ Write down all Four Rules of Cash Flow (from memory!).
- ✓ Commit to living them (whether you use YNAB or not).

## Day 10: Financial Success is Knocking. Will You Answer?

Alright, here we are on the last day of the course. I hope you've learned a lot, and enjoyed it as much as I have. It has been a lot of fun for me.

Today I'm just going to share with you a bit of motivation that comes right from my own life. I want to illustrate with the best example I have (our own) how absolutely powerful a budget can be in your life. Remember, it is the foundation of all other aspects of personal finance. It's the tree. The good stuff is the fruit. It's the sweet grandma with the gooey cookies. It just wants an hour or two of your time each month.

It was November of 2002 and I was newly engaged. People say when you're newly married that you live on love. But could love purchase my (overpriced) textbooks for the coming semester? Would love put food on the table?

Probably not.

So there I was, sitting in front of a computer in the library of the university. My fiancée was just across the hall working for \$8 an hour. I would be leaving for my job in a few hours to make a bunch more - \$10 an hour. I just sat there wondering exactly how we were going to manage. We were both full-time students, working part-time jobs. In our best combined month we would maybe make \$1,200. Looming in front of us was the purchase of a car (neither of us had one), and three more years of school for me.

I had just recently taken a course in Microsoft Excel. I thought I could make a little spreadsheet that would help us manage our finances. It was obvious we would need to manage what little we had.

A few weeks later I basically had the spreadsheet finished. We were getting closer to our wedding day and those things naturally took precedence over any "dinking around" I wanted to do on the computer. We were busy people in love and in school!

We were married the following February. Everything was absolutely great. I was definitely excited to be starting a new chapter in our lives.

I mentioned in Day Eight how Rule Four came about. I basically just thought it would be easier to budget if we lived on last month's income (and oh, how it is). I tailored the spreadsheet so that last month's money would flow into the current month. Some wedding money was our "buffer". I'll admit it - we had it easy.

Rule One seemed pretty obvious. Every dollar should be accounted for. It just didn't seem right to have some money sit there not doing anything. It was pretty easy to have the spreadsheet tally up the total available money each month, and have that reduced as we budgeted into our spending categories.

The budget meeting was an interesting thing when we first married. I thought it'd be more of a negotiating thing where she's guessing what I'm going to say, I'm guessing what she's going to say, and neither of us wants to say a specific number lest we leave some money on the table. It wasn't really anything like that. Not at all.

Basically we would just sit down together and look at our money situation. It was a pretty healthy relationship exercise. It helped us face reality. It helped us decide where we needed to focus. It motivated me to squeeze in a few extra hours of work whenever possible. It motivated Julie to try and land a good job once she graduated. It really brought us together as a newly-married couple. There weren't any fights. There weren't any hurt feelings. It was just two people sitting there trying to figure things out - compromising, and learning what their spouse thought about money. It's been an extremely positive aspect of our marriage for the past seven and a half years. I don't see that changing any time soon.

Rule Two, I hate to say, also seemed pretty obvious. We had big one-time expenses that would definitely need to be paid. But we knew we'd be sunk if we pretended like we would have all that money in one single month. I made sure the budget tallied up any surplus balances each month so that they would be cumulative and grow over time.

I remember the first time we were really nailed on one was with our license and registration tax that we needed to pay each May. We had been married over a year when we discovered that we owed the State \$150 just so we could re-register our vehicle. I won't go into the aspects of this particular highway robbery, but we were

caught by surprise. A hundred and fifty bucks was (and still is) a lot to us. We learned and adjusted. (How did we adjust? \$12.50 goes into "License and Taxes" each month. We don't even feel it now).

Rule Three I actually stumbled upon by necessity practically. As discussed on Day Seven, I didn't like the idea of continually being punished for mistakes in the past. And I REALLY liked the idea of starting with a clean slate each month for a category that had just taken a beating in the prior month. We would be able to sit down and figure out exactly what was happening for THAT month and see if we couldn't make things happen to our favor.

The problem was that you would have a surplus in some categories (say Christmas) because you're saving up all year for it. On the other hand, you would go over with groceries (as we did and still do). So if we did overspend by \$50 in groceries, it wouldn't cause us to overdraft in our checking account - far from it. We had some of the CURRENT month's income in there now (Rule Four), along with various category surpluses (such as Christmas) from Rule Three funds.

But the problem was that the \$50 was really gone. And the Christmas category, which had "paid" for the overdraft, was still showing the same surplus. I battled with the problem for a while and finally came up with the idea of taking overdrafted balances out of next month's available money. That way, any surplus categories that did pay for overdrafts of other categories were reimbursed. It was all good.

I tweaked the spreadsheet to do just that. Since then it's been on autopilot and I don't have to think through my reasoning each and every time.

To be honest, I really didn't know what we had. I thought it was just a somewhat clever (and somewhat obvious) way of budgeting. The spreadsheet started looking pretty good and doing its thing pretty well. We used it for a couple of years without much thought about it.

Since we were still in college, it was pretty easy for us to talk about our finances with friends. When everyone is broke, money isn't a sensitive issue. I would actually show them our budget. Our friends would ask me for a copy. I don't think

one of them actually used it though. It was too tailored to our specific situation. (And getting one month's expenses to follow Rule Four is no picnic either).

Well, our first child was on the way in June of 2004 and that got me thinking. We had always wanted Julie to be able to be a full-time mom. She was really looking forward to it. I had gotten a part-time "internship" at a company near the university. We figured out if I worked 30 hours per week straight through school, we'd be able to get by okay.

I didn't think 30 hours per week would be too easy if I wanted my grades to be somewhat respectable. So I presented Julie with the idea of selling our budgeting system online. She didn't think it would fly, which I still remind her about to this day.

I got cracking on the idea though. I worked tirelessly on making the budget as user-friendly as possible. As I tried to explain the budget to my potential audience, I began to truly appreciate what we had here: a budgeting system that didn't take a lot of time, that worked. It had worked for us - and if it worked for us it would work for just about anyone.

So here we are today. What was a "hobby" site is now a full-time endeavor with a team of 18 spread across the globe. I became a CPA and then immediately let it lapse to work on YNAB. I did graduate with a graduate degree (Masters of Accountancy, if you were at all wondering). Our little boy is now eight years old, with a little brother (6), little sister (4), another little brother (2) and another little sister (1).

Life is good. It isn't luxurious. The car with the broken door handle on the passenger side WAS my car and that WAS my grandpa that broke it (Day Eight). I DID have to run around to the other side to help my fair lady out of the car. If it was icy, I would be extra careful when running.

But we have something that so many people don't have. We have an easy-to-use, functioning budget. A PLAN. It may seem like I'm attributing too much to the budget, but I don't think so. We have never fought about money. We've never gone into debt. We own our used cars outright. At the end of a Master's degree,

where most people are at their poorest, we were at our richest! (Rich is very relative here, but you get my point).

I look around me and see people living above their means, with nicer cars, TVs, toys, homes, etc., and I can't help but feel a bit for them. True happiness does not revolve around the material things you have. True happiness comes from PEACE. And PEACE comes from living within your means. If you want to live within your means, well, the prior nine days have showed you what to do.

The Rules are there for you to implement. I'd be out and out lying if I didn't tell you that I'm hoping you'll give the YNAB system a try. It's evolved into a pretty nice piece of software, if I may say so myself. Support is first-rate, with a super-friendly online community, live classes, and *real-life* email support (when all else fails ;)

Also, remember that the Rules can be used independent of any software. You could even make your own system that does the same thing (don't underestimate the time involved though!). Implement the Rules if you do anything. They are powerful! They will help you!

Honestly, the Rules seemed to kind of fall into my lap. Looking back now on that day in November, when I was feeling pretty stressed about money, I don't know, maybe I can chalk it up to inspiration. But at that moment I just thought to myself, "I think we need a budget."

We did.

And so do you.

A handwritten signature in black ink, appearing to be 'John' or similar, written in a cursive style.

**P.S.** Feel free to pass this along to any kids, siblings, aunts, uncles, other family members or friends that "need a budget." You know you're thinking of someone... :)