Annual Financial Check up Guide

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Annual Financial Check-up
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Annual Financial Check up Guide

Welcome!

Annual check ups are pretty common occurrences in life. We are supposed to see the doctor to check our health annually. We are supposed to take our car in for routine maintenance. Our teeth, homes, and computers all require check ups. Even our finances need check ups from time to time.

The purpose of an annual financial check up is two fold: To look backward and reflect on the past year, and to look forward, developing strategies to improve your finances. Whether the news is good or bad, a financial check up can help you recognize your current position and make the chances that will allow you to move forward toward success.

This guide is designed to help you with this important process.

Working with Financial Advisors

In my 20 years of experience, I've come to believe that the majority of people need help with their finances. Many people work with financial advisors to review their financial positions from time to time, adjusting plans and learning strategies.

This guide is perfect for those working with their advisors because it forces the process to stay focused on the bigger picture. Unfortunately, too many annual reviews fixate on the portfolio and the investments because so many advisors are compensated that way. Always remember that **financial check ups are not portfolio check ups**. The investments are just one part of the overall financial review.

Contents

How are You Doing Financially?

When it comes to a financial review, it's really easy to become overwhelmed by the numbers and the details. Before you analyze the details, it's really important to start with general perspective.

On a scale of 0 to 10, how do you feel about your overall financial situation? Don't get too fancy, don't over think it; just be impulsive and give yourself a score.

- If you score yourself under a 6, it's important that you read this report to help you find ways to improve your score. This guide will help you identify opportunities to progress financially.

- A score greater than 6 indicates that you are probably doing a lot of the right things, and that your financial plan just needs fine tuning.

This question is not overly sophisticated, but it does remind us to trust our instincts from time to time. Sometimes we are paralyzed by details, suffering from information overload. Too many choices can prevent you from taking the first step.

Having this simple perspective starts the process rolling in the right direction. Now, it's time to dig a little deeper.

Have You Experienced Any Big Changes?

Change is a great reason to review your financial strategies. If major life events have affected you in the past year or two, you probably have been forced to make some financial changes. However, you may have also procrastinated in your financial response to major life changes. Reviewing this list may be the catalyst to proper addressing the ways major life experiences affect your finances:

- ❒ Graduation
- ❒ Changing jobs
- ❒ Marriage
- ❒ Divorce
- ❒ Children
- ❒ Caring for parents
- ❒ Buying a new house
- ❒ Mortgage free
- ❒ Debt free
- ❒ Bankruptcy
- ❒ Starting a business
- ❒ Retirement

- ❒ Disability
- ❒ New Grandchildren
- ❒ New investments
- ❒ Children leave home
- ❒ Children come back home
- ❒ Lend children significant amounts of money
- ❒ Children get divorced
- ❒ Health deteriorates
- ❒ Spouses health deteriorates

- ❒ Children's health deteriorates
- ❒ Receive inheritance
- ❒ Receive a large sum of money
- ❒ Lose a large sum of money
- ❒ Children going to post secondary education
- ❒ Disability
- ❒ Lose a job
- ❒

Think about how some of these changes have affected your finances and write down some of the issues that you face:

What is Your Net Worth?

Knowing your net worth is a very important aspect of personal finance. How can you know if you are getting ahead financially if you have no way to track or measure your wealth? If you want a benchmark for wealth, retirement or financial fitness, make sure your starting point is your net worth.

Creating a net worth statement is a basic skill you should know and practice regularly.

How to calculate your worth

Take a piece of paper and draw a line down the middle of the page from top to bottom. On the left side of the page write down all the assets you think contribute positively to your financial well-being (not depreciating assets). On the other side of the page, list all your debts or liabilities. At the bottom of the page, add up each column. Next, subtract your total liabilities from your total assets. The result is your net worth.

On the next page, you will find a little template to help you figure out your net worth. Alternatively, you can go to this link to download an excel spreadsheet template to help you calculate your net worth.
http://retirehappyblog.ca/money-tip-%E2%80%93-calculate-your-net-worth/

Is your net worth increasing?

Generally speaking, your goal should be to increase your net worth. If you think about it, there are only two ways to increase your net worth: Increase your assets or decrease your liabilities. Calculating your net worth regularly helps you to understand the importance of saving money, buying appreciating assets and paying down debts in order to increase your worth.

If your net worth is increasing, you are probably doing the right things. If your net worth is decreasing, it's imperative that you take a more detailed look at why, and see if you can make some changes to improve your net worth in the future.

Net Worth Statement

ASSETS

Liquid Assets

- Chequing Accounts
- Savings Accounts
- GICs
- Cash Value of Life Insurance
- Tax Free Savings Accounts (TFSA)
- Money Market Funds

Property Assets

- Principal Residence
- Recreational Property
- Investment Property
- Other Real Estate

Long Term Assets

- RRSPs/RRIFs
- Non-RRSP Investments
- Pension / LIRA
- Business
- Other Assets

TOTAL ASSETS (A)

LIABILITIES

- Mortgage
- Other Mortgages
- Personal Lines of Credit
- Investment Loans (Leverage)
- Student Loans
- Car Loans
- RRSP loans
- Credit Cards

TOTAL LIABILITIES (B)

NET WORTH (A-B)

How is Your Spending?

The wealthiest people in the world are not those with the most stuff. They are the ones that manage their lifestyle the best. It is so important that you simply live within your means.

Which statement best describes your spending?

- ❒ You spend everything you make
- ❒ You spend more than you make
- ❒ You spend less than you make

All you have to do is look at your bank account and check your inflow versus outflow. If you have more money coming in than going out, then you are likely living within your means. If your situation is the opposite, then you need a reality check.

Know how much you spend

How do you know if you are overspending when you never take steps to track your spending in some way? Some people assume this is where budgeting comes into play. Not me. I don't like the word 'budget' any more than I like the word 'diet'. Both of these words imply restriction of behavior. I'm not suggesting that everyone needs a budget. I am suggesting that everyone needs to know how much money they spend each and every month. If you have a spending problem, only then you need to budget your money -- just like if you have an eating problem, then you have to diet.

Successful people live within their means. In fact, studies suggest that about two thirds of wealthy people know exactly where they are spending their money. If you want to become wealthier, develop a habit of tracking where you spend your money on a monthly basis.

Remember, the more accurate the number, the better. Most people underestimate their spending because they ball park it with their big or regular expenses like the mortgage, car payments, utilities and food. The biggest culprit of underestimating expenses is something I call MYSTERY CASH.

How Much Do You Spend Every Month?

Most people don't know how much money they spend on a monthly or yearly basis. Some believe they know how much they spend, or have a vague idea, but they typically underestimate. Very few people know what they are spending; those that truly know are typically in pretty good financial shape.

Tracking expenses takes effort, conscious awareness and ongoing work. Maybe that's why most people don't track expenses (or calories}. The trick is to keep it as simple and effortless as possible. The key is to turn it into a good life habit.

January
February
March
April
May
June
July
August
September
October
November
December

Total

MONEY IN - Any cash going into the bank account. For paycheques, just include net deposits after deductions.

MONEY OUT - Any and all cash going out of the account. This includes bill payments, withdrawals, PACs, etc. Do not include any money going to savings or investments.

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Are you Saving Enough Money?

Wealth is not built by accident. Contrary to popular belief, most wealth is not inherited or won in a lottery. 80% of the wealthy are first generation -- and they built their wealth one step at a time.

Saving money is the foundation for financial success. It is the root of what separates the rich from the poor. For most people saving money is not easy. It feels more natural to spend money than to save it. Since saving is not natural, it is something we must learn to do and work at. Saving money over a lifetime requires conscious effort and continued awareness so that it becomes a habit.

Principles of Saving Money

You can use fancy financial calculators to help you figure out how much money you should save for retirement or financial independence, but sometimes the outcome can be depressing and de-motivating. No matter who you are, and how much you are saving, just remember these principles to help you understand the basics of saving money:

- It's never too late to start
- The sooner you save, the better
- Make it automatic
- Saving something is better than saving nothing
- It's all about staying disciplined
- Try to increase your savings each year
- Save extra lump sums when you come into money

Review your Savings

When reviewing your savings, review the above principles. Ask yourself if you are doing them. If you aren't, is there an opportunity for improvement?

- How much did you save last year?
- Can you save more this year?
- Can you increase your automatic monthly savings?

Are You in Control of Your Debt?

Certain financial behaviours indicate that your debt is starting to control you. Ask yourself:

- Is your debt stressing you out?
- Are you only able to make the minimum payments on your loans?
- Has your debt been increasing?
- Have you missed payments or had to take advantage of the “miss-a-payment” feature on your loans?
- Have you used a cash withdrawal from one credit card or line of credit to pay another?
- Are you at or near the limit on most of your credit cards?
- Have you obtained new credit because your current credit cards or lines of credit are at the limit?
- Have you borrowed additional money since consolidating your loans?
- Have you received a call from a lender looking for missed payments?
- Have you borrowed money from friends or family to make ends meet?
- Are you unable to set aside even a small amount of savings for a rainy day or emergency?
- Do you feel as though you are living from paycheque to paycheque?

If you answered “yes” to more than a couple of questions, it’s time to look at solutions, and perhaps get some professional advice.

Three strategies to get out of debt

1. **Increase Income and/or Decrease Expenses** are appropriate solutions when the debt level is lower or when more money can be made available to pay debts.
2. **Refinancing** refers to lengthening the duration of a loan in order to reduce the monthly payment. Good credit is essential for this to work, but extending the loan can help the payment “fit” better in your budget.
3. **Consolidation** is often the preferred solution for reducing the total number of payments and reducing the overall interest. Good credit is vital and collateral (assets) or a cosigner is often required. This solution is especially effective if you have a number of loans or several credit cards with higher interest rates. One loan could pay them off entirely, simplifying several monthly payments into one loan payment at a better interest rate.

Reviewing Your Debt

The Debt Manager

Name of Debt	Amount of Debt ($)	Interest rate (%)	Minimum Payment ($)	Actual Payment ($)	how long till this debt is paid off?

Set up your own spreadsheet like the one above to help you analyze your debt situation. Look for opportunities to lower your interest rates, or increase payments. Be aware of the total amount of debt you have, the percentage of your gross income that goes to debt and how long it will take to pay off those debts. Here are two important questions to answer once you've analyzed your debt:

1. Did your debt increase or decrease from last year? If the answer is yes, then it's time to get serious about stopping the trend. If your debt reduction strategy is on the right course, then keep it going and see if there is any opportunity to pay it off even faster.

2. Can you increase your payments to get rid of debt faster? Debt has been a wealth killer, even for people who save money. Paying off debt is a sure way to increase your wealth and reduce financial stress. Are there opportunities to earn more income to pay down debt faster? Are there ways to cut back on other expenses to increase debt payments?

Are there Opportunities to Increase Your Income?

According to the book, The Millionaire Next Door by William Danko and Thomas Stanley, there is a positive relationship between wealth and income: “Yes, higher-income households tend to have more wealth than lower- and middle-income households.”

So the solution is simple – just make more money. Unfortunately that’s easier said than done. At the same time, though, earning more is far from impossible. Too many people take the path of least resistance, insisting that it’s too hard to earn extra money.

Making more money may be simple, but it’s not necessarily easy. The opportunities are there. You just have to want it bad enough. If you feel like making more money may be an opportunity you want to explore, here’s a list of ideas for increasing your income:

- Work part time
- Get more education
- Change jobs
- Get a promotion
- Work overtime
- Have a garage sale
- Sell items on ebay or Kijiji
- Turn a hobby into a business
- Create income from your investments
- Rent out a room in your house
- Work harder

Despite this strong correlation, the key to financial success is not just how much money you make, but also what you do with it that really counts. What really matters is how much of that income is saved.

Are You Taking Advantage of Tax Strategies?

Saving money through tax planning is an ideal way to get ahead financially. Paying less tax means more money in your pocket.

To truly understand the basics of tax planning, you need to understand the three D's of tax planning:

- **Deduct** – A deduction is a claim to reduce your taxable income. A deduction will reduce your tax bill by an equal amount to your marginal tax rate. Some common deductions include:
    - Pension plan contributions
    - RRSP contributions
    - Safety Deposit Box Fees
    - Interest expense
    - Union/professional dues
    - Alimony/maintenance payments
    - Employment expenses
    - Moving expenses
    - Professional fees
    - Child care expenses

- **Defer** – A deferral strategy is to push paying taxes into future years. Deferring tax means you might avoid paying tax this year, but you eventually have to pay the tax down the road. Generally tax deferral has 2 advantages: (1) It is better to pay a dollar of tax tomorrow than it is to pay a dollar of tax today and (2) Tax deferral typically puts the control of when you have to pay the tax in the hands of the tax payer instead of in the hands of the Canada Custom Revenue Agency (CCRA). RRSPs, RESPs and various investment income strategies are the most common forms of tax deferral for the 'average' Canadian.

- **Divide** – Often called income splitting, dividing taxes implies the ability to take an income and spread it among a number of different taxpayers. For example, if you have one person paying tax on $70,000 vs. having 2 people (say husband and wife) paying tax on $35,000 each, you would rather have the second scenario. Unfortunately, you cannot arbitrarily decide who is going to claim what amounts for income. There are, however, strategies to divide income within the rules of the CCRA:

Tax Strategies (con't)

1. Spousal RRSPs help split income in retirement.
2. Splitting CPP retirement benefits with your spouse.
3. Pension splitting for retired couples.
4. Investing non-RRSP savings in the lower income family members.
5. Investing the child tax benefit in your children's names.
6. Utilizing RESP contributions.
7. Payment of wages to family members (through a business).
8. Use of partnerships or corporations to earn business income.
9. Utilizing either inter-vivo or testamentary trusts.

While taxation can become complicated, depending on your budget, the fact remains that you must understand the basic concepts of tax deductions, tax deferral and income splitting (dividing).

Sometimes tax planning brings immediate benefits. Often, though, the benefits of tax planning come later. Now is the time to look ahead and determine how you can improve your tax situation.

The key foundation stones to effective tax planning include:

1. Maintaining good records.
2. Keeping informed and up to date on the latest strategies.
3. Understanding your needs and goals.
4. Assembling a team of good professional advisors.

How is Your Investment Portfolio Doing?

To make sure your portfolio is really working to your advantage, it's important to review it from time to time. Too many people ignore or neglect their portfolio, leaving it on auto-pilot. The idea that your money will just take care of itself can lead to a false sense of security. Don't make that mistake.

Below is a checklist to help you think about your portfolio, and determine what changes need to be made. The more your KNOW about your portfolio, the better equipped you will be to manage your investment portfolio.

- ❒ Know how much money you have invested
  - Review your most recent statements.
  - Does your statement provide your personal rate of return?
- ❒ Compare recent statements to statements from a year ago.
  - Determine how much you contributed and withdrew in the past year
  - Determine your profit / loss over the past year

  (Some statements give you this information for the past year)
- ❒ Keep your statements organized with a good filing system or a binder. Keep everything in chronological order.
- ❒ Develop a spreadsheet to track your portfolio over time. Separate different accounts (RRSP, RRIF, LIRA, TFSA, RESP, etc)
- ❒ Update the spreadsheet at least once per year.
- ❒ Set investment goals. Monitor these goals to see if you have achieved any of them.
- ❒ Complete a new risk tolerance questionnaire
- ❒ Compare the results to the last questionnaire. It may be a good idea to keep these questionnaires in your binder so you can see previous results.
  - Has your investment knowledge changed? If so, why?
  - Has your risk tolerance changed? If so, why?
  - Has your risk capacity changed? If so, why?
  - Has your time horizon changed? If so, why?
- ❒ Review the asset allocation
  - Do you have the right balance of cash, bonds and stocks?
  - Do you have the right geographic mix?
  - Do you have representation in different market sectors?
  - Do you have a cross section of different bond types?
- ❒ Review your investment plan or strategy. If you don't have one, it may

Portfolio Review Checklist

be time to get one.

- ❒ Do you have an investment Policy Statement (IPS)?
- ❒ Do you review your portfolio at least once per year?
- ❒ Do you rebalance your portfolio at least once per year?
  - Rebalance your portfolio using cashflow
  - Consider whether or not you sell high to buy low
- ❒ Review the quality of your investment holdings
- ❒ Review your research process
- ❒ Know the fees you pay on your investments

This list is quite comprehensive. Not everything will apply to you, but hopefully going through the list will encourage you to think about some of the things you need to know about, and monitor, with respect to your investment portfolio.

Many people do not have the time, expertise, knowledge resources or desire to manage a portfolio on their own. In such a situation, the services of a financial advisor can help. If you are using an advisor, though, it is just as important to review the relationship as it is to review your investment portfolio.

Are You Protected from Financial Disaster?

Chances are that you worked hard to build your wealth. It takes years to build wealth, and financial disaster can destroy it all too quickly. Protecting you and your family from financial disaster can be just as important as building wealth. Here's a checklist to determine how much protection you really have from life's unforeseen circumstances.

- ❒ Do you have an emergency fund of 3 to 6 months?
- ❒ Do you have other assets and savings to draw on in the case of an emergency?
- ❒ Are you covered if you get disabled and cannot work?
- ❒ Is your family protected if you die?
- ❒ Are you protected if your spouse dies?
- ❒ Do you have adequate life insurance?
- ❒ Are your debts insured in case of death or disability?
- ❒ Are you in control of your debts?
- ❒ Do you have a plan or strategy to pay off your debts and become debt free?
- ❒ Do you have an estate plan?
- ❒ Do you keep your financial documents in an organized fashion where others can find them in case of an emergency?
- ❒ Do you have a will?
- ❒ Is your will properly updated?
- ❒ Have you told your executor or loved ones where they can find your will?
- ❒ Do you have an enduring power of attorney?
- ❒ Do you have a personal directive?
- ❒ Are all of your beneficiary designations current and up to date?
- ❒ Do you have adequate resources to fund medial expenses?
- ❒ Do you have resources set aside for long-term care if needed?
- ❒ Do you have access to a line of credit for emergencies only?
- ❒ Have you reviewed the downside risk in your portfolio and considered whether or not it's appropriate for your circumstances?
- ❒ Do you have a few safe and relatively liquid investments to draw on in case of an emergency?

If you are exposed to too much risk, the time is now to make necessary changes to protect yourself from financial disaster.

Setting Financial Goals and Priorities

When it comes to personal finance, too many people wander aimlessly, focusing on the 'now' and everything that needs to be accomplished immediately. Setting goals is very powerful and can be very rewarding simply because it provides a foundation for future success.

Many people skip this important step on the path to financial independence or retirement. Of those who set goals, many do not set goals properly. Skipping the step of goal setting won't necessarily stop you from finding success, but that success is likely to come by chance instead of choice. Setting goals can increase the likelihood of success because it provides a plan to follow. This reminds me of the saying, "***People who fail to plan, plan to fail***."

FINANCIAL PRIORITIES

One of the challenges to the world of personal finance is it's such a big space. Financial planning can mean many different things. When I think of financial planning, here are some of the areas I think about:

1. Financial Organization
2. Debt management
3. Managing your spending
4. Saving money
5. Career and Work
6. Tax Planning
7. Retirement planning
8. Estate planning
9. Risk management
10. Investing
11. Saving for a child's education
12. Working with advisors

What are your financial priorities?

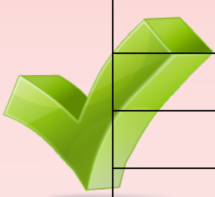
Setting Financial Goals and Priorities

SETTING GOALS

There are a few different approaches to this step. First, review the 12 financial areas again. Think about setting a goal or two in your areas of weakness, since weaknesses are easy places for improvement. Sometimes, it is hard to get motivated to work on your weaknesses, so the other area to set some goals around is your strengths. Even though these areas represent your strengths, it does not mean you cannot improve them.

Another approach is to consider areas you may not have a strong opinion about. It may be an area you have not thought a lot about, or an area that you don't have a lot of knowledge about. Setting research goals may be useful so you can learn more about finances.

Come up with a list of goals around your strengths and weaknesses. Remember that goals need to be specific and realistic. The best goals also set a time frame for accomplishment.



Setting Financial Goals			
WHAT IS YOUR GOAL?	WHEN DO YOU WANT TO ACCOMPLISH IT?	WHAT ACTIONS ARE REQUIRED?	PRIORITY

MONITOR YOUR PROGRESS

It's important to develop an action plan. Goals cannot be met without action. These actions need to be monitored. You can make your goals more manageable, in some cases, if you them down into smaller milestones. It's OK to make adjustments to your goals as necessary. Find a balance by setting goals that can be accomplished, yet that are still challenging enough to be rewarding and interesting.

Developing an Action Plan

The best idea is the implemented one

If you always DO what you have always DONE, you will always GET what you already HAVE. Financial success is simple, even if it's not easy. The things you need to do for success are not rocket science. You've heard these messages over and over again: Spend less than you earn, live within your means, pay yourself first, pay down your debts, know your spending, track your worth, get your financial house organized, prepare a will.

Even though you know what you need to do, change is not easy. In order to change, you must not only be aware that change is needed, but you must have the motivation to start. Even if you do get started, it can be tough to have the discipline to keep it going.

Just do it!

Nike said it best: Just do it! You are better to have done something and failed, than to have done anything at all.

Develop an action plan by making a list of three actionable items that you wish to accomplish. Write them on a piece of paper in large letters, and put that paper somewhere you look every day. Maybe it's the mirror in your bathroom, or on a yellow sticky note on your computer screen, or on the dashboard of your car. It's time to take control of your money by implementing all the great things you learned in your financial check up!

Good luck!

My Action Plan

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Jim is one of Canada's leading experts on money, retirement, investing and personal finance. He has a passion for teaching and helping people make better decisions with money so they can all retire happy and achieve financial freedom.

As a well-known financial speaker, he has entertained audiences large and small with his common sense, 'to the point' approach. Audiences rave about Jim's ability to take complex matters and deliver them in a way that makes sense. He believes that true success as a professional speaker comes not only from education, but also from entertainment and inspiration.

You can also find Jim's other products, including books, CDs, DVDs and financial tools, by visiting his other website www.RetireHappy.ca.