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The Benefits of Having a Comprehensive Financial Plan for the Average Consumer, And the Necessary Components Comprised to Make an Effective and Efficient Plan

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Abstract

Socioeconomic changes in American society over the past few decades, as well as an overwhelming amount of uncertainty and misconceptions, have resulted in a majority of Americans to fall short of their financial goals in the short-term, the mid-term, and the long-term. Without proper preparation and financial planning, it is likely that these Americans, and many more, will be unable to reach these goals as well as retire comfortably. Many Americans are overwhelmed with the immense amount of financial information, tools and resources, and as a consequence are unable to plan their finances efficiently and effectively. Americans need a better understanding as to which financial tools are most relevant to their goals, and the proper procedure to initiate a comprehensive financial plan for themselves. Understanding the benefits and drawbacks to each of the components of a comprehensive financial plan, and how they relate and complement each other, of a financial plan will greatly improve the numbers of Americans who are easing their way to a more financially predictable future.

Introduction

Comprehensive financial planning has a different meaning to everyone, but it is very uncommon to find an American consumer who has a full grasp on what it actually means. There is a common misconception between saving and investing, and financial planning. The former is simply funding savings and retirement accounts, and many consumers in America participate in that sort of fundamental planning. Comprehensive financial planning, on the other hand, is a whole new ballgame, and is much more advanced and effective. In the general sense, it involves strategies and financial tools that allow the consumer to achieve their financial goals and in turn diminish one of the most stressful worries throughout their life: lack of money. The most important idea to realize and keep in mind about a comprehensive financial plan is that it is like a well-oiled, working machine, and that each component to this machine is crucial in order to maintain its functionality, effectiveness, and efficiency. If one or more of these components ceases to work, the financial plan is at risk of ceasing as well. It is the combined efforts of the consumer, as well as the financial advisor if commissioned, to not allow this to happen.

A fully functioning comprehensive financial plan is one which will accumulate wealth most efficiently and will proficiently manage risk along the way; with the ultimate goal of making the consumers financial future as predictable as possible. What makes a financial plan fully comprehensive is that it supports the consumer financially throughout every major step in his life in accordance to his individual-specific goals; typically categorized as short-term, mid-term, and long-term goals. There are two main portions to a comprehensive financial plan; defensive, or risk management, and offensive, or wealth management. The defensive portion is in place in case the worst case scenario were to occur; death, sickness, injury, or any other obstacle that would prevent the ability to work. The offensive portion, on the other hand, is used to accumulate wealth through investments and retirement planning, which play a vital role in achieving the specific financial goals. This part of the plan is more exciting, and allows the consumer to seamlessly ease into the next step, or next big purchase, in their life without the worry of affordability. A comprehensive financial plan allows the consumer to have a much more predictable financial future. It is as relevant to the goals and current financial situation the consumer is currently in, and is managed and updated according to any sort of change in life; whether it be a big life change such as a promotion or a newborn child, or a small one such as a change of goal or subtle alteration in the plan. The plan is routinely stress tested in certain situations having to do with stock market performance or current tax rates. For instance, if the stock market fails, the plan is diversified enough that regardless of the potential loss incurred in market-related investments, there is still a sum of easily accessible money taken from a different, unaffected tool in case of any type of emergency, such as cash value life insurance which is not linked to the market. In time, the stock market will bounce back, and the consumer will have zero *actual* loss in market investments while still taking the necessary emergency money out from a separate “nest egg.” If planned out extensively and done correctly, a comprehensive financial plan will allow the consumer to take care of himself and his family as efficiently and effectively as possible, with as little *actual* loss as possible.

There are many concepts that will be discussed about the idea of comprehensive planning and whether or not it will truly benefit American consumers and the current crisis American citizens are in, which will be discussed in the next chapter. Some of the concepts revolve around the decision to start a financial plan; why it is so important nowadays to have one, and why a majority of Americans either don't have one, or have one that needs improvement. There are also concepts as to what the tools, resources, and strategies are that truly make a financial plan comprehensive, as well as efficient, effective, and relevant to the consumer. The final concept that will be discussed is how an American consumer can use those tools, resources, and strategies in such a way as to create the most efficient comprehensive financial plan in relation to their goals. These tools will be discussed in accordance to the time line of goals that they help to reach and achieve; short, mid, long-term. One of the main goals of this topic is to educate Americans, regardless of age or background, and prevent further misunderstanding and misconceptions of comprehensive financial plans. America is currently in a financial crisis, especially on an individual level, and with the knowledge of the options and choices that can be made to reverse this dilemma, perhaps this generation will be the leader of many more to be debt-free and financially prepared through every stage in life.

Socioeconomic Changes in America

It is very important for Americans in this society, amongst other times in history, to have their own comprehensive financial plan due to many socioeconomic factors currently changing the nation as a whole, as well as the way people think about their finances; Social Security dying, lack of pensions, and an increase in life expectancy. According to a 2012 study by Newsmax Finance, “Social Security is failing even faster than we thought. The Social Security Administration [in 2011] reported that the fund will probably run out of money in 2036”.[1] As the article continues, each year brings a new, less-distant estimate as to when Social Security will cease to exist. These falling estimates emphasize the fact that when workers retire, they will not receive the full Social Security benefits they were expecting and hoping for. “When the Social Security trust fund starts running on empty, it will probably slash benefits by about a quarter. Prospective retirees will need $92,175 in additional savings to fill that gap. With Social Security on borrowed time, workers must start saving now or they won’t be able to make up for lost time” (Kling, 2012). Workers who are expecting these benefits have prepared their future around it, and with the fund estimated to run out of money in only twenty years; a number which continues to drop, workers currently as old as forty-five years old must now find other ways to save money to support themselves through retirement.

[1] Kling, Michael. "Social Security May Be Dying Even Faster Than We Thought." *Newsmax.* 17 Feb. 2012. Web. 30 Nov. 2015.

The second socioeconomic change that has been affecting savings strategies for Americans is the decrease in careers which offer pension plans upon retirement. Based on an article by Emily Brandon on behalf of U. S. News[2], less than a third (31 percent) of employees in America were offered a traditional pension in 2010, and only 28 percent of those employees participated. This number decreases dramatically if an American is not in a union, is a private industry worker, works in a pension-less industry, is traditionally not a long-term employee, doesn't work full-time, or lives in an area where pensions are not prevalent such as the southern United States. Furthermore, the U.S Social Security Administration: Office of Retirement and Disability Policy admitted that "the percentage of workers covered by a traditional defined benefit pension plan that pays a lifetime annuity, often based on years of service and a final salary, has been steadily declining over the past 25 years. From 1980 through 2008, the proportion of private wage and salary workers participating in defined benefit pension plans fell from 38 percent to 20 percent".[3] The article continues by explaining that this shift is attributed to a number of factors; government regulations which decreased employer incentives to maintain such plans, the employment-sector shift away from manufacturing toward service and information technology which decreased availability of pensions, and worker demand preferring plans which are portable across jobs, with balances more transparent, and with assets managed by the employees themselves. It is unsure

[2] Brandon, Emily. "7 Reasons Why You Don't Have a Pension." *US News.* 11 Feb. 2011. Web. 30 Nov. 2015.
[3] Butrica, Barbara, et. al. "The Disappearing Defined Benefit Pension and Its Potential Impact on the Retirement Incomes of Baby Boomers." 2009. Web. 26 Nov. 2015

where pension plans and their availability will be in the future, but for the past few decades they have been on a constant downward spiral and Americans in this current society must understand and prepare for their future financial situation and retirement as if pensions cease to exist. The final socioeconomic change in America which is changing the way its citizens must prepare for retirement is the ever-increasing life expectancy of American people. An article from USA Today[4] explains that life expectancy in the United States as of 2012 rose to an average of 78.8; a record high. Although this may be one of society's greatest achievements in the 20th century, it also has its downside; American consumers must now save more money than ever for retirement. As years pass and there are breakthroughs and innovations with medicine and technology, the life expectancy of American citizens will continue to rise. However, if the retirement age remains at 65 years old, then those years added on will simply lengthen the amount of time in retirement; when one does not work, has no constant stream of income, and relies on their prepared savings to survive. It is difficult to say when someone will perish, but it is important that he plans for anything; in this case living past life expectancy. These three socioeconomic changes in today's American society relevant to a majority of Americans, and explain why it is most important now more than ever to understand and prepare for future financial issues and retirement using the tools, resources, and techniques of today's financial planning.

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[4] Copeland, Larry. "Life Expectancy in the USA Hits a Record High." *USA Today*. Gannett, 9 Oct. 2014. Web. 25 Nov. 2015.

Financial planning is an idea that many people may think is extremely important and necessary in order to get by comfortably in every stage in their lives; however, very few people fully act upon it in a timely fashion. People want to save money and have some sort plan for their future finances, but they tend to push it aside for another day. There are many misconceptions and ideas that allow them to think that “now” is not the best time, of which we will touch upon. In a sense, saving money is like breaking an old habit. They spend their entire adolescence and young adulthood worrying very little about how they can afford their next big purchase or prepare for the next big step in life; buying a new car, a new house, a wedding ring, their children’s education, their second home. They either lack the knowledge, tools, and resources required to fulfill and maintain a comprehensive financial plan, they simply do not have the time it takes to get one running and fully functional, or they do not understand the immediate importance of their financial planning. One of the key concepts to understand is that it is never too late to begin financial planning, but more significantly it is never too early. The reason why it is extremely important to get an early start on financial planning and saving is not only to start the habit, but more significantly to take advantage of compound interest. As an example of its power, imagine a consumer who has an account with 8% rate of return, and wants a million dollars in that account by the time he turns 65 years old. If he begins saving at 25 years old, he would only have to put $250 into that account each month to reach that million dollar goal. However, if he waits ten years until the age of 35, the monthly contribution increases to a little less than $750; almost triple of what he needed contribute a decade ago. Now, he waits another ten years, and starts saving at the age of 45. In order to reach the million dollar goal, he would have to quadruple his contribution from a decade ago and put in roughly $3,000 every month to reach that goal. This perfectly exemplifies the power of compound interest, and it is a power that every American has the capability of harnessing. If this knowledge was more well-known, Americans would have a higher sense of urgency to begin some sort of saving.

The most successful consumers, in terms of financial planning, are the ones who understand the importance of saving and budgeting, but most importantly are the ones who have a good head on their shoulders and are very forward-thinking. These consumers sacrifice overindulgences in unnecessary luxuries and spending in the present in order to ensure a consistent comfortable living in the future. They understand the comfort level of the life they want to live both while in the workforce and during retirement, and they budget themselves strictly in order to fulfill those comfort levels throughout their lives. Getting an early start to a comprehensive financial plan is one of the most important and beneficial concepts, and nearly every tool and strategy used will benefit greatly as time goes on.

There is a significant amount of Americans who either need help improving their financial plans, or simply have not begun their saving process.

According to a study released by Northwestern Mutual[5] in 2015, some 58 percent of Americans believe their personal financial planning efforts need improvement, but over a third, 34 percent, of Americans have done absolutely nothing to plan and prepare for future finances and retirement. This study was conducted by Harris Poll, and is based on an online survey of 5,474 American adults ages 18 and over. The survey results were weighted to U.S. Bureau targets for education, age and gender, race and ethnicity, and region and household. The study found that there is a deep disconnect between what Americans should know about their financial planning and what they are actually doing, in terms of saving and financial planning, to reach their goals. For example, 67% of Americans consider themselves to be adequate savers; however, 54% of the American population has a level of debt that is equal to or greater than the amount they currently have in savings. This shows that there is an inconsistency with what Americans believe is an ideal amount of savings necessary to cover their current and future expenses. A consumer cannot solve this problem unless there is first an understanding of the situation he is in. When in debt, it is important to know that that debt will steadily increase through time as interest compounds, so the consumer must pay off the debts as soon as possible. It is easier said than done, but any unnecessary spending will make the situation worse, so there must be a great deal of discipline in order to move towards a debt-free life. Without the proper understanding and preparations for this situation, the amount of debt lingers throughout their lives

[5] Robaton, Anna. "Study: 33% of Americans Have No Financial Plan. " *CNBC.* 29 Apr. 2015. Web. 25 Nov. 2015.

and remains comparable to the amount of savings one has for some time. This means that for years, possibly decades, these consumers are forced to pay off their debts rather than begin to save for their future, like a candle burning at both ends. By the time these Americans finally pay off their debt, there is little or no time to prepare for retirement. Although this is a huge problem for the individuals, two in five Americans with debt-related problems have not discussed or evaluated their financial struggles with anyone; neither loved ones nor professionals. Additionally, 21% of Americans firmly believe they will never reach their financial goals. Many Americans are so overwhelmed with their situation and they amount of information, tools, and resources at their disposal that they sift through such information in order to make decisions that they think will better themselves financially, which unfortunately is not always the case. Without proper procedures, such as professional help and advice, many more Americans will enter retirement at a later age, with little to no personal savings, or even still in debt.

In conclusion to the results of the survey, Americans need help digging themselves out of a hole. They need to understand the financial situation they are currently in, and not allow another day to pass without consulting their loved ones about it, but more importantly for their financial future; a professional working in the field of financial advisory. Another key takeback from this survey is that in order to be financially successful, one must set goals and priorities, and also hold themselves accountable to either making or missing said goals. These goals can be as current as saving and paying off debt, or as forward-thinking as preparing for retirement. Once these goals are set, it is then important to determine what steps to take to work towards those goals. When a consumer possesses a set plan with concrete steps and ideas, the chance of reaching financial success grow immensely.

Why Many Americans Do Not Have Financial Plans

As recently discussed, there are massive proportions of Americans who currently need improvements with their financial plan, or who need to start one from scratch. It is extremely important to lay out the reasons as to so many American consumers do not have a fully functional comprehensive financial plan, and explain where exactly the faults in the reasons are. It will become evident that there are very few reasons in the end for American consumers to withhold having a financial plan.

There are numerous myths and misconceptions as to why many Americans have done little to no planning. Many of these misconceptions are obvious and relevant, but others are not so much. The first and most common reason, especially with young adults who have just joined the workforce, as to why many Americans cease to have a plan is because they believe they currently do not have enough money to start a financial plan. They believe they need personal wealth first and a financial plan second, but ironically this is completely backwards. Although initially having wealth will benefit a “newly born” financial plan, proper comprehensive financial planning will lead people to create wealth, which can then fuel a larger, more efficient plan in a snowball effect. In short, a comprehensive financial plan is in place to grow any sort of wealth currently owned. Although not having much wealth will yield a slow acting plan at the beginning, that additional capital gained from starting early with have profound effects on total accumulated wealth, the process of which will be discussed in a later chapter.

An additional misconception to the personal wealth aspect is that many Americans believe there is a "minimum investment requirement" in order to work with a financial planner. There is some truth to that, as many financial planners hold their standards higher and expect to work with more wealthy, successful, and potentially risky clients, and therefore require immense amount of investment in order to make their professional time, as well as their clients', worthwhile. However, since the middle class is the largest economic class in America and therefore represent the average consumer economically, there are many financial planners in the business who do not have a minimum investment requirement, and are extremely willing to guide clients through investment strategies with whatever amount of money they want to invest. However, if a consumer is not quite ready for an advisor and still wants to make an investment in order to increase his or her capital, each investment vessel has its own minimum investment requirement variations. For example, one of the most common investment tools is mutual funds, which is a professionally managed investment program that is funded by shareholders or investors that makes trades in diversified holdings. Although most consumer mutual funds require an initial $500-$3,000 initial investment, there are options and choices one can make when choosing the mutual fund that require an investment as little as $100, $50, or even as low as $25 each month, such as the mutual fund TIAA-CREF. The same sort of layout goes for most other investment tools; larger firms have higher minimum investment requirements, and smaller firms have lower minimum investment requirements. This goes to show that although one's capital may not be great yet, he can still invest that money proportionately. Through time, his capital will grow, and so will his investment amount.

Another main reason why many Americans have done little to no preparation towards a fully functional and well-oiled comprehensive financial plan is because they believe they have the time, resources, and knowledge to manage their own finances themselves, furthermore that their financial situation isn't complicated enough that they can't personally handle it. Although deserving of credit for attempting to make themselves financially stable through hard work, learning, and dedication, and actually applying themselves with a start to a financial plan, there are always gaps and adjustments that can be made to make the plan more efficient and relevant to one's current situation. Life is always changing, so therefore so is one's financial plan. What was current mere months ago may not be current for them today. There comes a time when managing one's own financial plan becomes a second job, and may become overwhelming. At this point, it may be best for those dedicated and ambitious Americans to seek some sort of financial advice. Professional aid and advice will only better what has been started, and will further it to being the most efficient financial plan one can have. No plan is perfect, but with much help, as well as multiple points of view considering the best options, the plan will continue to strive towards its utmost potential.

As for the consumers who have yet to begin their financial plan, and believe they are mentally and physically capable of starting one and keeping it up to date throughout the course of their lives, their head is absolutely in the right place, but there are some things to discuss before a consumer begins this journey. First off, consumers must realize how much time and effort is put into customizing, applying, and managing a financial plan is until they attempt and witness it themselves. It is also extremely important to know one's limits. A consumer may be the most productive salesman, the most influential professor, or a renowned doctor; it is common for people to apply how much they know in a certain field, and transcribe that to their ability to manage their finances and keep their financial plan as relevant and up to date as possible. It may seem as though when a person attempts to manage his or her own financial plan, that they will be financially set if they routinely manage that plan. Although they are in much better shape than the Americans who have done no planning at all, more than half of these consumers' financial planning efforts still need improvement, based on the study by Northwestern Mutual previously discussed. When one tries to manage his financial plan by himself, without the help of a financial representative or advisor, he can miss proper techniques, tools, and advice from a professional who advises finances for a living. The steps and applied tools missed due to lack of knowledge and resources can be anywhere from applying the most efficient savings product that can earn an additional 3% return; which in the long run is life-changing, to a miniscule miscalculation that alters the amount of money into a certain tool which can add hundreds or thousands of dollars of unnecessary expenses through the years. Any plan done by oneself is technically a financial plan, but with the help of a professional in the financial planning field, the plan can turn more efficient, and most importantly comprehensive, and the consumer will have a more finically secure and predictable future.

The final reason that will be discussed as to why many Americans lack financial planning is that a majority of them need some sort of professional advice to get started or improve their current plan, yet they have a difficult time trusting anyone who is trying to help put their money in the right places. Skepticism for financial planning and the professionals who work in that field is at a very high level, due to relatively recent headlining activities of fraud, such as the Madoff Investment Scandal[6] which came to light in December 2008. In this scandal, former NASDAQ Chairman Bernard Madoff and founder of the Wall Street firm Bernard L. Madoff Investment Securities LLC, admitted that a major part of his business, the wealth management arm, was nothing more than an elaborate Ponzi Scheme; stealing approximately $64.8 billion from the accounts of his 4,800 clients. Although instances and scandals like this are rare, it is understandable that such events have made Americans hold on a little tighter to their money, but with proper research and recommendations one can find the most reputable and reliable financial planning firms that have the client history and fiduciary standard ratings to prove it. Some firms have been around for over a hundred years, with hundreds of billions of assets in their portfolio to back up

[6] Yang, Stephanie. "5 Years Ago Bernie Madoff Was Sentenced to 150 Years In Prison - Here's How His Scheme Worked." *Business Insider.* Business Insider, Inc, 1 July 2014. Web. 24 Nov. 2015.

their financial strength and trust, such as Northwestern Mutual. At the end of the day, every option or suggestion made by a financial advisor is not a concrete step in the plan; the consumer is the one who officially makes every decision and puts any amount of money he wishes into the places he wants it to go. The suggestions are clean cut and transparent, with little to no ambiguity or fine print, due to regulations in the field and the nature of most of these tools.

Many consumers don’t understand that if they manage their own financial plan, the one they need to trust the most is themselves. As human beings, we are emotionally attached to our money. We want it close and easily accessible and if things go downhill, we want to cash out and make sure we have some money to spend in the harshest of times. This idea is related to the stock market. Historical data shows that the stock market decreases on average three out of every ten years[7], but there has never been an overall net decrease in the stock market over a fifteen year span. As an investor of one’s own money, he is more likely to take the money out of the market when there is a sharp decrease in the market or his share value as a safety precaution. When one does this, he experiences an *actual* loss in wealth when he takes the money out. When the consumer entrusts his investment with a professional; however, he knows that the loss experienced when the market decreases is not an actual loss if the money in the market, and that the decrease in total market or stock value is only temporary. The professional is trained to understand the inner workings of the market, and unless there is an absolute

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[7] Conerly, Bill. "What's Next For The Stock Market After A Big Drop?" *Forbes.* Forbes Magazine, 24 Aug. 2015. Web. 25 Nov. 2015.

desperation for the money and it is needed immediately without any other more viable options, the money will stay in the market and it will increase in value in time. As an example of the importance of keeping money in the market regardless of market performance, consider the housing market. If one buys a house that is valued appropriately at $750,000, and the housing market crashes, the house will decrease in value to, say, $500,000. This decrease in value does not mean the house gets smaller in size or that there is a physical change that decreased the value; it only means that the home owner will experience the *actual* loss of property value if he sells the house for anything less than the initial purchased price. As long as he continues to own the house, he will not experience any loss, and eventually, due to historical trends, the house will regain its initial value, and may even be valued at a higher price in the future. Subtle details and knowledge like that can make or break the final return of one's investment, and can ensure the highest rate of return for the money put in.

The Tools That Comprise a Comprehensive Financial Plan

Now that it has been discussed why many Americans lack comprehensive financial planning, it is time to take a look into the tools, resources, and advice that should be used in order to make the plan the most efficient and effective it can be. It is important to understand that there is no perfect financial tool available; there are benefits and drawbacks to each and every one of them. An idea which encompasses this fact is that there is a negative correlation between liquidity and efficiency. Liquidity is the ability to quickly convert an investment or portfolio to cash with little or no loss in value. Efficiency relates to the rate of return; a higher efficiency of a tool yields a higher rate of return, and vice versa. Investment tools which are the most efficient are typically the least liquid, such as retirement plans. On the other hand, tools which are most liquid are usually the least efficient, such as cash savings. Although not every tool will be relevant to any given financial plan and its goals, it is important to evaluate the main financial tools which belong in a comprehensive financial plan.

The first financial tool that will be discussed is one that has capabilities which the average American consumer may not be aware about; life insurance. There are two main types of life insurance; term and permanent.[8] It is easier to understand the differences between the two by relating them to the housing market; renting and owning a house. With term insurance, the consumer is renting the policy for a specific period of time; he pays the premiums and is covered up

[8] Magni, Peter. "Whole Life vs. Term: There's a Clear Winner Here." 19 June 2013. Web. 25 Nov. 2015.

until the policy expires. When the policy does expire, he is no longer covered and must purchase another policy to be covered again. Permanent whole life insurance is much like owning a house. It is much more expensive, but the payout in the long run is much greater. This policy stays with the owner until he passes away, it builds equity, and in emergency situations it can be held as collateral in case a loan is necessary.

One of the most integral components to a comprehensive financial plan is whole life insurance, otherwise known as cash value life insurance. According to an article on behalf of LifeHealthPro, "cash value life insurance offers great competitive advantages versus alternative financial assets. These advantages fall into three major categories: 1) Tax advantages 2) Financial and actuarial advantages and 3) Legal and contractual advantages".[9] It has a vast array of benefits; offensive and defensive, as well as in the short, mid, and long term. On one side, the defensive side, it is a life insurance policy that lasts the policy owner's entire life; regardless of when he lives past his life expectancy or not, his family or loved ones will be paid a death benefit. Although a morbid thought, and may not be applicable to every consumer, this will ensure that the family will be taken care of financially if the worst case scenario were to occur. On the other side, the offensive side, this policy begins building a cash value portion; a sum of money that is contractually guaranteed to grow tax-deferred throughout the lifespan of the policy, and is available to be withdrawn by the consumer at any

[9] Towers, Russell. "Here's Why Cash Value Life Insurance Is a Superior Product." 26 Feb. 2015. Web. 25 Nov. 2015.

time. This policy also distributes dividends to its policy owners; which may be cashed as a check, or reinvested in the policy to further increase the cash value. It is important to note that the cash value sum is guaranteed to grow at a rate that outpaces inflation; a problem which many tools in a financial plan faces. This policy is funded with after-tax dollars, so any withdrawal from the cash value, as well as the death benefit, is tax-free to the recipients. Additionally, this growth of the cash value is not tied to the market, but rather to the entire portfolio of the company which issued the policy. When the value of the market decreases, the cash value continues growing at the same rate, which makes it relatively more valuable at this time.

The term insurance, on the other hand, is much less practical in relation to whole life insurance. Costing a fraction of the price of whole life insurance, term insurance is purchased at times of large purchases, such as a second home, so that the family or loved ones will not incur a financial burden in case the policy owner were to pass away. The sole reason one would purchase term insurance is precautionary; to leave a death benefit for loved ones in case of premature death. Although it is not as useful as cash value life insurance in the long run, it compliments it very well in a comprehensive financial plan.

The third type of insurance is the most important part to the financial plan as a whole; income protection, otherwise known as disability insurance.[10] Disability insurance is cheapest component, yet has the largest impact by

[10] Steuer, Tony. "Why Disability Insurance Is More Important Than You Think." *Financial Wellness Work.* 13 June 2012. Web. 25 Nov. 2015.

promising to pay a majority of the salary of the consumer in case there is an inability to work; either from sickness or injury. It is the most important aspect to the plan because the plan, and all the hard work put into it, would slowly crumble without a constant stream of income. Not only would there be no constant flow of money being invested or expensed into certain tools of the plan, but money would soon be taken out of the components to cover expenses throughout the recovery period. The entire plan is predicated on the salary, so as long as money is coming in through disability insurance, the financial plan as well as the standard of living of the consumer and his household will remain intact and relatively unchanged.

Now that the insurance policies have been discussed, it is time to change pace and move on to the major investment components of a comprehensive financial plan. One of the most common forms of investing are buying stocks or putting money into mutual funds, and can be extremely rewarding with patience and discipline. These two investment tools are related, moreover intertwined. Mutual funds are classified by share class; A, B, and C shares. There are striking differences between these three classes, and knowing the difference will help preserve wealth and maximize returns.

Class A shares come with "front-end load fees" of up to 5 percent, which means that there is a fee up to a given percentage of the entire purchase price. However, although these fees are larger than the other classes', they are offset by lower ongoing maintenance fees and discounts for high-value initial investments. The higher the initial investment, the lower the front-end load fee will be. Class A shares are meant to be ongoing, for years or decades before being sold. With the initial front-end load fee and low maintenance fees through their lives, Class A shares are meant to be long-term investments. Class B shares are quite different than class A shares. They do not have front-end fees; however, they do have back-end fees, meaning when they are sold, there is a fee up to a given percentage of the fund's total balance that must be paid to the firm. It is important to note that after a certain amount of time, B shares convert to A shares. Class C shares differ the most out of the three classes. These shares do not have required front-end load fees and generally have very low back-end load fees. However, to compensate for this, Class C shares haven't relatively high ongoing maintenance fees and expense ratios. Due to these distinctive traits, Class C shares are meant to sold within a year or two of purchase; yielding a quick profit for its shareholder.[11]

The final investment component that is crucial to the comprehensive financial plan is retirement planning. The two main retirement plans available are the 401(k) and the IRA, or individual retirement plan. A 401(k) is a retirement savings plan sponsored by an employer and allow the consumer to save and invest part of their paycheck in the stock market before taxes are taken out; however, when the money is withdrawn at retirement it will be taxed. In most companies, the employer will actually match the consumer's contribution to his 401(k) up to a certain percentage. One of the many benefits to a 401(k) is that it is possible for the consumer to control how the money is invested, and there are options to

[11] Hirby, James. "What Is the Difference Between Class A, B, and C Mutual Fund Shares?" *The Law Dictionary.* 11 Mar. 2013. Web. 25 Nov. 2015.

choose from. Most plans allow the consumer to invest in mutual funds which are composed of bonds, stocks, and money market investments. The option which is most favorable is investing the money in target-date funds. Target-date funds are a combination of bonds and stock which gradually become more conservative as time goes on. The reason why this is preferred is because as the investor ages, he has fewer years for the market to reach its peak. For that reason, he must choose a more conservative route as he reaches his retirement years in order to receive the highest rate of return on his investment. There are drawbacks to owning a 401(k). For instance, the consumer must work for an employer for a certain amount of years in order to qualify for the employer's matched contributions. Another drawback to a 401(k) is that there are strict rules as to when one can withdraw his money in the account; money withdraw before the age of 59½ will be subject to a 10% penalty as well as taxed. This will be an advantage in the long run; however, due to the negative correlation between liquidity and efficiency. Retirement plans will be the components with some of the highest rates of return in the comprehensive financial plan. There is also a limit as to the amount of money one can put into a 401(k) in a given year; $18,000, or $24,000 for participants over the age of 50.[12] Money in these accounts grows tax-deferred and can be rolled over into an IRA if the consumer is terminated from employment.

There are many similarities between the 401(k) and the IRA, such as the 10% penalty for a withdrawal before the age of 59½; however, there are major

[12] Miller, Stephen. "For 2015, 401(k) Contribution Limit Rises to $18,000." 23 Oct. 2014. Web. 22 Nov. 2015.

differences as well.[13] The most striking difference between the two is the IRA is not set up with an employer; rather it is set up with a third party company. There are also differences in contribution limits. With an IRA, the contribution limit for participants under the age of 49 is $5,500 a year, while participants over the age of 50 have a limit of $6,500 a year. There are two types of IRA's; traditional IRA and Roth IRA. The traditional is similar to the 401(k) in that it is funded with pre-tax dollars, and at the time of withdrawal, it is taxed at the then-current tax rate. The Roth IRA, on the other hand, is funded using after-tax dollars, and thus upon withdrawal, no taxed will be taken out. The latter benefits younger consumers. These consumers are new in the workforce, and hence are typically at the lowest paying positions and are in the lowest tax bracket. It is at this time that the consumer wants to pay his taxes; when they are the lowest, for he knows that as times passes and he assumes higher professional positions, his salary and tax bracket will also increase. However, at this time in his life, he has already paid taxes on his IRA account, so it does not matter how high his tax bracket is; he will receive his retirement savings tax-free with a Roth IRA.

No component to a comprehensive financial plan if flawless; each are either not liquid of efficient enough, have penalties if prematurely withdrawn from, have limits on contributions, cater to one timeframe and not the others, and many more drawbacks. If used effectively, and understanding where those flaws lie and where other components of the plan can make up for those flaws. Taking

[13] McKittrick, Leo. "The Differences Between a 401(k) and a Roth IRA." *BiS*. 31 Oct. 2012. Web. 24. Nov. 2015.

advantage of what each and every tool and resource has to offer will make the financial plan as efficient and effective as possible in terms of providing the consumer with a predictable, stable financial future.

The Importance of the Design of the Comprehensive Financial Plan

With the details and understanding of each of the major components with comprise a comprehensive financial plan, it is time to see how each of these components relate to and complement one another to form a well-oiled financial plan. It is important to note that these financial tools, more specifically the investment tools, belong in specific timeframes, and the amount of capital investment in each timeframe and tool is completely dependent on the financial goals of the consumer. Although some tools are in more than one timeframe, each one belongs in its specific place mainly due to its efficiency and liquidity, amongst other attributes. Before a comprehensive financial plan can exist, there must be much thought put into it. How diversified should it be? Does it make sense to incorporate every tool? What goals should it achieve? How risky or conservative should the plan be? Once questions like these are answered, it will give the consumer a better judgement and understanding as to how he would like his plan to be structured, and how much each tool will relate and complement one another. It is at this point that the most effective and efficient financial plan can be constructed.

As previously mentioned, the most important idea to understand is that it is crucial that the consumer not put “all their eggs in one basket.” For example, if a consumer chooses to put all of his invested money in the market, and the market crashes, then he experiences an *actual* loss in his investment and loses capital. However, if the consumer has a diversified portfolio, with money in the market as well as other areas not directly linked to the market, then there is virtually no risk in the investment as a whole. Using every component and resource at one's disposal will ensure the most predictable and efficient financial future. Every tool has its benefits and its drawbacks- not one of them is perfect in every way. If the consumer spreads his wealth amongst many different tools, then he can choose what accounts to use at the most financially beneficial time, taking advantage of the tools when they are at that time the most advantageous.

It is important to discuss in detail how these tools vary in time with regards to when the most beneficial time is to use them. All of these tools are either taxed or not taxed when the consumer withdraws cash from them. Additionally, these tools are either tied to the stock market or they are not. Throughout time, the tax rate and the value of the stock market fluctuate often, and it is extremely difficult to estimate when either will be on the rise or the fall. Due to this uncertainty, it is ideal to be prepared for every scenario. For example, if the tax rates are high and the stock market is low, it is ideal to avoid any money tied to the market so that no loss is incurred, as well as avoid any money which could be taxed. Although this does not seem like a model situation, if the plan is diversified enough and has a cash value life insurance policy, then the tax rate and market value is irrelevant. The policy is not tied to the market in any way, and it has been funded with post-tax dollars, so any withdrawal is tax free. There are solutions to every scenario involving fluctuations in tax rates as well as market value. As long as the financial plan is diversified enough, and has been stress tested for each scenario, the consumer will incur as little loss as possible when in dire need of money. This idea will develop further as the tools to use in a comprehensive financial plan are discussed.

Before a financial plan is put into place, many things, goals, and ideas must be established and discussed. These details must be discussed and analyzed because this plan belongs to the consumer and the consumer only, and must be customized to his life, his goals, and his financial situation. The most important discussion to have before setting up a comprehensive financial plan revolves around the personal, professional, and financial goals in mind. It is equally as important to put a time frame on those goals as well; short-term, mid-term, long-term. The reason for this is because with every tool used in the financial plan, as previously mentioned, there is a negative correlation between efficiency and liquidity. This means, simply put, that if the money is accessible today, such as in a savings account, there is a low rate of return on that money, ranging below 0.5%. However, if the money is in a retirement account that can't be withdrawn penalty-free until the age of 59½ , there is a much higher rate of return, typically between 7-10%.[14] With that being said, putting money in the proper places in accordance to the set goals, whether they be near sighted or far sighted, is one of the most important steps to creating and managing a comprehensive financial plan.

Other ideas to discuss and put thought into that will further customize and, in turn, make the plan more efficient and effective are how well of a saver the

[14] Brandon, Emily. "11 Ways to Avoid the IRA Early Withdrawal Penalty." *US News.* 23 Sept. 2013. Web. 24 Nov. 2015.

consumer is, how risky or conservative they would like to be with their invested money, and what their situation currently looks like; personally, professionally, and financially. Topics discussed in that conversation consist of employment, salary, savings and investment accounts, existing debt, dependents, and any insurance plans currently in place, just to name a few.

A comprehensive financial plan is most easily split up into two categories; defensive planning and offensive planning. Although there is some crossover between the two with certain tools and techniques, it is very important to have a completely separate planning strategy for each category. The defensive takes place in the short term; however, the offensive can split up into timeframes in accordance to the goals of the financial plan. Defensive planning has to do with risk management and cash and debt management. The defensive planning is to ensure that if the worst case scenario were to happen, such as death, injury, or illness, then the consumer and his household can continue to live and maintain the same standard of living. It may not be the most attractive part of the planning, quite frankly it is the most morbid, but it is a conversation that is necessary to have, especially if the consumer has a family to take care of and put food on the table for.

The three main components of the defensive side of the financial plan are disability insurance, an emergency fund, and life insurance. As previously mentioned, disability insurance, or income protection, is the most vital part to the comprehensive plan as a whole. It should be the first policy purchased and fortunately, it is the least expensive components to the plan. Many tools require constant payments in order for them to continue producing results and yielding the highest rate of return on invested money. The entire plan is predicated on the consumer's salary and constant stream of income. If injured or sick and unable to work for a period of time, the consumer will eventually begin to drain his financial plan in order pay every day expenses to keep a roof over his head and food on his table. To make matters worse, money taken out of certain accounts may be subject to actual loss, taxes, and ever penalties. With disability insurance in his financial plan, the consumer can expect to receive payments exceeding 90% of his original pay. The policy owner can never expect to receive disability benefits equal or greater than his original paycheck because the insurance company must provide some sort of incentive for the consumer to want to get back to work with his usual pay. The other downside to owning a disability insurance policy and needing to use it is the elimination period; the consecutive amount of time between an injury or sickness begins and receiving disability benefit payments from the insurer. This is to ensure that the policy owner is without a doubt sick or injured enough to be able to work for an extended period of time. There are ways to decrease the length of the elimination period; however, the premium costs of the policy will increase proportionately. The solution to this downside is simple; an emergency cash savings account. Since the average elimination period is 90 days, the rule-of-thumb amount to keep in the emergency fund is no less than three to six months' worth of total expenses; including financial plan expenses and premiums, mortgage, car payments, groceries, etc., or

$10,000; whichever is greater. That number grows to $20,000 if the consumer is married with a family. With the emergency fund and income protection in place, the consumer and his family are financially protected in case he is physically unable to continue working, regardless of the cause. Disability insurance is in place to protect the consumer's most important asset; his current and future earnings.

The last component to the defensive, risk management side of the financial plan is life insurance. Life insurance in the defensive sense is particularly important if the consumer has a family. Simply put, if the consumer owns a policy and passes away, the family or loved ones will receive a tax-free death benefit from the insurance company. Although it will not take the place of the loved one, it will help compensate and fill the financial burden created due to his death. Life insurance is not meant to make the family or loved ones rich; it is a carefully calculated death benefit that will cover future expected costs, with little left over. These costs are typically monthly expenses, total debt to date, future education for children, and funeral costs for the deceased. As previously mentioned, there are two types of life insurance policies; term and permanent. It is important and useful to compliment permanent with term insurance in a financial plan, because the death benefit for the permanent insurance will steadily increase through time and the term insurance is much more affordable; coming in at a fraction of the price. Additionally, the term insurance is useful at the time of a major purchase or around the time of a birth of a baby, for if the policy owner passes away around these times then the family must incur an unaccustomed and substantial expense, thus creating a financial burden.

It is relevant and organized to categorize the offensive, investment components of the financial plan in their respective timeframes; short, mid, and long-term. The short term is defined as any amount of time shorter than five years, and goals and tools that would fit in that timeframe vary from building up cash savings and setting up the defensive planning to beginning short term investments in the stock market. Assuming that no financial planning had been done before the start of the plan, it is also safe to assume there has been little to no savings currently in any accounts. It is also safe to assume that the goal of this timeframe would be for the consumer to make a large purchase, such as a new car or a down payment on an apartment. It is important to understand that any substantial purchase in such a short period of time will require the most liquid, yet not necessarily the most efficient, tool to be used; cash savings. In the short time before making one of these large acquisitions, it is important to build up cash savings for a number of reasons; it is easily accessible, it is not taxed when taken out, and if the money to make the purchase is in a market investment, there is a high chance that the consumer will incur an *actual* loss and have less money to spend. Another component one should consider in the short-term timeframe is investing in mutual funds, more specifically Class C shares. When initially purchasing Class C shares, there is no purchasing fee and little to no selling fee, which makes it as close to a free investment as possible. However, there is a high, year-to-year maintenance fee, which is the reason why the consumer must sell it sooner rather than later. Class C shares are a short-term investment, and are the final components of the investment portion of the short-term time frame.

The goals in the mid-term, from years six up to fifteen, are more drastic and life-changing than the goals in the short-term. Rather than a down payment on an apartment, the consumer is more likely to make a down payment on a house, then must prepare for the mortgage payments which will not stop coming for thirty-or-so years. If the consumer is in a relationship at the beginning of the financial plan, perhaps his goals are now relationship oriented; buying a ring and preparing for a wedding. Weddings in America have an average cost of around $25,000, meaning it is necessary to begin saving for it, and the many other goals, as soon as possible. In this timeframe, which is over a decade away, the efficiency part of the investment becomes more important than the liquidity. The first component which may be used for these goals is cash value life insurance. There is a reason why whole life insurance is not in the short-term time frame, and instead it is only in the mid-term and more prominently long-term timeframe. The consumer must fund the policy in order to receive its benefits; death benefit and cash value. The cash value portion is the investment portion. However, due to its nature, the cash value vests after a period of twelve to thirteen years. Vesting, in this sense, means that the amount of cash value, or money one can withdraw from the policy, finally exceeds the amount of money one put into it. It is at this time considered an investment, and the cash value will exponentially increase as time goes on. It is extremely important to know that cash value life insurance is not a short-term investment; if it is treated as such then money is guaranteed to be lost.

A major factor as to whether or not to withdraw money from the cash value depends on tax rates and the market. Since cash value is not linked to the market, and its withdrawals are tax-free, the consumer should take money from this component if the market is on the fall, and tax rates are on the rise. The final component which will help reach the financial goals of the mid-term timeframe are investments in the stock market, primarily through Class A and B shares. Class B shares require no purchasing fee, or “front-end load fee”, but have a selling fee, or “back-end load fee,” which makes it ideal for mid-term investing. This investment requires no fee to start, and upon selling the shares, the consumer is simply taking a small percentage out of his investment which more likely than not was more than he started with. If, by chance, there is a loss in the investment after the back-end load fee is taken out of it, then the consumer should take money out of another component in order for the Class B shares to fully mature. When enough time passes with the Class B shares, they eventually convert to Class A shares, which are also ideal investments for the end of the mid-term timeframe. Although starting with a proportionately large start-up fee, the Class A shares continue to grow for minimal maintenance fees. If necessary, it is preferred that Class B shares are cashed in before Class A shares in order to fulfill the mid-term goals; as time passes, the Class A shares become far more valuable than Class B ever could. A major factor as to whether the consumer should cash these shares in or not also depends on market performance and tax rates at that time. The profits of these shares are taxed, and they are directly linked to the market; if taxes are low and the market is doing well, the consumer should cash out the shares for a profit and use the money to fulfill his goals. In case of desperation or emergency; however, cash value, Class A, and Class B shares are the components which help the consumer ease into a new stage of life by helping to achieve his mid-term financial goals.

The final stages of life, from around twenty years into the financial plan until retirement, may be the most rewarding period of time in terms of investments. The long-term goals vary from buying a second home, to paying for children's education, to saving for retirement, and last of all preparing one's legacy to pass on to the next generation. In this timeframe, liquidity has no influence on present decisions, and efficiency is at its greatest power. Compound interest throughout the decades has made life-changing additions to investments and overall capital. Two components overlay from the mid-term timeframe; cash value life insurance and Class A shares. At this point in time, assuming the cash value has not been touched and each dividend had been reinvested back into the policy, it is now a viable source of capital in order to achieve a wide variety of financial goals. It is important to note that at this time, the cash value has one of the highest rates of return of all the components. It will never fully mature so as long as it is untouched, it will continue to grow exponentially. The other component which was also in the mid-term timeframe is Class A shares. With no back-end load fee requirement, and the lowest maintenance fees of all three classes, Class A shares will also continue to grow and will be a significant factor in ensuring a stress-free long-term timeframe and retirement, at least from a financial standpoint. As discussed before, whether to withdraw money from the cash value or the Class A shares depend on market performance and tax rates. However, this is only prevalent is the consumer is under the age of 59½. As soon as he reaches this age, he is not entitled to his retirement plan; whether it be 401(k), IRA, or both. Retirement plans, similarly to Class A shares, are taxed when withdrawals are made. However, the taxation of the withdrawals depends on which type of retirement plan he chose; if Roth, there is no taxation, but it he chose traditional, then he is taxed at the current tax-rate.

Regardless of the short, mid, and long-term goals that this financial plan was designed for, the main goals that were achieved; making a more predictable and stable financial future, and having a stress-tested plan for any scenario, provided the consumer with a future that is as worry-free financially as possible. Throughout each timeframe, each component of the comprehensive financial plan was in its specific place on the timeline for a reason; to take advantage of it when others were currently flawed. Although there are countless investments and goals, a plan as simple as this one can be the deciding factor between a lifetime of work, and a relaxing, worry-free retirement.

Conclusion

There is a financial crisis in America, both on an economic scale as well as with individual Americans. It is understandable that many Americans feel uncomfortable discussing their financial situations; especially when they are struggling or crippled from debt. The truth is that they are not alone, and that there are more Americans in the same situation that there are not. For those who think it is too late and want to throw in the towel to debt or other financial struggles; it is never too late to plan finances out and decide what the next move is. Regardless of the situation, there is always something to be done. Those who are struggling can coordinate which debt to pay off first, while those who are prepared with a financial plan can make improvements to that plan. No plan is perfect, but American consumers must start from somewhere; even if they start with nothing.

A comprehensive financial plan is not effective unless there is both defensive and offensive planning, as well as financial tools and techniques which encompass every timeframe relating to the set goals. As long as there are complimentary financial tools and vessels in each timeframe, there is a miniscule chance that the financial plan will fail at what it was designed to do; help achieve financial goals, ease consumers into new major periods in their lives, and make the financial future of the consumer more predictable.

A concept which was mentioned but wasn’t touched upon was the use of professional help. That was not included, and only hinted at, because it is the ultimate decision of the consumer whether or not he chooses to consult a financial planner. Professional advice can be the difference between retiring at 70 and retiring at 60. These advisors plan finances for a living, and understand rules-of-thumb which can be defining techniques to make one's financial plan the most effective and efficient that it can be. In the end, financial planners merely bring up options and suggestions, and explain in a straight forward manner why he thinks that decision should be made. Ultimately, the consumer has all the power to do what he chooses with his money, regardless of what anyone suggests he do with it.

There are many ways in which a comprehensive financial plan can benefit an average consumer; given he applies the proper techniques, advice, resources, and tools that encompass it. It is very important for the consumer to understand that no financial tool is perfect, and that if he understands which ones have advantages and disadvantages, and plans accordingly, he will gain financial security both now and in the future. It is not a simple process, and it will not diminish every financial struggle overnight, but with proper planning and discipline, the average consumer can live out his life with one less stress on his mind.

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