Developing a Financial Plan: Frequently Asked Questions

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How do I determine my long-term financial goals?

The first step is to decide what you realistically want to achieve financially. Financial goals might include early retirement, travel, a vacation home, securing your family's financial comfort on the death of a bread-winner, planning for the care of elderly relatives or building a family business.

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Is there any validity to financial planning "rules of thumb" such as "saving 10 percent of your gross income"?

The following **rules of thumb** may work for some people, but they do not make financial sense for everyone. What is more important is to be able to know whether a particular rule of thumb suits your situation. Here are six of the more common rules along with some considerations that should not be overlooked.

1. Life insurance should equal five times your yearly salary
This rule of thumb has been used to answer the question: How much life insurance should I have? The ideal amount of life insurance is the amount that will, when invested, generate enough income to allow your survivors to maintain the level of income they are used to. "Five times your salary" will accomplish this objective in some cases, but there is no substitute for making the calculations necessary to find out how much life insurance you need to buy for your particular situation. The amount of life insurance you need depends on how many people there are in your family, whether there are other sources of income besides your salary, how old your children are, and a few other factors.

2. Save 10 percent of your salary per year
You may need to save much more than ten percent of your gross income to have a comfortable retirement. The amount you need to save for retirement depends on how large your existing nest egg is and how old you are. Those who started saving late in life, for instance in their 40s, need to save at least 15 or 20 percent per year.

3. Contribute as much as you can to retirement plans

This makes sense for most people, but if you've accumulated a large amount of money in a retirement plan, say close to a million dollars, you may reach the point where the negatives of contributing to your retirement plan savings outweigh the positives.

4. You need 80 percent of your pre-retirement income to retire comfortably

Although people may need 80 percent of their salaries during the first few years of retirement, later on they are often able to live comfortably on less. The amount of income you need depends on whether you have paid off your mortgage, whether you will have other sources of retirement income, and other factors.

5. Subtract your age from 100 and invest that percentage in stocks

This is one of those "cookie cutter" rules that only pans out for certain investors. For others, it results in a portfolio that is much too conservative. The best method of allocating percentages among various types of investments depends on your investment goals and needs and your willingness to risk your capital. In this case, rules of thumb do not serve the investor very well at all.

6. Maintain an emergency fund of six months' worth of expenses

Depending on your family's situation, three months' worth of expenses might be enough. On the other hand, for some families even six months' worth might be totally inadequate. The amount you should keep on hand depends on how easy it would be for you to take out a short term loan and how much money you have in savings and investments among other things.

Tip: Do not rely on any rule of thumb to make financial decisions. Instead consider carefully what your needs and goals are, and then calculate what you'll need to do to fulfill them.

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What do women in particular need to keep in mind with regard to financial planning?

With more women remaining single, nearly half of all marriages ending in divorce, and the odds of becoming a widow by the age of 55 hovering around 75 percent, nearly 9 out of 10 women will be solely responsible for their financial well-being at some point in their lives. But many are ill-prepared to do so.

Here are several areas where women fall behind when it comes to planning for their financial future:

- Women save considerably less for retirement, on average 60 percent less than men according to a 2010 study conducted by LIMRA of close to 2,500 employees. This is significant because women typically live longer than their male counterparts and need more retirement savings.
- In that same LIMRA study, 29 percent of men and only 14 percent of women consider themselves knowledgeable about financial services and products. Fifty-four percent of women felt at least somewhat knowledgeable about financial products and services, but nearly three-quarters of men felt the same way.

- And, in 2011 a Harris Interactive survey commissioned by RocketLawyer.com found that of the more than 1,000 people surveyed, 5 percent of the women do not have a will, 26 percent of them citing cost as the primary reason they don't have one.

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What special problems do unmarried couples have to be concerned with in financial and estate planning?

In 2010, there were 7.5 million unmarried couples living together in the US, according to the US Census Bureau. This represents an increase of 13 percent over the previous year. And because unmarried couples don't enjoy the same legal rights and protection as married couples do, financial planning considerations for issues such as retirement planning, estate planning, and taxes can be quite different. For example:

- Unmarried partners do not automatically inherit each other's property. When an unmarried partner dies intestate (without a will) the estate is divided according to laws of the state, with property and assets typically going to parents or siblings and rarely or never to the beloved partner. In other words, married couples who do not have a will have state intestacy laws to back them up, but unmarried couples need to have a will in place in order to make sure that their wishes are met.
- Couples who aren't married also do not have the right to speak for each other in the event of a medical crisis. If your life partner loses consciousness or becomes incapacitated, someone has to make a decision whether to go ahead with a medical procedure. That person should be you, but unless you have a health care directive such as a living will in place, you have no legal right to make decisions for your partner.
- Tax and estate issues are also more complicated. In most cases it makes more sense not to own property such as a car or electronics equipment together or to have a joint loan. Whereas marital assets can be divided equally by a judge, there is no legal recourse for unmarried couples in the event of a breakup. Another example is home ownership. If one partner is listed as the sole owner of a home that the couple lives in together and he or she dies, the surviving partner might be left homeless. This can be resolved by properly titling assets, in this case making sure the home is in joint tenancy with rights of survivorship.

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