

Best Practices – Goal-Based Budgeting

One of the key financial planning services you can provide is in the area of budgeting. Rather than presenting the concept of budgeting in the negative light in which it commonly appears, as a process that limits enjoyment and spending, you can successfully present budgeting as a means of achieving goals and peace of mind. Helping your clients monitor their budgeting and achieve their financial goals can be presented as part of your ongoing services.

Step 1: Start with the Goals Conversation – see Best Practices sheet on Setting Goals

Step 2: Create a Cash Flow Summary from Last Year's Activity

While we don't like to dwell on the past when budgeting to meet goals, you need a starting point, and the previous year's activity will give you guidance on the client's cash flow experience. Note that the budget going forward will not be a copy of last year's income and spending but instead a blueprint for achieving future financial goals.

Your goals in this process include:

- Helping the clients understand their current income and spending habits
- Providing insight into clients' capability to handle debt
- Determining savings opportunities for the clients
- Teaching clients that budgeting is a life-long process that evolves as they do

Note: When reporting income in budget, show amounts as gross income, and then show withholdings as expenses. This helps the client understand all aspects of income and spending, including those hidden amounts that occur when items are withheld from salaries and wages.

Step 3: Work with Client to Create a Future-Facing Budget

The budget process needs to have buy-in from the client. Setting income and expense expectations without client acceptance will position the budget process for failure. Go through the budget line-by-line and discuss opportunities for change and improvement with a focus on increasing income to achieve goals, if this is necessary. Keep in mind that it's quite possible the client is already on track for being able to fund financial goals and may only need advice on the best ways to save and invest that money.

- Opportunities for increasing income include:
 - Increased wages through raise, promotion, new job, overtime, second job
 - Improving skills to qualify for better-paying positions
 - Increased savings by taking advantage of 401(k) match
 - Higher earnings rates on income already in savings
 - Paying off debt
 - Reducing unused recurring membership/subscription charges
 - Selling unneeded items
- Discussion about reducing expenses without changing lifestyle can include:

- Opportunities to consolidate debts
- Lowering transportation costs by carpooling, working remotely, more efficient vehicle
- Refinancing debt
- Utilizing in-home energy efficiencies
- Reassessing insurance needs and looking for bundling opportunities
- Reducing income taxes with tax planning techniques

Step 4: Introduce Clients to Technology

Using personal finance technology tools can prove inspirational for keeping clients engaged with their budget. The more they see the results of earning, saving, and efficient spending, the closer they feel to the process. Many personal finance programs provide goal-setting incentives as well. You will want to familiarize yourself with a program before recommending it.

Step 5: Monitoring and Updating the Budget

For a budget to work, it must adapt to the needs, goals, and lifestyle of the user. As a financial planner, you have the opportunity to help your client improve the budget annually by reassessing goals, analyzing past performance, and offering insights to improving budget usage. Annual budget meetings should include:

- Discussion about budget usage and performance over the past year
- Measuring progress toward goals
- Reassessment of client goals
- Adjusting budget for the coming year
- Determining budget goals for the year ahead

By keeping the budget fluid and demonstrating to the clients how the budget process is helping them get closer to future financial goals, this annual budget meeting update becomes an excellent opportunity to provide value to your clients.