Plan to Win: Avoid the Five Most Common Planning Pitfalls

Steve Harvey

Financial planning is important. Because planning can be time consuming and force families to deal with difficult questions that are more easily ignored or delayed, it often slides down the list of priorities.

But planning is worth the effort. Individual and family finances have many moving pieces — income, real estate, credit, business interests, education funding, lifestyle aspirations, retirement plans, philanthropy and taxes, just to name a few. It's a lot to ask for all these moving pieces to magically fall into synchronized motion like the inner workings of a watch. Trying to operate without the benefit of planning is like trying to steer a boat without a rudder and invites poor and possibly disastrous results.

Those who do create plans face potential challenges and pitfalls, too. Here are the top five scenarios to avoid:

1. Creating multiple, unconnected plans

In many households, financial planning occurs on a squeaky-wheel basis, where a specific financial need or goal nags for and eventually receives the attention it demands. This ad hoc approach typically results in a mismatched array of plans, each assembled independently by a different specialist. While each plan may meet the immediate need, over time the pieces may fail to mesh. For example, investment accounts and insurance policies often create redundancy in goals and unnecessary duplication of costs.

Looking at all planning elements together, rather than independently, is both more efficient and more effective. A well-thought-out financial plan can provide a foundation for making important financial decisions. Life events such as marriages, births, inheritance and new business opportunities, among many others, provide ideal opportunities to not only consider new wealth planning needs but also provide an opportunity to re-examine and modify your existing plan.

2. Starting late

The oldest rule in the book is to start planning and saving as early as possible. Starting at age 35 is better than 45 or 55, and 25 is even better. The magic of compounding rewards those who start saving and investing early.

The math is compelling. A 25-year-old individual investing $10,018 annually and earning a 7 percent annualized return will accumulate $2 million by age 65. To reach the same $2 million level

at 65, an investor who doesn't start until age 45 would need to put away more than $48,000 each year.

Happily, for those who start early, the planning process can be a relatively simplistic regimen of regularly funding retirement accounts, with additional elements and strategies added as one's goals, family and income grow.

3. Building — and forgetting — a giant, obsolete binder

Assembling a comprehensive, cohesive financial plan is a big job. Designing a plan that addresses savings, spending, investment, taxes, insurance, education, estate planning and philanthropy requires serious discussions, careful thought and tough choices.

Frankly, financial planning wears out a lot of people. This may explain why so many thoughtful plans end up largely unimplemented — impressively fat binders collecting dust on a shelf. A plan without action is all pain and no gain. Also, a financial plan is not a one-size-fits-all, one-time endeavor. There is one constant in life, change. Everyone's life looks different today than it did five years ago. Everyone's life will look just as different five years from now. A financial plan is not like a one-time set of blueprints for building a home that must be followed exactly as detailed. A well-designed financial plan is a living, breathing roadmap that can and should be modified as life circumstances change.

4. Relying on false assumptions

Every plan requires assumptions about the future. Trying to "make the numbers work" by using faulty assumptions can lead to serious problems down the road.

For instance, many investors overestimate the returns they can expect to achieve. This can lead to major shortfalls. In the example above, a 25-year-old investor seeking to reach $2 million by age 65 and expecting a 12 percent annualized return would put away just $2,607 per year. If the actual return is not 12 percent, but instead 7 percent, the nest egg would grow to only $520,000.

Other suspects for garbage-in/garbage-out include assuming that markets will repeat recent performance year after year; not factoring in taxes or inflation; placing too much faith in future Social Security benefits; not including the impact of market volatility on returns; and trusting rules of thumb, for instance, that a couple can retire on just 60 percent of their annual working income without lowering their standard of living.

Assumptions must be made in any wealth planning activity, but erring on the conservative side is preferable to creating a rosy, but unattainable, forecast.

5. Putting other goals ahead of retirement

Retirement can seem so far off in the future that it takes a backseat as other more immediate financial issues are handled. Funds may be allocated to a home renovation, private elementary school, a vacation home or other worthy causes, while little or no money goes into retirement

accounts. With individuals living longer than ever, the consequences of delaying retirement savings can be devastating. Having a plan in place can provide a framework for making decisions around the use of available funds. Discretionary spending should be part of the plan.

Like it or not, retirement is expensive, and every dollar spent today reduces what's available later. Consistent retirement savings should be part of every financial planning decision. Many families find it useful to think of investing for retirement as a mortgage or other monthly expense. It is simply an expense that gets paid every month like every other bill.

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Steve assists clients in developing long-term investment strategies and creating investment portfolios designed to achieve their financial goals and objectives. In the community, Steve is involved with the Lake Travis Education Foundation, and he is the chair for the Center for Child Protection NFL Alumni Classic Golf Tournament.

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