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The Future American Nightmare

By Thomas Houck, CPA, CFP®

We've all been programmed to pursue the American Dream - a nice house, fast cars, and lavish vacations. Unfortunately, there's a short circuit in the current generation's thinking. Many are living the new American Dream: Live the dream now, and figure out how to pay for it later. Unfortunately, this only creates a future American Nightmare. The truth is simple - in order to attain the American Dream, you need good money habits; work, save, and then spend. The current generation, however, has developed some bad habits: spend, work, and then maybe - someday - save.

Brian, a small business owner, was in a financial crisis that was causing him stressful days and sleepless nights.

"It seems like the business is doing okay," he thought. "My numbers are up from last year, and my expenses are about the same; but I can hardly pay my bills. The bank won't lend me money because my credit cards are almost maxed out. My accountant is always on my case about funding my retirement plan, but how the heck am I supposed to do that if I can't even make the mortgage payment? What's going on?"

Brian decided to hire a consultant to look at his business to see what was broken and how he could fix it. To the entrepreneur's surprise, the consultant discovered that the business was outperforming many similar competitors in his industry. But his bottom line discovery was news to Brian: The problem was not the business; it was Brian's bad money habits. The consultant suggested that Brian and his wife, Jen, sit down with him, take a good, hard look at their financial situation, and commit to developing good financial habits.

This meeting was tough for the couple.They quickly realized how out of control they'd become over the years, and how challenging it was going to be to right their ship. To help them make this change, the consultant suggested that they mutually agree on some hard and fast rules regarding their finances…and abide by them.

Rule One: Don't spend more than you make

Although this sounds simplistic, there are millions of Americans who can't pull this off. Some guidelines are:

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· Determine how much you make after taxes; i.e., your "take-home pay." This would be the amount that you can comfortably "draw" from your business each month, while setting aside cash to take care of taxes. This number shouldn't drain the business to the point of causing a cash flow crunch.

· Choose a monthly figure for your "necessary spending," which includes rent or mortgage payment, food, utilities, insurance, and clothing. It does not include a BMW, a three-week vacation in Maui, dining out five nights a week, or a new Jacuzzi.

· Divide your necessary spending by your take-home pay. If the number is higher than 75 percent, you have work to do. The immediate, short-term action is to cut down on your spending. The long-term goal is to increase business cash flows so that you can increase your draw.

Rule Two: If you can't afford it, don't buy it.

This rule may sound obvious, but an entire generation of Americans doesn't "get" it. There's a huge difference between a "want" and a "need." If you make your living by fishing, you need a boat. If you see a cool catamaran at a boat show and decide to buy it, even though you've never sailed before and are up to your eyeballs in debt, that's a "want." If you really must have a boat, save up for a few years, and buy it without any financing.

Rule Three: Don't use ANY debt, especially high-interest options.

This one isn't complex, either. When you borrow something from someone, they expect you to pay it back. As a matter of fact, they take it pretty darn seriously. And credit card companies are the most serious of them all, which is why using plastic is an expensive way to buy anything. These companies charge you an outrageous interest rate, tempt you to buy more by offering points and perks, and then ruin your credit rating if you fall behind. If you really want something, determine the cost, and buy it only when you have the money in hand.

Rule Four: If you don't save for retirement, you won't be able to retire.

Many people are missing this one. If you spend more than you make, and rack up high interest debt during your working years, what's going to happen when you want to stop working? You won't be able to, because you won't have any money; or worse yet, you'll have more debt than assets. The smartest thing that an entrepreneur can do is to talk to a CPA and financial advisor, and pick a suitable retirement plan.

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Then, fund the plan until it hurts. If you do this for 20 years and then sell your business, you should be able to retire comfortably.

Rule Five: Make the best investments

The education of your children is by far the best investment you can make. Today, almost every state has some type of prepaid college plan. The younger the children are when you start funding the plan, the easier the payments will be. Visit www.collegesavings.org to find options in your state.

So what about Brian and Jen?

They had several disagreements, but made some tough decisions during the first six months after their meeting by playing by the rules. Brian sold his treasured boat, and they cancelled a Hawaiian vacation. Going out to eat became a delicious and rare treat. On the flip side, they've paid off most of their credit cards, and are funding 529 plans for the kids' educations, and retirement accounts for themselves. Brian's business has started to take off, because he can now sleep at night and isn't stressed over money all the time.

They both agree that abiding by these five simple financial rules is going to let them make their own **American Dream** a reality.

About the Author:

Thomas E. Houck, CPA, CFP®, is a speaker, author and consultant whose program, "Your CFO Advantage™" helps business owners grow their businesses, reduce their taxes and lower their stress level. His book, "The Top 10 Mistakes Business Owners Make (and how to fix them) ™" helps business owners develop strategies to lead a better life by running a better business. For more information you can visit Tom's website at www.heritagebusinesssolutions.com