12 STUPID MISTAKES PEOPLE MAKE WITH THEIR MONEY

And Smart Ways to Avoid Them

A Step-by-Step Guide to a Secure Financial Future

DAN BENSON

Author of The New Retirement

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by

Dan Benson

THOMAS NELSON
Since 1798

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INTRODUCTION

Are You Making a Stupid Money Mistake?

If you find yourself in a hole, the first thing to do is stop digging.

—WILL ROGERS

Wow, do I need that book!"

How soon will it be ready? I want copies for my kids—and for their kids!"

Quite often, after a speaking engagement or media interview related to my earlier books on personal finance, people ask me about my next project. During the past year, I've been telling them about *12 Stupid Mistakes People Make with Their Money*, and the response has been electric:

"I could be your cover model for stupid money mistakes!" one interviewer offered.

"Did I ever need that book when I graduated from college!" an audience member reflected.

You work hard to provide life's necessities . . . to pay monthly bills and supply needs and wants . . . to handle unexpected financial emergencies . . . to provide for your children's college and wedding expenses . . . and to save and invest for a meaningful retirement. You want financial freedom—who doesn't? But succeeding with your money is one of life's biggest challenges because there are so many ways to "blow it," so many pitfalls along the path to financial freedom.

You've undoubtedly stumbled into a few of those traps yourself. As a former financial planner, I've seen the damage caused by twelve all-too-typical mistakes people make with their money. Stupid mistakes, really. Little boo-boos that can postpone goals. Big blunders that can devastate dreams. Common missteps that otherwise intelligent, well-meaning individuals and couples easily, frequently make with their money. It's not that these good people are stupid; they've simply made some stupid money decisions. And there's a big difference. The folks I quoted earlier were indeed wise to recognize that they'd slipped up and needed some guidance. It happened to be my privilege to show them how to pull themselves from the trap, dust themselves off, and start anew on the road to financial freedom—smarter, wiser, more hopeful about their financial futures, and a bit shrewder about the inevitable traps waiting for them down the road.

How to Attain Good Judgment

I would be dishonest if I were to pretend that I have not made any of these Stupid Mistakes myself. I have. I'm reminded of the ambitious young man who interviewed the successful senior citizen:

"Tell me, sir, how did you attain all your good judgment?"

"From experience."

"And where did you attain your experience?"

"From bad judgment."

Indeed, if experience and bad judgment are good teachers, then I should be wise beyond my years. Much of what I now do right I first did wrong, and there isn't an honest financial adviser in the world who would tell you differently. So if you count yourself among the hapless souls who feel they can be poster children for the 12 Stupid Money Mistakes, please do not feel ashamed or that all hope is lost.

In fact, I'm very encouraged at your realization that perhaps you've made a mistake or two along the way . . . and that you may be susceptible to mistakes in the future. I'm encouraged that you want to learn smart ways to avoid the Stupid Mistakes, smart ways to manage and invest your money more productively, smart ways to indeed get your ducks in a row so you can:

- handle future emergencies such as unexpected job layoffs, car or home repairs, and medical expenses;
- provide for your children's college education, wedding expenses, and other important family goals; and
- enjoy a financially secure retirement in which you can live out your dreams.

The Journey to Financial Freedom

I'm here to tell you that you, too, can extricate yourself from the money traps of your past, dust yourself off, and begin again your journey to financial freedom with a level of wisdom and confidence greater than ever before.

That's why I take delight in preparing this book for you, for your present or future spouse, and for your present or future children. In the following pages you're going to discover twelve of the most common mistakes good people make with their money . . . the havoc or lost opportunity each Stupid Mistake can wreak in your financial life . . . smart ways to avoid those traps in the future . . . and, most important, the amazing benefits to your finances—and indeed, your life—as you steer clear of the 12 Stupid Mistakes and build a solid financial future.

For example . . .

- When you learn to avoid Stupid Mistake #2, you will no longer be caught like a deer in headlights whenever a financial emergency crests the hill. Your next out-of-the-blue car repair or medical copayment will be far more manageable. Even a job layoff will be less stressful. (Notice I didn't say *fun*. Just less stressful—for you and your pocketbook.)

- Steer clear of Stupid Mistake #4, and you'll *save hundreds of dollars—more likely thousands—this year alone*. It can mean saving *tens of thousands* over a lifetime, dollars you can put to work building financial independence.

- If you break free of Stupid Mistake #5, you'll regain control of hundreds of dollars each month—"found money" that will help you free up your cash flow and save for future needs and dreams. Investing this money instead of washing it down the drain could make you *$150,000 richer* twenty years from now.

By now I hope you're beginning to see that this book is not simply a lament over the costly mistakes people make with their money. Will Rogers's homespun wisdom is just as appropriate today as it was in his time: "If you find yourself in a hole, the first thing to do is stop digging." If you find yourself in the hole with one or more of these mistakes, my goal is to help you stop digging and turn your financial life around. And if you're fortunate enough to have steered clear of the holes to this point, I want to prepare you with the knowledge and insight to avoid those costly traps in the future.

- You may not think Stupid Mistake #6 is a financial issue—until you begin paying its high cost. This trap will not only cost you thousands of dollars, it will also deteriorate *your job capability* and *your overall quality of life*. We'll pinpoint ten key strategies for steering clear of this common pitfall.

- Stupid Mistake #7 could mean the difference between *striving* or *thriving* financially in your retirement years. Keep digging this hole, and you may as well plan on moving in with your kids. But heed the guidance in this crucial chapter, and you can build the financial freedom to *enjoy the retirement of your dreams*.

- I call Stupid Mistake #8 "extreme investing" for good reason: *Many of us invest either too fearfully or too aggressively*. Fear can cause us to keep our money in ultraconservative investments that barely keep up with inflation; fear can also cause us to "invest with the lemmings" and buy and sell our investments at precisely the wrong time. On the other hand, if we invest too aggressively, we seek high returns at too high a risk. (Everyone who was heavily invested in technology stocks or technology mutual funds in early 2000 knows too well the heart-stopping losses that can result from this form of extreme investing.) In this chapter I'll show you how to design *an investment plan that avoids the extremes and enhances your opportunity for steady growth*.

- Allow Stupid Mistake #10 into your life, and it may not let you go. Unfortunately, this one has become more and more prevalent over the past decade; it is not only a drain on your own financial resources, but it is also a terrible disservice to your children. Its negative impact can affect multiple generations. The good news is that *you can totally avoid this mistake*—if you have the courage to do so.

These are just a few samples of the discoveries that await you as we visit together in the coming pages. So find a pen or highlighter (go ahead; I'll wait), then turn the page and see if you recognize someone you know in *12 Stupid Mistakes People Make with Their Money*.

Yours for financial freedom,

DAN BENSON

STUPID MISTAKE #1

Counting on the Illusive "Someday"

The best time to plant an oak tree is twenty years ago. The next-best time is now.

—David Chilton, *The Wealthy Barber*

Someday I'm going to get out of debt."

"When I get my next raise, then . . ."

"Maybe after Christmas I can start saving."

"Someday, when our ship comes in . . ."

If you've caught yourself entertaining such thoughts recently, welcome to the club. Ours is a culture of financial discontent. Like everyone else, you probably make enough to "get by" each month, maybe even make payments on an extra vehicle or two or tuck away a few dollars in the company retirement plan. But you dream of a better, brighter financial future. A time when cash flow isn't so tight, when you have savings and investments to cover needs and dreams. A time when you can say good-bye to fifty-hour work weeks and "graduate" to a retirement in which you're financially free to live the adventures you've always wanted to live. And as you envision these things, you sense a nervous, nagging feeling, deep inside, that there is much more you should be doing if you're ever going to move beyond "getting by" and enjoy a life of financial freedom.

You want to, but you don't know how. You're aware of some crucial steps you need to take, but with your present-day obligations you don't see how you can possibly do so.

So you lapse into the illusive "Someday."

Maybe your consumer debts are piled high: Despite good intentions, you've put too many expenditures on credit cards and now the payments are draining your monthly cash flow. *How did those balances get so high so fast? Cash is tight, so I'll just make minimum payments for now. Someday . . .*

You may be among the millions whose savings accounts aren't where they need to be. Maybe you had to drain your savings to pay for an emergency and haven't been able to pay yourself back. Or perhaps you raided savings to handle another "emergency" such as a new sound system (got to have that MX-57 Master-Blaster Surround Sound with Quadruple Earthquake Woofers) or riding mower (everyone else on our street has one) or expensive vacation (we deserved it). You were going to rebuild that rainy-day account quickly, but real life and its related expenses overwhelmed your good intentions. Or maybe, like millions of others, you've just never been able to save successfully in the first place. *If only I made more money. When I get my next raise, maybe then . . .*

Your kids are growing fast; it won't be long until they're ready for college. Will you be? During the next decade a four-year public-university education is expected to cost $40,000—double that for a private college. By the year 2018, pundits are saying, four years at a public college or university could run $100,000 and a private college nearly $200,000. Intimidating, isn't it? *Can't do much right now . . . but someday our ship will come in. Maybe an inheritance from Mom and Dad . . .*

As quickly as the kids have grown older, so have you. We don't like to admit that or give in to it; that's why hair coloring, tooth whitening, plastic surgery, vitamin supplements, health clubs, home-fitness machinery, and Viagra do land-office business among today's aging baby boomers. Suddenly, we realize that our lives are most likely half over. That the time is rapidly approaching when either we or our employers will say "Time to hang 'em up," and the steady paycheck will be suddenly replaced by a card and a pen-and-pencil set. But how many of us will be financially ready? One recent study reported that 60 percent of baby boomers in their forties think they could personally face a retirement savings crisis. Will you? *Can't do much now. But once we get the kids through school, then we can save for retirement. Besides, there's Social Security, and probably an inheritance . . .*

Someday. It's human nature's way of acknowledging guilt without repenting and changing our ways. It's like saying "I'll stop procrastinating tomorrow." But like tomorrow, Someday never arrives. There's no date on the calendar called "Someday." It's just a hazy, shapeless, undefined concept in time—always out there somewhere in the nebulous future, as far away as we can mentally push it so that we won't have to think about it. "Someday thinking" enables us to continue our nonproductive or counterproductive courses by assuring ourselves of good intentions to do better . . . later.

Someday's High Cost

Why are we citing Someday thinking as one of the 12 Stupid Mistakes people make with their money? Because Someday thinking leads to procrastination, and *procrastination is easily the number-one, most common, most damaging blunder you can possibly make with your money*. If you put off until Someday what you could and should be doing today, you will pay a steep price indeed. Check out Jack and Jill:

- Jack, 50, who always knew that Someday he should begin saving for his retirement years, has finally realized that he'd better turn someday into today—and fast. He determines to set aside $300 each month in his company's 401(k) plan. Assuming Jack works sixteen more years to age 66, and that his investments within the 401(k) grow an average of 10 percent per year over those sixteen years, Jack will have $141,131 when he retires. Sounds like a big sum now, but how long will that amount last when Jack is no longer working? Three, maybe four years?

- Jill, 30, started her own 401(k) contributions this year, also contributing $300 per month. If Jill also works to age 66, averages the same 10 percent on her investments, and never contributes more than $300 per month, she will retire with $1,262,028 in her retirement fund. Same monthly contribution, same return on investment. The difference? Time. Jill didn't fall victim to Stupid Mistake #1, Counting on the Illusive "Someday." Instead, she made the commitment twenty years earlier than Jack to save the same amount. *The difference: $1,120,897.*

Someday and Your Credit Cards

Another area in which Someday thinking costs dearly is credit card debt. Today the average American family carries balances totaling more than $8000 on fourteen credit cards, and more offers for more credit cards arrive in the mail every week. Whenever you place an expense on a credit card, you procrastinate payment for the item or service you've purchased. It's one thing to know you have the cash set aside to pay in full when the bill arrives, but if you procrastinate payment beyond the grace period, then interest accrues on the unpaid balance. This is delightful to the credit card issuer, but a big, stupid mistake on the part of the credit cardholder. An $8000 credit card balance, at 16.9 percent annual interest, costs $1352 per year. At 19.9 percent, it's $1592. Now observe Brittany and Ted:

- Brittany has heeded the call of consumerism: "Buy now, pay forever." Some of her credit card purchases have already been consumed (vacation, dinners out, hair and nail salon, gasoline); others have depreciated in value (CD player, CDs, furniture, Home Shopping Network gotta-have-its). And instead of paying these purchases in full when her card statements arrived, she procrastinated payment. "Someday," she said. Just what the credit card issuers wanted to hear. They'll make nearly $1500 in interest *this year alone* from Brittany's procrastination. Meanwhile Brittany's debt service of $400 per month (of which nearly $125 is interest) wreaks havoc with her monthly cash flow.

- Ted, on the other hand, doesn't believe in Someday thinking. His income is similar to Brittany's, but he spends according to plan from his cash allotment or checking account, saves in advance for larger purchases, and if he should use his one and only credit card, he pays off the balance in full as soon as the statement arrives. Credit card issuers don't like Ted as much as they like Brittany, although that doesn't stop them from trying. But Ted shreds every credit card sales pitch upon arrival; his one no-fee card is all he'll ever need, thank you. Since he carries no consumer debt, Ted can take the same amount Brittany spends in debt service and invest it each month in a mutual fund. If that fund averages just 8 percent over the next three years, Ted will have added $16,214 to his nest egg. Meanwhile, Brittany will be continuing to flush away hundreds each month, thousands each year, still and forever paying for those consumed and depreciated purchases.

You May Be Making Stupid Mistake #1 If . . .

- you find yourself counting on a raise to break even
- you're putting off saving or paying off debts until a "better day"
- you hope Mom and Dad leave you a nice inheritance
- you catch yourself thinking, *If only I made more money*
- you play Lotto or otherwise long for your ship to come in

"If Only I Made More Money . . ."

Jeff and MaryAnn were Someday thinkers. In their midthirties, they had one elementary-age child and earned an above-average income. They had suffered no devastating setbacks. Yet financially they were barely keeping their heads above water. When they came to see me and pulled out a list of their monthly expenses, I could see frustration in their eyes.

"We work so hard, it seems we should have more to show for it," Jeff said. "But our monthly expenses wipe out about everything."

"We'd really like to be putting some aside for retirement and for Amanda's college education," MaryAnn joined in. "Really, we just need breathing room. But with all our monthly expenses and then insurance and Christmas and birthdays, there just isn't enough. If only we made more money . . ."

If only. Jeff and MaryAnn were stuck on a paycheck-to-paycheck treadmill. It didn't take an accounting degree to quickly see that they had chosen a high-expense, credit-driven lifestyle that demanded inordinate proportions of each month's available cash. But because they had identified their problem as insufficient income, the only solution they could see was to *make more money*. Such longing is a common manifestation of Someday thinking: We can't imagine restructuring our financial priorities, and we don't want to face the "pain" of disciplined spending and saving, so let's hope that someday we'll make more money.

I told Jeff and MaryAnn about Parkinson's Second Law.

In 1960 a book titled *The Law and the Profits* swept management circles around the world. Its author was C. Northcote Parkinson, who is still widely quoted today because of a shrewd observation that would become famous as Parkinson's Law: *Work expands to fill the time available*.

This principle underscores a universal truth that workers had always suspected but were embarrassed to verbalize: that no matter how much time you're able to save in the workplace, your workload will always increase to fill the time you thought you had saved. What many people don't remember is that within the same book, Parkinson made a second statement that in my view is even more timely and prophetic than the first: *Expenditures rise to meet income*.

Think about that for a moment. Have you ever promised yourself, "After my next raise, I'm going to pay off my bills and start saving more . . ." only to see your personal expenses rise to consume the amount of the raise? You're not abnormal or alone; this happens every day. Parkinson knew human nature well. He went on to say, *Individual expenditure not only rises to meet income but tends to surpass it, and probably always will*. In other words, by the time any extra income happens along, we already have a list of plans for it.

Jeff and MaryAnn's problem was not their income level. Their true problem was they had literally "bought in" to America's get-it-now, do-it-now syndrome, which drove them to spend everything they made, and then some, in conformance to Parkinson's Second Law. Without a major turnabout in their financial priorities and practices, "more money" would only continue to be consumed by higher expenditures. Therefore, Jeff and MaryAnn's Someday thinking regarding "more money" was not the answer to their dilemma but simply a smokescreen to mask their need for an intervention in their financial decision making.

I assured Jeff and MaryAnn that they were neither abnormal nor alone. Indeed, theirs is the financial road most traveled in our world— the path of too-easy credit, of instant gratification with the newest and best, of putting off what should be done while longing and hoping for a mythical ship to come in. I also assured them that this path of least resistance can be a slippery slope of financial despair. With my encouragement, they resolved to back up and choose a surer path. Together, we turned bad habits into good habits, and before long Jeff and MaryAnn were well along the road to financial freedom. They learned that *it's not how much you make, but what you do with what you make* that makes all the difference.

"Someone Else Will Take Care of Me . . ."

Few people have the nerve to state this aloud, but, deep down, millions hold this Someday fantasy in the back of their minds. It comes from the old-school, outmoded mind-set that as we grow older we'll be financially cared for by our government, our former employers, or inheritances from our parents or a long-lost rich aunt. And if none of those come through, we can always move in with our adult children.

"Someday I'll Get Social Security . . ."

America's Social Security system was born in 1935 as a federal initiative to help bring the country out of the Great Depression. Its purpose was to provide an incentive for workers to leave the labor pool at age sixty-five, thus leaving their jobs open for the droves of younger adults who were urgently searching for work.

But in 1935 the average life expectancy was sixty-three, so our benevolent government figured that starting payouts at age sixty-five was a fairly safe commitment to make. Even those who made it to age sixty-five were likely, on average, to survive just four or five more years. The government's promise was doubly conservative because during the system's first ten years, more than forty workers contributed to the system for every one retiree drawing a stipend. The maximum annual contribution was $30.

Today life spans have increased to the point that a typical retiree may draw benefits for fifteen to thirty years instead of just four or five. Now there are only three workers supporting every retiree, and the Social Security board of trustees projects that by the year 2025 the ratio could be as low as two workers per beneficiary. Social Security taxes keep going up as payouts grow larger and Congress indexes benefits to inflation. In addition, benefits have been expanded to include health and disability insurance.

As a result, every few years a watchdog group proclaims that the Social Security system will go bankrupt within the next few decades, leaving today's younger baby boomers and Gen Xers in the lurch when they reach retirement age. One recent survey reported that more men and women under the age of thirty-four believe more readily in UFOs than in the availability of a Social Security stipend when they grow older.

I do not share the view that Social Security will go under, for the simple reason that congressmen and -women and presidents like to stay in office. The senior voting bloc, already powerful in Washington, will grow even stronger as 76 million baby boomers begin joining its ranks over the next several years. Politicians know a big voting bloc when they see one, so to court the senior vote they'll keep the system struggling along by continuing to increase the Social Security tax, pushing the qualification ages higher, and possibly instituting some form of privatization—all while screaming that the other party doesn't care about senior citizens.

But even though Social Security may indeed be there for you, what should you plan on? Not much. It's crucial to recognize that Social Security was never designed to be a "retirement plan" or the sole source of one's retirement income. It was established to serve only as a *supplement, a safety net*. Today it provides less than one-fourth of most retirees' monthly income needs. Here's why: If you were to qualify for the full Social Security pension today, you would receive approximately $12,000 per year per working person—half that for a spouse who hasn't accrued sufficient Social Security credits. Sure, $12,000 helps, but it won't provide the life you want to live after you stop full-time work. I usually suggest that today's midlifers plan on receiving approximately one-half that amount, or $6,000 per year. I hope I'm wrong and that the system thrives in the future, but I'd rather err on the side of caution. Many financial planners go so far as to counsel clients to work, save, and invest as though Social Security won't be there at all. You can't go wrong that way, and this book is geared to show you how to do just that. Then, if Social Security income happens to be there for you in the future, you can regard it as icing on the cake. The bottom line is that Social Security is in the hands of politicians, which means that it'd be another Stupid Mistake to rely heavily on the system for your retirement years.

"Someday I'll Get a Pension . . ."

In days of old, the typical corporate pension was the defined-benefit package, in which the company funded the plan for you, took responsibility for managing its investments, and, upon vesting, guaranteed you a specific monthly pension upon your retirement.

But in recent years this has shifted dramatically. The old pensions assumed mutual loyalty and long tenures between employers and employees—two qualities that, to our discredit, can no longer be counted on. Downsizings, buyouts, new technologies, and tough times have made corporations more likely to turn employees loose before the employees are fully vested in their pension plans. Likewise, unlike our parents' generation, it's rare for today's employee to stay with the same company for an entire career. Such mobility makes defined-benefit pensions cumbersome to administer and difficult to benefit from. Another factor in the decline of such pensions is that horror stories abound of pension funds disappearing into fiscal sinkholes—and former employees suing their companies for mismanagement or fraud. Fewer and fewer companies want to bear responsibility for the performance of a pension fund's underlying investments. Thus, defined-benefit pensions are becoming either obsolete or difficult to count on.

"Someday, When I Get My Inheritance . . ."

Our parents' generation built assets of $10.4 trillion, which will soon begin to be passed on to us, their adult children. But not all of our parents participated equally in the post–World-War-II boom, and neither will we share equally in the future transfer of wealth. There may be an inheritance in your future or maybe not. However, it's unwise to count on an inheritance because there are simply too many unknowns. You may not know your parents' fiscal situation and may find it awkward to ask; even if you ask, they may not want to tell; and no one can predict how long they'll live, what their future expenses will be, or how much of their asset bases will remain once they are gone.

And there's a deeper, more visceral reason why I discourage anyone from relying on an inheritance. I hold a strong conviction that an inheritance is not an obligation, but a *gift*. It's our parents' hard-earned money, not ours. They've already given us far more than we can ever repay. As they grow older, they deserve to enjoy financial freedom and live out their dreams with absolutely no pressure, spoken or implied, to leave some for us.

In my opinion, it's sad commentary that many of today's middle-*age* adults seem to regard an inheritance as an entitlement. I'm disgusted whenever I hear presumptuous, boomer-*age* children bemoaning the fact that "Mom and Dad are out spending *our* money."

Hello? It's not our money. It may never be. It belongs to our parents. Contrary to popular thought, we do not *deserve* it. Therefore, it's not only boorish but also stupid to plan on it.

Kathy and I have tried to remove any inheritance pressure from our parents by assuring them that we hope they spend their last dollar the day they die. In other