



Research Paper

**Creating an Intentional Budget**

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1. The information in this material is not intended as tax or legal advice. Please consult legal or tax professionals for specific information regarding your individual situation.
2. The content herein was developed from sources believed to be providing accurate information.
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4. All final investment and planning decisions are at the discretion of the client.

## INTRODUCTION

A budget is an estimate of income and expenses for a future period of time which, along with an income statement and balance sheet, help define your current financial situation and are the basis of any financial plan. A budget defines your ability to save for future goals or highlights the need to make adjustments to avoid or reduce debt. A budget is also an excellent tool to assess potential changes in your financial life such as buying a house, starting a business, relocating or changing jobs.

This article will provide an overview of the budgeting process and provide guidance on how to create an intentional budget. An intentional budget should be detailed, set for a clearly defined window of time, monitored for accuracy and updated as appropriate.

We promote a budgeting process that starts simple – an Excel spreadsheet will suffice – as we have found this is the most effective option to establish an initial budget and create variations to assess what-if scenarios.

# TERMS AND DEFINITIONS

1. Budget: a spending plan defining **projected** income and expenses. Similar in structure to an Income Statement, a budget is based on projections of **FUTURE** income and expenses and the resultant **FUTURE** cash flow. A budget is a key tool in building a Financial Plan.
2. Income: money received for labor or as a return on an investment. We use three general categories of income, aligned with taxation factors:
  - A. Earned income: salary, wages, tips, commission, bonuses.
  - B. Portfolio income: dividends and capital gains earned on invested assets.
  - C. Passive income: interest income, royalties, rent and certain types of owner's equity.
3. Expenses: services and products that you pay for. Examples include rent, utilities, daycare, insurance, monthly mortgage payments, monthly car payments, food and entertainment, clothing, taxes, transportation (gas, maintenance, parking, tolls), travel and recreation, subscriptions, gifts, etc.
4. Cash Flow: this is calculated by subtracting expenses for a given period from income for that same period. A positive cash flow denotes a surplus of money exists at the end of the measured period of time; a negative cash flow indicates that more money is being spent than is being earned during the measured period of time. A positive cash flow can be used to INCREASE net worth; a negative cash flow will DECREASE net worth.

## TYPICAL USES OF A BUDGET

Establishing a budget, and checking it periodically for accuracy, is a fundamental financial planning task for everyone, regardless of their financial situation. A budget helps create financial stability and puts you on stronger financial footing for both the day-to-day and long-term financial timeframe.

A budget is used to:

1. Understand and manage monthly expenses. With the increased use of credit cards, monthly subscription-based expenses, and direct ACH payment options, spending has become easier and not as closely monitored.
2. Assess your financial ability to fund additional expenses and purchases.
3. Prepare for life's unpredictable events via the establishment of an emergency savings account.
4. Allocate excess cash flow for investing.
5. Assess the implications of life events (marriage, job change, retirement, home purchase, childcare, etc.).

# GETTING STARTED

1. Gather documents that define your income, expenses, assets and liabilities. These include:
  - a. Pay stubs or W2 forms.
  - b. Pension, Annuity and Social Security Statements.
  - c. Credit card statements.
  - d. Checking account statements.
  - e. Investment and retirement account statements.
  - f. Health Savings Account and Flexible Savings Accounts (FHA, FDCA, etc.) statements.
  - g. Loan and mortgage summaries.
2. Create a Balance Sheet and Income Statement. These documents are discussed further in other Eustace Advisor resources.
  - a. An Income Statement summarizes income, expenses and net cash flow for a **past** period (typically a month, 3 months or 12 months). Similar in structure to a budget, the income statement is based on income and expenses that have already occurred.
  - b. Most people find that their income statement is an excellent starting point to establish their budget. See the Resources section.
3. Select a simple budget template or app that is easy to complete and maintain. The income and expenses categories of your budget template should match, or be very similar to, the categories of your Income Statement.
4. Use the same time period to budget income and expenses (monthly or quarterly).
5. Define all sources of projected income.
  - a. If your income fluctuates month-to-month due to bonuses or commissions, or an irregular payroll schedule, estimate over a 6-month or 12-month period, then normalize to a monthly or quarterly average.
  - b. I often recommend using the last pay stub of a given calendar year, dividing the pay/withholding/tax information by 12, and using that as a starting point for the monthly amount of those categories.
6. Define all projected expenses.
  - a. Your income statement will help, as a start. Use the expenses in your Income Statement as a baseline, then adjust as appropriate for the future period you are budgeting.
  - b. Add any new expenses that you expect to incur. Example: if you are buying a house, you will have property tax, home maintenance, HOA, and other expenses that don't exist for renters.
7. Subtract your projected expenses from your projected income to define your projected cash flow.

# EUSTACE ADVISORS' BUDGET TEMPLATE

Monthly Budget - <Client Name>		
Date Completed		
<b>GROSS INCOME</b>	Monthly Amount	Description
Salary, Bonuses and Commissions		Pre-tax amounts
Investment income (interest, dividends, capital gain distributions)		Only include if NOT re-invested.
Social Security		
Retirement Plan Distributions		
Pension		
Annuity		
Alimony / Child Support		
Business and Rental income		
Other (tips, royalties, etc.)		
<b>Total Gross Income</b>	<b>\$0</b>	
<b>WITHHOLDING</b>	Monthly Amount	Description
Withholding - Retirement Plan		
Withholding - Health, Dental, Vision Insurance		
Withholding - Life/Disability Insurance		
Withholding - FSA/HSA		
Withholding - Income Taxes		
Withholding - Other		
<b>Total Withholding</b>	<b>\$0</b>	
<b>Net Take Home Pay</b>	<b>\$0</b>	
<b>EXPENSES</b>	Monthly Amount	Description
Alimony / Child Support		
Charitable contributions / Gifts		
Clothing		
Entertainment		
Food (groceries and dining out)		
Gifts		
Gym and other memberships (streaming services, etc)		
Household supplies and maintenance		
Insurance - Auto		
Insurance - Health and LTC		
Insurance - Homeowner's / Renter's		
Insurance - Life / Disability		
Insurance - other		
Loan - Auto		
Loan - Other		
Loan - Student		
Medical / Dental / Vision out-of-pocket		
Mortgage		
Rent		
Taxes (property)		
Transportation (fuel, parking, maintenance, etc.)		
Travel		
Utilities (electric, water, cable, internet)		
Other		
<b>Total Expenses</b>	<b>\$0</b>	
<b>Monthly Projected Cash Flow - SURPLUS / (DEFICIT)</b>	<b>\$0</b>	
<b>Notes</b>		
1) All values are MONTHLY, unless otherwise noted.		
2) All income is PRE-TAX.		

This template is for a single person; I also have a template for couples.

# ONGOING BUDGET MANAGEMENT

Once a Budget is established, monitor and adjust it on a regular basis.

1. Track actual income and expenses vs. the budget on a monthly basis, to start.

*Eustace Advisors offers a template that automatically calculates budget vs. actual differences.*

2. Adjust your budget as appropriate to reflect improved estimates.
3. Continue the monthly updates or until actuals correlate with projections.

Once your budget is stable:

1. Review and update every six months or when a pending life change is imminent.
2. If expenditures are higher than projected, scrutinize your spending and try to reduce expenses to establish or increase your budget surplus.
3. If you have a surplus, allocate the surplus amount every month towards your emergency fund, long-term savings goals, or a planned significant purchase (home, car, etc.). This is sometimes referred to as “paying yourself first” – i.e., prioritizing saving a portion of your income before paying for other expenses.

## WHAT IF MY BUDGET IS IN DEFICIT MODE?

As noted, the bottom line of a budget is your Net Cash Flow.

**Net Cash Flow = Income MINUS Expenses.**

A positive Net Cash Flow indicates you are bringing in more money than you are spending; this is a good situation. A negative Net Cash Flow, also referred to as a budget deficit, indicates you are spending more money than you are earning; this situation needs to be addressed to avoid debt.

The math behind addressing a budget deficit is fairly simple, and requires an increase in income, a decrease in expenses, or both. Options to consider include:

1. Seek additional income: ask for a raise, work overtime, get a 2<sup>nd</sup> job, sublet a spare room, etc.
2. Reduce expenses:
  - A. Start with discretionary expenses, which are typically the easiest to reduce or eliminate.
    - Reduce dining out, travel and entertainment expenses.
    - Scrutinize automatic monthly payments (streaming, gyms, other memberships).
  - B. Then focus on the largest expense categories (loans, insurance, food/entertainment).
    - Assess loans for interest reduction opportunities.
    - Scrutinize credit card usage and avoid paying interest on balances.
    - Shop around for lower-cost insurance.

There is much literature written on managing expenses – review online resources or consult with a financial advisor for help.

3. If necessary (i.e., Steps #1 and #2 above aren't sufficient), reduce retirement and discretionary savings allocations in your budget, TEMPORARILY. This is not a good long-term budget fix but is a better temporary option than taking on debt.
4. If you are comfortable using financial apps, consider the use of a budget app that tracks your actual spending against your budget goals and warns you if the budget category is being exceeded.

## BUDGETING APPS

There are many tools available to create and manage a budget.

### Our Recommended Options to Start (as of mid-2024)

We suggest that you start with one of these options, keep things simple to start, and always take advantage of a free trial if the app has a fee to see if you like it before making a commitment.

1. Excel template. There are many free Excel Budget templates, including ours.
  - A. Advantages: Cost (free), easy to use and customize, can be updated on desktop or mobile devices.
  - B. Disadvantages: Requires manual data entry, use on mobile devices isn't easy, no pizzazz (reminders, etc.).
2. Nerdwallet. <https://www.nerdwallet.com/article/finance/nerdwallet-budget-calculator>
  - A. Advantages: Free; you can start with their simple budgeting template or create an account to access their budget app; part of the extensive NerdWallet ecosystem with a lot of resources (blogs, etc.).
  - B. Disadvantages: Lots of ads and partner offers (typical for a free app).
3. YNAB – You Need A Budget. <https://www.ynab.com/>
  - A. Advantages: Includes financial education features and a lot of resources (blogs, etc.).
  - B. Disadvantages: \$99/year fee; steep learning curve and time required for maintenance vs. options 1 and 2 above.

### Other Options to Consider

1. Monarch – emerging as the replacement of choice for former Mint users.
2. Simplifi – requires account synching; best for detailed cash flow analysis.
3. EveryDollar (part of Ramsey Solutions) – aligns with Ramsey's Financial Peace University.
4. Fudget and Goodbudget – limited Free versions; easy to use.
5. Honeydue – best solution for couples with both separate and integrated accounts.
6. Personal Capital – more of a wealth building application; better for investors.
7. Pocketguard – requires account synching; makes budget recommendations. Often recommended for Overspenders.
8. Wally – customizable; only available on iPhones. Liked by data-driven, advanced users.



# SITUATIONAL EXAMPLE

This example is hypothetical and is NOT based on a real client.

## Background:

- Ray and Lottie are a married couple with two school-age children. They live in Peekskill, NY.
- Ray and Lottie own a home, with approximately 15 years remaining on their mortgage.
- Lottie works full-time and her annual compensation is \$80,000, before taxes and withholding.
- Ray works part-time and his annual compensation is \$24,000, before taxes and withholding.
- Ray and Lottie have \$50,000 in savings and checking accounts, \$50,000 in retirement accounts, and estimate their home is worth \$200,000.
- Based on sound financial advice, Ray and Lottie have an Emergency Savings Account at their bank with 6 months of living expenses in value.

## Preparation

As recommended earlier in this document, Ray and Lottie began the budgeting process by establishing a Balance Sheet and Income Statement. Creation of these documents required them to gather financial documents including pay stubs, bank and retirement account statements, and their credit card statement.


1. Lottie's pay stub:
  - Lottie gets paid 2x/month; straight salary of \$80,000 per year with no bonuses or commissions.
  - Lottie withholds 8% as a retirement plan contribution.
  - Lottie's income tax withholding is 15% of her gross income.
  - Lottie pays \$200/month towards her employer health insurance coverage.
2. Ray's pay stub:
  - Ray gets paid 1x/month; straight salary of \$24,000 per year with no bonuses or commissions.
  - Ray doesn't have an employer retirement plan.
  - Ray's income tax withholding is 15% of his gross income.
3. Expenses:
  - Home-related (per month): \$1,500-mortgage; \$200-property taxes; \$150-insurance; \$200-maintenance.
  - Transportation: their car loan and insurance costs were defined in their bank statements, and they used their credit card statements to define fuel, parking and maintenance costs.
  - Food, clothing, utilities, entertainment, household supplies: taken from bank and credit card statements.
  - Gifts: estimated \$300 per month average for charity and personal gifts.
4. Discretionary savings: Ray and Lottie have been contributing \$300/month to education savings plans for their children.

## Creating the Budget

Ray and Lottie were confident that they could establish their budget using the Excel spreadsheet template provided by Eustace Advisors. Once they established this initial budget, they may adopt an app-based budgeting tool such as Honeydue.

To further simplify the budget template, Ray and Lottie removed categories that weren't relevant to their personal situation, such as alimony, rent and social security.

## The Resultant Budget

		
Financial Budget - Ray and Lottie		
Date Completed	11/7/2023	
INCOME	Monthly amount	Notes
Salary - Lottie	\$6,667	Gross amount before taxes and withholding.
Salary - Ray	\$2,000	Gross amount before taxes and withholding.
Other income	\$0	
<b>TOTAL INCOME</b>	<b>\$8,667</b>	
EXPENSES		
Withholding - Retirement Plan	\$533	Per Lottie's pay stub
Withholding - Health Insurance	\$200	Per Lottie's pay stub
Withholding - Income Taxes	\$1,300	Per both pay stubs
Mortgage	\$1,500	Per bank statement
Utilities (electric, water, cable, internet)	\$300	Per bank statement
Household supplies and maintenance	\$300	Per credit card statements
Loan - Auto	\$225	Per bank statement
Transportation (fuel, parking, maintenance, etc.)	\$100	Per credit card statements
Insurance - Auto	\$100	Per bank statement
Insurance - Health and LTC	\$0	
Insurance - Life / Disability	\$75	Per bank statement
Insurance - Homeowner's / Renter's	\$150	Per bank statement
Clothing	\$200	Per credit card statements
Entertainment	\$250	included kid's camps and sports
Food (groceries and dining out)	\$800	Per credit card statements
Gym and other memberships (streaming services, etc)	\$75	Per credit card statements
Medical / Dental / Vision out-of-pocket	\$100	co-pays, deductible and miscellaneous
Taxes (property)	\$200	
Travel	\$250	allocated annual \$3000 trip into monthly portions
Charitable contributions / Gifts	\$300	
Other	\$300	education savings accounts for kids
<b>TOTAL EXPENSES</b>	<b>\$7,258</b>	
<b>NET CASH FLOW</b>	<b>\$1,408</b>	GOOD NEWS! This excess can be invested.

## The Budgeting Effort Never Ends

Since a budget is a PROJECTION of future income and expenses, Ray and Lottie need to track actual income and expenses vs. the budget on a monthly basis, to start. Eustace Advisors has an Actual vs. Budget Template which automatically calculates the differences between projections and actuals to highlight areas that need analysis.

- If actuals differ from the budget estimates, Ray and Lottie need to assess the difference and adjust their budget as appropriate to reflect improved estimates.
- Items such as salary increases, loan payoffs, property tax increases should be reflected in budget updates.
- Ray and Lottie should continue the monthly budget reviews and updates for at least 3 months, or until actuals match projections.

Once their budget is stable:

- They can reduce the frequency of budget reviews to every six months, or in the case of a significant change in income or expenses (pay raise, loan payoff, etc.).
- If the budget surplus reflected in their spreadsheet is validated per actual data, Ray and Lottie should allocate a significant portion of the \$1,408 surplus amount every month towards other savings goals. Since they already have an adequate emergency savings fund, they can allocate this monthly surplus to other financial goals or to pay off their loans early.

## BOTTOM LINE

If we compare your financial journey to a physical journey, your balance statement and income statement are your current location, your financial goals are your destination, and your budget is the route currently defined to get from location to destination. As with a physical journey, the budget may need to be updated (rerouted) periodically to reflect changes in circumstances.

If you don't have a budget, you should make the time to build one as it is arguably the most important tool to start building a sound financial plan.

If you need assistance getting your budget in place, feel free to contact us.

# RESOURCES AND REFERENCES

Eustace Advisors has several Budget templates available for client use, in addition to Income Statement and Balance Sheet templates - contact us for access.

## Websites

1. [www.investopedia.com](http://www.investopedia.com) – this is a great resource for financial, tax and estate related topics.
2. [www.nerdwallet.com](http://www.nerdwallet.com) - this resource is very helpful for assessing “best of” subjects such as credit cards, insurance, loans, banks.
3. <https://www.nerdwallet.com/article/finance/best-budget-apps>.
4. [www.thebalancemoney.com](http://www.thebalancemoney.com) – similar to Nerdwallet, this resource has a wide range of calculators, “best of” articles and useful posts on a range of personal finance topics.
5. <https://bettermoneyhabits.bankofamerica.com/en/saving-budgeting/creating-a-budget>.
6. <https://tickertape.tdameritrade.com/personal-finance/monthly-budget-checklist-17451>.
7. <https://www.investopedia.com/these-are-the-costs-of-family-life-to-the-dollar-8422254>.