The 15 Crucial Steps Needed To Achieve Financial Independence

CORNERSTONE
WEALTH MANAGEMENT

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Just about everybody wants to become financially independent – so why do so few people get there?

One of the secrets to attaining financial independence is that it doesn't usually "just happen".

It starts with a detailed plan, and a willingness to commit to that plan.

To help you get going in the right direction, here are 15 steps to become financially independent.

1. "Decide You Want It More than You Are Afraid Of It"

OK - that quote is from the recently discredited Bill Cosby, but it's brilliant nonetheless. And it's an important point too. One of the reasons more people don't reach financial independence is they're afraid – not of being financially independent, but of the changes in their lives they'll have to make to get there.

If you are new to the financial planning process, it's important to remember you don't need to go from zero to sixty overnight. Just like a fitness trainer would be hesitant to recommend an all-out body straining routine on your first day in the gym, I wouldn't expect someone to start implementing advanced planning techniques in the first week. Pick a reasonable and attainable goal, and get used to achieving small wins on your track to financial independence.

For example, if you are new to saving, you don’t need to immediately put aside half of your paycheck. Start with a small amount - maybe $20 per pay period - and increase it as you get more comfortable with the process. Starting out slow will help you build the confidence needed for long-term success.

In order to become financially independent, you have to have a serious heart-to-heart talk with yourself. You want to get a few things clear in your head, including:

- A definition of exactly what financial independence means to you - following someone else's definition won't get you there
- A realistic picture of your current financial situation
- A realistic idea as to what you'll have to give up to get where you want to go
- A realistic assessment of the obstacles in your path
- A series of goals that will help you to become financially independent

That last point is a discussion all its own…

2. Create a Series of Steps that Will get You Where You Want to Go

Becoming financially independent isn't a single goal, but a series of sub-goals. This is because your financial life has several facets. In order to reach your overall goal of financial independence, you'll have to establish goals in the various areas of your financial life, including,

- Increasing your income
- Controlling your spending habits
- Paying off your student loan and credit card debt
- Understanding your savings patterns
- Determining your investment objectives
- Defining your long-term financial goals
- Purchasing the best life insurance for your family
- Implementing a legacy plan for your heirs

We're going to go over each of these categories in some detail, but it's important you create such a list, with a corresponding goal relating to each individual category. That will ensure you are moving your entire financial situation forward, rather than trying to do it one category at the time.

3. Commit Now that You Will Live Beneath Your Means for the Rest of Your Life

If I can pick one step out of this list 15 that's more important than the rest, it's this one. That's because no other steps you take will be possible unless you fully commit to mastering this one.

The reason it’s so important is it’s the single step that will provide most of the spare cash you will need in order to accomplish most of the other steps. Learning to live beneath your means is one of the central costs of learning how to become financially independent. And if you have not mastered this technique in the past, doing so will range anywhere from uncomfortable to downright painful.

“Setting goals is the first step into turning the invisible into the visible”

Delayed Gratification. Get comfortable with that term. No - make that, get very comfortable with it. It means being willing to sacrifice now in order to provide for a better life for you and your loved ones in the future.

If you're currently struggling with your finances, there'll be no easy way over this hurdle. You'll probably have to cut out every expense in your budget that is not absolutely necessary, it even do what you can to reduce those that are.

It could include passing of the annual family vacation, driving your car for years after paying off your car loan, living in your current home even though most of your neighbors traded up, and buying your clothing in thrift stores while everyone else you know shopping at the mall.

That's just a short list of the sacrifices you'll have to make. But in making them, you'll be clearing money in your budget to build savings, to get out of debt, and to invest for the future.

4. Block Out the Spendthrifts in Your Life

Are there one or more people in your social circle who you could reasonably characterize as a spendthrift? If so, one of the sacrifices you may need to make to reach financial independence will be to either reduce your contact with this person (or people), or even eliminate them from your life altogether.

I know that sounds harsh, but is also totally necessary. The people who we keep company with can have a profound effect on how we view and spend money.

If you are surrounded by people who "live for the moment" - meaning they mostly spend their money having fun rather than saving for the future, you will inevitably get pulled into that behavior.

5. Always Keep Your Career or Business Moving Forward

In Step 3 I said that living beneath your means is the single most important step on this list, and that's true. But you can give yourself a major assist in that effort by making sure you steadily increase your income in the future. If you can steadily increase your income – while keeping your spending level – you will reach all of your financial goals much more quickly.

You can keep your career moving forward by keeping your work skills sharp, and increasing your value to your employer. You should put yourself in the running for promotions where possible, and hold yourself open for better opportunities with other employers. If you are self-employed, it means steadily working to keep your business moving up to the next level.

Working on advancing your career is like investing in yourself. It's one of the best ways to get a good return on your investment, whether you are salaried or self-employed.

If you are self-employed, that just means you have a lot of "bosses" that you serve. So, periodically ask those "bosses/clients" how you can better serve them. I have done this in the past through simple surveys. I simply ask what challenges they are facing and how I can better serve them. The better you can serve people, the more value you bring to the table, the more it helps you become a higher earner.

6. Vow to Always Save Money - No Matter What Your Income Is

Don't be one of those people who says "I'll start saving money when..." The problem with telling yourself that is "when" never comes.

The better position? When is now! When is always. You should always be saving money no matter what's happening. That's one of the very best strategies to make sure you are always moving forward.

If you don't have enough room in your budget to save money now, then the answer is to increase your income, lower your expenses, or both.

We set up a business and personal budget for ourselves and include savings goals. Then to keep ourselves accountable we review our budget monthly. This keeps us on track to reaching our financial goals. I'd recommend setting up a system that works best for you and your family. Just writing down your goals will help you start the process. But, reviewing them daily and having honest conversations about where you are financially will determine your success or failure in becoming financially free.

Never let excuses stand in the way of saving money. It's a long term goal that starts today – and never stops.

7. Insulate Yourself in the Short Run - Creating a Safety Net

If you have been living paycheck-to-paycheck up to this point, your first savings goal should be to create a safety net. You can do that by creating an emergency fund.

An emergency fund should be held in a perfectly safe account – like a savings account, money market account, or a short-term certificate of deposit. It's not for investment, because investment involves risk, and that's not the purpose of an emergency fund.

Your first goal should be to accumulate a sufficient amount of cash in the account to cover 30 days worth of living expenses. Once that's achieved, your goal should be to add another 30 days worth of living expenses. The account should have between three months and six months of living expenses if you're a salaried employee, and between 6 and 12 months if you have a self-employed job or paid entirely by commissions.

Life is full of surprises and changes, and it will do you a lot of good to have a liquid stash of cash you can access quickly in case of an emergency. Emergencies like getting laid off, the car dying, or your child needing an urgent medical treatment, and your health insurance doesn't quite provide the coverage you thought it did.

Do you want to be up a creek without a paddle when those situations occur? Sure, you could probably charge those emergencies to a credit card with rewards, but that's going to end up costing you a lot in interest charges in the long-run. The goal is to make smart choices by planning ahead.

Additionally, more and more today, I am seeing the need for an emergency fund because people get sick of working for tyrant bosses, and want the financial flexibility to walk out the door if they can't stand the frustration anymore. No emergency fund - no flexibility to call your own shots.

8. Invest Everything Above That

Once your emergency fund is adequately stocked, you can begin thinking about investing your money. This is important, because investing is about using your money to earn more money. The larger your investment portfolio becomes, the closer you get to financial independence.

Ideally, your efforts to save money should never slow down once you have built your emergency fund. Instead, increase your efforts to fund your investment accounts. That should be easier to do once you have an emergency fund in place.

9. Invest No Matter What the Market is Doing

In hindsight, it's obvious there have been better times to invest than others. But since no one knows what the future holds, you can't know when that will be in the future. Plan to invest no matter what the market is doing. If you're investing periodically, you'll be dollar cost averaging into the market, which will minimize the risk you're taking should the market decline.

If you do feel it's a bad time to invest, then simply cut back on how much you are investing in equities. But at the same time, continue accumulating cash and fixed income investments in your portfolio, that way it'll be there to buy when the timing looks little bit more favorable.

10. Diversify Your Investments

This gets back to not knowing what the markets will do in the future. The best way to protect yourself against unexpected surprises is to diversify your investments across several different asset classes.

Big picture, you should have a certain amount of money invested stocks, fixed income investments, peer to peer lending, cash, natural resources, and real estate. That will keep you from taking a big hit in the event any of those sectors crashes, while at the same time taking advantage of strong markets wherever they may be.

Also, don't get crazy with your investments. Stick with index funds for stocks, since they have lower investment fees and don't generate a whole lot of capital gains taxes. Keep your real estate investments in real estate investment trusts (REITs), which are actually something like real estate portfolios themselves.

11. Diversify Your Income Sources Too!

Just as you would diversify your investment portfolio, you should also diversify how you make money. Both the economy and the job market are not as stable as they were a couple of decades ago, and you have to be prepared to ride out the ups and downs.

For example, if you have a full-time job, work on creating a side business. Not only will it provide you with an additional source of income for savings and debt reduction, but it may also form the replacement for the job you lose in the next recession.

If you have a business, look to diversify into related sources of income. You may even consider creating passive income sources, such as being an investor in a small business that is run by someone else.

Multiple income sources, in and of themselves, can represent a form of financial independence all by themselves.

12. Shield as Much Income From Taxes as Possible

Taxes represent a major reduction in your income, that means you will have less money available to save, invest, and pay off debt. By using strategies that reduce income taxes, you'll be able to keep more of your income, rather than turning it over to the tax authorities.

The easiest and best way to shield your income from taxes is retirement plans. If your employer offers a 401(k) plan at work, put as much of your income into it as you can afford. At a minimum, invest up to the amount that will get you the maximum employer matching contribution. For example, if your employer offers a 50% match (3%) up to a 6% contribution by you, you should contribute at least 6% – and of course, more is always better.

If you're self-employed, create your own retirement plan for your business, such as a self Managed Super Fund.

13. Get Out - and Stay Out - of Debt

It's hard to make a case for being financially independent when you owe money to banks or other people. You should have a goal of getting out of debt as soon as possible.

You can have different time horizons for getting out of debt with each debt category.

For example, you can commit to eliminating your credit card debt in five years, while in 10 years, eliminating your student Hex debt and your mortgage in 15 years.

That's not an overnight solution to your current debt problems, but it sets you to heading in the right direction.

And once you get out of debt in any category, stay out and never come back! There's no such thing as "good debt" when you're trying to achieve financial independence.

14. Make Sure You Have Enough Insurance Coverage

Early in your journey toward financial independence, you may want to maintain minimal insurance coverage to keep your insurance expense low. But, as your wealth grows, your insurance coverage has to rise along with it.

Though we don't normally think of it in this way, the primary purpose of insurance is to protect our assets. The more assets you have, the greater your insurance coverage needs to be.

Review all of your coverages annually. That includes health, auto, homeowners, disability, and affordable life insurance. As your wealth grows, low coverage levels and high deductibles can work against you in a crisis. That defeats the whole purpose of having insurance of any kind.

15. Commit to Refocusing on Your Goal Regularly

In order to become financially independent, you will need to become fully committed to your plan. You should have a written plan – that includes goals for each financial category – and plan to review them annually.

The purpose is twofold:

1. To make sure your goals are on track, and
2. To keep yourself focused on your ultimate goal of becoming financially independent

This is incredibly important, particularly number two. It's very easy to get sidetracked on the road to financial independence. For example, you may find yourself getting very comfortable about two thirds of the way there, and starting to spend more money and save less.

Think of it as an affirmation, in which you renew your commitment. You should do that at least annually, but in reality you should do it as much as you need to.

Becoming financially independent isn't easy. That's why you need a detailed plan, and a commitment stick to it. Use this list as a guide, and modify it to fit your own circumstances. You'll get there - as long as you don't give up!