



# Control Your Cash Flow – the Envelope System

Robert Abboud

One of the biggest mistakes people make with money is that they do not have any control over their monthly cash flow. Money comes in and money goes out, few actually take the time to review how much they make and how much they spend and then try and work in some savings for life goals. Unfortunately most budgets are like diets as they are very hard to stick to. One of the most successful and long lasting diets in the world is Weight Watchers. Why? It's a simple, common sense diet that is easy to implement and more important to maintain.

## Introducing the Envelope System

The envelope system is a cash flow control system that has been around for years and is one of the few “budgets” that works because it is so simple. Here is the concept in six words: Don't buy what you can't afford. As reasonable as this sounds, not many people follow this principle. Nowadays we are constantly hearing ads that suggest easy credit or refinancing. It is not uncommon for people to borrow to buy furniture, TVs, computers or to have their eyes lasered. The envelope system is a simple, proven method that helps people live within their means while still doing the things they want and can afford to do.

It works as follows. First, you need to know what you earn each month, after tax. For example, if the amount you receive in your bank account from your employer every two weeks is \$1,700, then your net monthly income is simply \$3,400. Don't worry about the extra two pays per year not being accounted for. Next, list your monthly expenses (see the cash flow analysis worksheet or for a full-size Excel cash flow sheet go to [www.lifegoalsplanning.com](http://www.lifegoalsplanning.com) and click on resources).

You will find that most of your monthly expenses are relatively consistent and fixed, such as your mortgage/rent, property taxes, utilities, retirement savings, goal savings, car loan/lease, etc. These fixed expenses should be auto-

*“Everything should be made as simple as possible, but not simpler.”* Albert Einstein

matically debited from your bank account. This puts most of your monthly cash flow on automatic pilot.

## No More Variable Expenses – Make It Fixed

This is the most important part of any budget and it is where most budgets usually fall apart. Many of your discretionary expenses, such as clothing, home maintenance, gifts, groceries, and entertainment are somewhat optional and vary every month. For example, gift expenses are usually much

Cashflow Analysis Worksheet			
	Existing	Revised	
Pension Income (Net)	\$ _____	\$ _____	
Salary (Net)	\$ _____	\$ _____	
Spouse's Salary (Net)	\$ _____	\$ _____	
Other			
<b>Monthly Net Income:</b>	<b>\$ _____</b>	<b>\$ _____</b>	
<b>Less:</b>			
Mortgage/Rent	\$ _____	\$ _____	
House Insurance	\$ _____	\$ _____	
Property Taxes	\$ _____	\$ _____	
Car Loan	\$ _____	\$ _____	
Car Insurance	\$ _____	\$ _____	
Car Maintenance	\$ _____	\$ _____	
Pocket Money	\$ _____	\$ _____	
Other Loan	\$ _____	\$ _____	
Memberships	\$ _____	\$ _____	
Credit Card	\$ _____	\$ _____	
Groceries	\$ _____	\$ _____	
Utilities (cable, heat, hydro, phone, water)	\$ _____	\$ _____	
Clothing	\$ _____	\$ _____	
Entertainment	\$ _____	\$ _____	
Gifts	\$ _____	\$ _____	
Education Savings	\$ _____	\$ _____	
Travel	\$ _____	\$ _____	
Gas (automobile)	\$ _____	\$ _____	
Life Insurance	\$ _____	\$ _____	
House Maintenance	\$ _____	\$ _____	
Medical	\$ _____	\$ _____	
Charity	\$ _____	\$ _____	
Child Care	\$ _____	\$ _____	
Miscellaneous	\$ _____	\$ _____	
RRSP Savings	\$ _____	\$ _____	
Other Savings	\$ _____	\$ _____	
Large Trip/Emergency	\$ _____	\$ _____	
Other	\$ _____	\$ _____	
Other	\$ _____	\$ _____	
<b>Total Expenses:</b>	<b>\$ _____</b>	<b>\$ _____</b>	
<b>Surplus / Shortfall</b>	<b>\$ _____</b>	<b>\$ _____</b>	

higher around the holidays. Put a monthly fixed dollar amount in these discretionary expenses. Try and use a number that is realistic and that you would feel comfortable spending each month. If you feel \$300 per month is a reasonable amount to spend on entertainment, put that figure in the entertainment column. Do this with each category. When you get to the bottom of the list, add up all your expenses and deduct them from your net income. You should be running either a surplus (extra \$\$) or a shortfall (not enough \$\$). If you are running a shortfall, you should review and reduce where you can until you run a balanced budget. Remember, if you don't run a balanced budget each month, you will only continue to borrow to sustain the lifestyle you are living, and it will eventually catch up with you.

## Implementing the System – Cash is Back

Groceries are the one variable expense that cannot be radically reduced. They are not really optional, as we need to eat on a regular basis. So, for groceries, if your monthly budget is \$600, then I suggest that with each pay (assuming you are paid bi-weekly) you take \$300 cash (yes, cash) and place it in an envelope labelled Groceries. Use this cash to pay for your groceries. Next, set up envelopes for the other usual expenses. Label your envelopes as follows (dollar amounts are for you to fill in, these are just examples): Gifts (\$200 per month), Clothing (\$200 per month), Entertainment (\$300 per month), Home Maintenance (\$100 per month). You now know you have discretionary expenses of \$800 per month, or \$400 per pay. When you receive your pay, go to the bank machine and withdraw \$400 cash. When you get home, place \$100 in the Clothing envelope, \$100 in the Gift envelope, \$150 in the Entertainment envelope, and \$50 in the Home Maintenance envelope. Yes, it is a little time consuming, but it works. And yes, you should physically put cash in the envelopes.

Now what? Anytime you want to do something under the Entertainment heading, such as order take-out on Friday night, use the cash in that envelope. If there is no cash in the Entertainment envelope, unfortunately that means no take-out tonight – so get cooking! On the other hand, if you haven't used any Entertainment money in five months, you would have \$1,500 saved up. Reward yourself – maybe book a weekend spa or golf getaway!

For Gifts, most of your spending will occur at certain times of the year, i.e. birthdays, Christmas, etc. So, don't spend it on something else if you notice it's full of cash. Clothing expenses can vary wildly as we sometimes go months without buying any clothes and then replace a wardrobe in one swift shopping session. So, only use cash from your Clothing envelope

to buy clothes. If there is not enough money in the envelope to buy your outfit, then you'll have to wait. You could always just take some cash from your entertainment envelope to use for clothes, but that would mean less money for entertainment that month. It's up to you.

If you are uncomfortable with the idea of having all this cash on hand at home, you could set up a separate account and have the bi-weekly amount automatically go to this account. But, then you would have to track how much of the balance in the account was for each expense. This practice could prove quite time consuming and may eventually be overwhelming and cause you to give up on the system. Our clients have tried many different envelope system variables, from spreadsheets to multiple accounts, and in the end the cash-in-envelopes method always works best and is the easiest to stick to. If you feel that you need one, buy a safe to keep your cash in.

## The Debt-Free World

The envelope system makes money real again. Credit cards, direct payment, buy now and pay later plans – money has become virtual. It's very easy to lose track of something that was never physically in your hands to begin with. Now

you can even buy fast food on your credit card. Is that really necessary? Our society is far too focused on having everything we need or want now, which is why we are more indebted than all previous generations. If you don't have the cash to buy something, wait until you do.

This was obvious to previous generations, but seems to be a new concept to this generation. Remember, there are many industries that have a vested (and very profitable) interest in keeping you in debt. In 2005, for each \$1.00 of disposable income, Canadians owed \$1.16 (Statistics Canada, *Perspectives on Labour and Income*, January 2007). Somehow, the worlds of marketing, industry, and banking have managed to convince us that debt is the norm and not the exception.

## The Envelope System in Action

One of my clients has been using the envelope system to manage their family's monthly cash flow for almost 7 years now. As a couple, they are much happier, as they feel the money disagreements have all but disappeared. They now live within the agreed-upon expense levels. Now his spouse knows she has \$300 per month that she can spend on home decorating without having to "get it approved". They say that they cannot imagine going back to the old way of doing things. By the way, this is a family that has a net worth

*"Don't buy things; buy freedom."* David Futrelle

of \$2 million and earns an annual household income of over \$170,000.

Another family, a working couple with three children, resisted the envelope system for years. Due to a growing debt and a sense of being out of control, they decided to give the envelope system a real try. Two years later, they are envelope system believers. Their debts have been reduced dramatically, and they were able to take a family vacation to the Caribbean that they had always dreamed of – and they had the cash to pay for it!

### Stick to It

This is not to say the first couple of months will not be challenging, but believe me, it is worth it. After four to five months it will become routine. Yes, you will be frustrated at times because you don't have the cash to buy something

you really, really want. But sometimes that can be a good thing. It should eliminate spontaneous buying, and will allow you to appreciate the item even more if you finally do get it.

*"I may not be there yet, but I'm closer than I was yesterday."*

Author Unknown

Here is the best part. Once you get the system running for a few months, you may be able to start directing some monthly savings towards some of your life goals. Maybe you've always dreamed of taking a cross Canada train adventure, going to Paris for the week-

end or starting your own business. Whether you earn \$35,000 or \$170,000, you can apply the envelope system, or a modified version of it, for your lifestyle to help you take control of your cash flow.

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### Special Report



# Critical Illness Insurance 101

Rino Racanelli

**Y**ou need financial independence when you're ill. Not because you're going to die, but because you're going to live," stated Dr. Marius Barnard, world renowned heart surgeon who helped develop critical illness insurance.

In 1996, I was invited to attend an all day seminar hosted by Canada Life Assurance Company. They were introducing a new product called critical illness insurance.

Critical illness insurance had already been well established in countries such as South Africa, Australia, and England. And, for the first time ever, Canadians would have an opportunity to purchase the product here.

They explained how critical illness insurance began and how its founder, South African, Dr. Marius Barnard was consulting with Canada Life to develop a plan for Canadians. Dr. Barnard witnessed the emotional strains that many of his patients faced after surviving serious illnesses. Financial stress often worked against recovery. In many cases, it

left patients struggling to pay bills as they resumed their lives. These were real life examples of people who had survived a serious illness, then had to deal with the medical and financial burdens of that illness.

Getting sick isn't something any of us likes to think about. But it does happen. When it happens, thanks to advances in medical science and technology, along with improvements in healthy living, chances are you'll recover and get on with your life.

It got me thinking and asking myself.

- What if I was diagnosed with a critical illness?
- Where would the money come from?
- What would happen to my finances?
- Could I cover all of my debts including my mortgage?
- Could I cover my medical expenses?

Critical illness insurance was designed to cover these costs and allow us to focus on what matters most – getting better.