

LEARN TO PAY YOURSELF FIRST

Let's talk about budgets. You're never going to need one again.

Wait a minute. Wasn't the point of *The Latte Factor* to track how much you're spending so you can cut back and save? And doesn't saving mean being on a budget?

No. The point of *The Latte Factor* was to demonstrate that you earn enough, right now, to start saving and investing and building future wealth. And that means throwing away your budget.

BUDGETS JUST DON'T WORK

Why do most people think they need a budget? Because that's what their parents or grandparents told them. Maybe a financial expert. But were they rich? Were they free from financial worries?

Budgets don't work because they're hard. Just like diets, budgets ask you to deprive yourself today for a reward tomorrow. We're not good at that sort of thing. It goes against human nature.

Budgets don't work because they ask you to be disciplined and be controlled. But we don't like being controlled; we want to be *in* control. And for

most of us, we're too busy to be disciplined—it takes too much time. You should never let your money control you. You should be able to do this with very little discipline and time commitment. So, for your own good, please dump those budgets in the garbage. There really is an easier way. I'm going to give you an alternative—a system that allows you to tear up your budget and never worry about it again.

EXERCISE

No More Budgeting!

Living on a budget is so ingrained that it's hard for many people to imagine not living on one. So in case you're having a rough time with the idea, we're going to map out, in black and white, just how good you are (or aren't) at staying within your budget and saving money. Trust me, this will be an eye-opener.

How to use it: At the top, write down the month you're using as an example (ideally, last month). In the first column, you'll find boxes listing typical monthly expenses, with a Miscellaneous box for others I didn't think of. In column two, write down what you budgeted for each expense last month. If you're not sure, take your best guess. In column three, write down what you actually spent last month for each expense. And in the last column, write down how much you were under or over budget for each.

Once that's done, add the totals for columns two and three. If two's total is higher than three's, congratulations. You lived within your budget, something most people don't do. If column three is higher than column two, you're over budget. Below that, write down how much you were over or under budget for all expenses for the month. Then look at the same month and write down how much you were able to save in a retirement account. Did you save anything?

If you want a broader picture, I suggest you do this exercise for two or three months. I'll bet you start to see a pattern. When you're finished, go to the last box and write down any reasons you can think of why you should continue budgeting. Are there any that make sense for you?

NO MORE BUDGETING!			
Month _____			
I. Expenses	2. What You Budgeted Last Month	3. What You Spent Last Month	4. How Much Over or Under Budget
<i>Example: Food</i>	\$300	\$450	\$150 over
Food			
Utilities			
Clothing			
Entertainment			
Car			
Misc.			
Total:	\$ _____	\$ _____	\$ _____
Amount Over/Under Budget for the Month: \$ _____			
Amount Saved Toward Retirement Last Month: \$ _____			
<p>List 3 reasons you should continue budgeting (if you can):</p> <p>1.</p> <p>2.</p> <p>3.</p>			

When you've finished the exercise: You may feel like tossing your latest budget into the garbage can. Good! Do it! Budgets are the last thing you need if you're going to become an Automatic Millionaire. What you need is what I'm going to share with you next.

IF THIS WERE THE ONLY THING YOU DID, YOU'D BE RICH

If you want to be rich, all you have to do is make the decision to do something most people don't do:

Pay Yourself First.

What does that mean? When most people bring home their paycheck, the first thing they do is pay everyone else: the landlord, the credit card company, the government. If there's anything "left over" at the end, they pay themselves by saving.

That is completely, positively, financially *backward*. If you pay everyone else first, you will *never* get rich. Think about it this way: There are six primary ways to get rich in this country:

1. Win it.
2. Marry it.
3. Inherit it.
4. Sue for it.
5. Budget for it.
6. **Pay Yourself First.**

EXERCISE
The “What Are the Odds” Get-Rich Lottery

Let’s have a little fun with the great American get-rich-quick schemes. I’m always amazed at how many people believe that getting rich “just happens” somehow. It doesn’t. But you can plan to get rich by becoming an Automatic Millionaire. To see how silly, petty, or downright ridiculous the other methods really are, and how Paying Yourself First is the only true, dependable way to build genuine long-term wealth, try this exercise.

How to use it: Just read the six scenarios for getting rich and what you’d have to do to make each one happen. Then rate your odds, from “Dream On,” or no chance in this life, to “Certain,” which means you can practically guarantee success. At the bottom, write down the method that gives you the best odds of building real wealth.

THE "WHAT ARE THE ODDS" GET-RICH LOTTERY		
The Method	What You'd Need to Do	Your Chances of Success
Win It	Have the one winning lottery ticket out of 20 or 30 million sold each month.	Dream On Certain
Marry It	Find someone wealthy who's not married and whom you could live with for 30–40 years.	Dream On Certain
Inherit It	Be lucky enough to have a rich relative and mean enough to wait around for them to die.	Dream On Certain
Sue for It	Spend years in court with no guarantees, only to pay 40% to your lawyer.	Dream On Certain
Budget for It	Brown-bag it, watch every penny, and never have a major emergency expense.	Dream On Certain
Pay Yourself First	Put 10% of every pay-check into a retirement account.	Dream On Certain
<p>Which method for getting rich makes the most sense for you?</p>		

When you've finished the exercise: Now you have some valuable perspective on the sillier ideas people have about hitting pay dirt. For instance, did you know that you literally have a better chance of being hit by lightning than of winning most state lotteries? But the odds of getting rich by Paying Yourself First are excellent . . . if you take action today!

BRAINSTORMING BREAK

What plans have you had for getting rich?

WHAT DOES “PAY YOURSELF FIRST” MEAN?

So it's clear that Pay Yourself First is the one get-rich plan that actually makes sense. But what does it mean? Look at it this way: When you earn a dollar, before that money even gets into your paycheck, Uncle Sam gets his cut for federal income tax. Then the state takes its five cents. On top of that, you have Social Security taxes, Medicaid, and unemployment taxes. That's 35 to 40 cents out of your hard-earned dollar.

It wasn't always this way. Before 1943, people took home everything they earned and the government came calling for taxes in spring. But people often didn't save enough money to pay their taxes. The government's solution to this problem was brilliant: The IRS *automated the process*, taking the money out of people's paychecks before the checks even reached the workers. The government set up a system to Pay Itself First.

That's *exactly* what you're going to do. You're going to set up a system that ensures that you get paid automatically—even before the IRS does. How sweet is that?

AN AUTOMATIC MILLIONAIRE SUCCESS STORY

Since reading *The Automatic Millionaire*, I have increased my 401(k) to 10% and I'm working on writing down everything I spend. I was also able to start putting \$25 a week into an automatic savings account. The next step is to set up a biweekly mortgage payment plan. I'm now paying myself first because if I can pay the government, I can pay myself. Thanks for the inspiration.

Joyce Franklin
Lynchburg, VA

WHOM ARE YOU REALLY WORKING FOR?

Driving down the freeway not long ago, I saw a billboard that read, “Who you work for is waiting for you at home.” First it made me laugh, then it made me think.

Our employers want us to think we're working for them. The government wants us to think we're working for a healthy economy. But we're really working for ourselves. The reason you go to work is to provide for and protect yourself and those you love. *You* are your first priority.

But if that's true, why aren't more people creating financial plans centered on themselves? Before you start laying out a financial plan, you've got to ask a crucial question: "Am I really working for myself?"

EXERCISE

How Many Hours Did You Work for Yourself?

This exercise will give you more perspective on your working life than any other. You'll understand, maybe for the first time, how much of your workday you've devoted to your own needs . . . and you'll be determined to spend more of your work time working for yourself.

How to use it: Fill in each box and do the math.

HOW MANY HOURS DID YOU WORK FOR YOURSELF?
<p>a. Last week, I worked a total of _____ hours.</p> <p>b. I earn \$_____ an hour before taxes.</p> <p>c. Last week, I put aside \$_____ for my retirement.</p> <p>d. So last week, I worked _____ hours for myself ($c \div b$).</p>

When you've finished the exercise: Now you know what you're doing today. Tomorrow, you can start working *more* for yourself.

IT'S ABOUT HOW MUCH MONEY YOU SAVE

Working for yourself is about saving money toward your future. How much should you be working for yourself? Let's consider someone who earns \$50,000 a year before taxes:

- That person earns roughly \$1,000 a week (with two weeks off for vacation)
- That's roughly \$25 an hour for a 40-hour week

A good benchmark for retirement savings is between 10% and 15% of your income. Let's split the difference and say 12.5%. Now, 12.5% of \$1,000 is \$125. So if you're earning \$1,000 a week, you should be saving \$125 a week, or \$25 a day. In other words, you should be working at least one hour per day for yourself.

Unfortunately, most people don't. According to the U.S. Department of Commerce, the average American works barely 22 minutes a day for himself, and saves below 5% of what he earns. One out of five workers saves nothing.

AN AUTOMATIC MILLIONAIRE SUCCESS STORY

We're feeling great today after reading *The Automatic Millionaire*. Despite having three special-needs kids and the mounting bills that accompany them, we started the automatic deduction process 10 years ago with my husband's 401(k). You really do not miss what you cannot see! That automatic deduction has grown from zero to over \$126,000 even though we have had to tweak our percentage to match our financial needs. Despite dropping to 2% some years, we are back to 18%. . . . Like you said, the only true way to do this is through automation.

We live comfortably below our means, knowing our future will be set! We also make one extra payment a year on our mortgage. Not bad for a family beset with many challenges.

Marie Louise Kier
Chester Springs, PA

STARTING TODAY, YOU'RE WORKING FOR YOU

That's tragic. Why would you work hard for decades and NOT work at least one hour a day for yourself?

You shouldn't. An hour a day is really not a lot to ask in return for a bright future. You deserve at least that.

LET'S GET BUSY!

Here's the plan you've been waiting for. Starting today, you should:

1. Decide to Pay Yourself First.
2. Work at least one hour per day for yourself.

3. Open a retirement account if you don't already have one.
4. Fund it with 10% (an hour a day) of your gross income.
5. **Make it automatic.**

That's it. If you follow just those basic steps, you will be rich by the time you retire. I'll explain how to do each one of these things as we move through *The Automatic Millionaire Workbook*.

PAY YOURSELF BEFORE YOU PAY THE GOVERNMENT

Congratulations on deciding to Pay Yourself First at least one hour's pay per day. But don't just put that money into your savings account. The key to Paying Yourself First is to pay yourself before you pay the government, using a pretax retirement account. With a 401(k), 403(b), IRA, or SEP IRA, you can keep everything you earn without the government taxing one cent of it.

There is no catch! Starting tomorrow, you simply arrange to have 10% of your gross income automatically deducted from your paycheck and deposited in a pretax retirement account. If you did only that, you would eventually accumulate more wealth than 90% of the population.

AN AUTOMATIC MILLIONAIRE SUCCESS STORY

After reading *The Automatic Millionaire*, my first financial goal was to become debt-free within a year. So 20% of our family income went toward paying off our debt. It was limiting our available money but it was no burden to us since we had decided to simplify our lives by cutting down on shopping, doing more meaningful activities, and driving our paid-off cars longer instead of getting a newer one on consumer loan. At the same time, I unexpectedly had the opportunity to do some freelance work in addition to my regular job. Now, after only one year we paid off all of our debt (\$12,000) plus I was able to establish a 4-month financial cushion for security. Before I read your book, I would have spent the extra money pretty quickly for all kinds of reasons but I was determined that this time, I would act differently. This time I had goals. It was not as hard as I expected it to be. For the first time, our family will not have to live paycheck to paycheck. I can't wait to achieve the next goals on my list and to put more of your advice to work. Once again, thank you very much!

Brigitte Rush
Seattle, WA

WHY THIS WON'T HURT A BIT

When I tell people about the Pay Yourself First system, the first objection is “There’s no way I could save an hour’s pay every day!” That’s a perfectly normal reaction. The idea of cutting your take-home pay by, say, \$200 every two weeks, or \$14 a day, might seem scary. But as we saw when we looked at your Latte Factor, and as you’ll see in the next chapter, it’s actually easier to save that money than you might think.

As it turns out, automatically deducting \$14 a day from your pay actually reduces your *spendable* income by only \$10 a day. The next exercise will explain in detail how this is possible, but basically it works this way: When you move money from your paycheck into a pretax retirement account, you don’t pay income tax on that money. So your paycheck goes down less than your retirement account goes up.

Still unclear? This exercise should do the trick.

EXERCISE

How Little Will It Hurt Today to Save for Tomorrow?

Thanks to the wonders of tax-deferred retirement accounts that Pay You First, investing 10% of your gross income will hit you in the wallet a lot less than you think. Use this worksheet to figure out how much saving 10% will cost you in spendable income each month.

How to use it: First, take a look at the example exercise. Then go step by step and fill in each box. You may want to grab your pocket calculator to make things easier and faster.

HOW LITTLE WILL IT HURT TODAY TO SAVE FOR TOMORROW?		
Today—Example		
a.	My gross annual income	\$50,000
b.	My tax rate	25%
c.	How much I'm taxed on my salary ($a \times b$)	\$12,500
d.	What I actually take home each year ($a - c$)	\$37,500
Tomorrow—Example		
e.	10% of my gross income (my pretax savings goal)	\$5,000
f.	My gross income minus my pretax savings goal (my new taxable income) ($a - e$)	\$45,000
g.	How much tax I'll pay on my new taxable income ($f \times 25\%$)	\$11,250
h.	My new annual take-home income ($f - g$)	\$33,750
i.	How much less I'm really taking home per year ($d - h$)	\$3,750
j.	How much less per month ($i \div 12$)	\$312.50
k.	How much less per day ($j \div 30$)	\$10.42
<p>Conclusion:</p> <p>Saving \$5,000 per year for my retirement will cost me \$3,750, or \$10.42 per day.</p>		

HOW LITTLE WILL IT HURT TODAY TO SAVE FOR TOMORROW?		
Today		
a.	My gross annual income	\$ _____
b.	My tax rate	_____ %
c.	How much I'm taxed on my salary ($a \times b$)	\$ _____
d.	What I actually take home each year ($a - c$)	\$ _____
Tomorrow		
e.	10% of my gross income (my pretax savings goal)	\$ _____
f.	My gross income minus my pretax savings goal (my new taxable income) ($a - e$)	\$ _____
g.	How much tax I'll pay on my new taxable income ($f \times 25\%$)	\$ _____
h.	My new annual take-home income ($f - g$)	\$ _____
i.	How much less I'm really taking home per year ($d - h$)	\$ _____
j.	How much less per month ($i \div 12$)	\$ _____
k.	How much less per day ($j \div 30$)	\$ _____
<p>Conclusion:</p> <p>Saving \$ _____ per year for my retirement will cost me \$ _____, or \$ _____ per day.</p>		

When you've finished the exercise: What a revelation, right? Pretax accounts mean that saving will affect your take-home pay much less than you'd think. If you're making a decent average income, I'll bet you can save that 10% of your income for the cost of your Latte Factor.

THE "PAY YOURSELF FIRST" FORMULA

Now you know that you can save enough money to get rich. But how much of your income *should* you save? Ten percent? Twelve and a half percent? An hour a day? Two hours? The realistic answer is "As much as you can." Saving something, even if it's just 5%, is much, much better than saving nothing. But if you want to know how much you ought to be Paying Yourself First to achieve your financial goals, use this formula as a basic guideline. Which choice is right for you?

EXERCISE

The Pay Yourself First Formula

How to use it: Decide what your goal is for retirement, then read the choices and choose which Pay Yourself First amount fits your goal and place a check mark next to it.

THE PAY YOURSELF FIRST FORMULA		
How much of your income should you save? That depends on your goals.		Your choice
To be ...		
Rich enough to retire early	Pay Yourself First at least 20% of your gross income.	
Rich	Pay Yourself First 15% to 20% of your gross income.	
Upper middle class	Pay Yourself First 10% to 15% of your gross income.	
Middle class	Pay Yourself First 5% to 10% of your gross income.	
Poor	Think about Paying Yourself First, but don't actually do it.	
Dead broke	Don't Pay Yourself First. Spend more than you earn, borrow money you can't pay off, and live on credit cards.	

When you've finished the exercise: Now you have your Pay Yourself First goal. Next, you're going to work on reaching it!

TELL ME MORE!

In the next few chapters, you'll learn where to put your Pay Yourself First money and how to create a systematic savings plan that will never fail. But first, let's solidify what you've learned in this chapter by completing the Pay Yourself First Motivator.

KEY POINTS TO REMEMBER FROM THIS CHAPTER

- You can't get rich by budgeting.
- Paying Yourself First is the only sure way to get rich.
- You should be working at least one hour a day for yourself.
- Using pretax retirement accounts means saving 10% of your income will cost you a lot less from your take-home pay.

EXERCISE

The Pay Yourself First Motivator

How to use it: First, record the ways your eyes were opened by learning about Paying Yourself First. Next, jot down a to-do list of action steps for 24 hours and 7 days. Finally, list a few people with whom you want to share your new insights about paying yourself before creditors or Uncle Sam.

THE PAY YOURSELF FIRST MOTIVATOR	
What is your biggest breakthrough from this chapter?	
1	
2	
3	
What are the most important actions you want to take in the next 24 hours?	
1	
2	
3	
What are the most important actions you want to take in the next 7 days?	
1	
2	
3	
What from this chapter do you want to share with someone else in your life?	Why?
1	
2	
3	

When you've finished the exercise: Decide which of your action items you can tackle before tomorrow, then get going.

OK, you've made tremendous progress so far! In fact, just by getting to this point, you understand more about the mechanics of building wealth than most Americans. But now that you have the knowledge, it's time to take some action. So let's take what we know and look at how you'll turn your Latte Factor and Pay Yourself First into wealth by Making It Automatic.

NOW MAKE IT AUTOMATIC

You remember Jim and Sue McIntyre. They became Automatic Millionaires by setting up a Pay Yourself First system that automatically saved a percentage of their incomes for more than 30 years. Because their plan was automated, they never had to write checks. Implementing their plan took no time and no discipline. Once they decided how much to Pay Themselves First, the plan took care of itself.

So the most important thing you can do is to begin Paying Yourself First—RIGHT NOW. Even if you can only set aside 1% of your income, fine. Do it. Start saving. Once you do, you're on your way to becoming an Automatic Millionaire.

In this chapter, you're going to learn how to Pay Yourself First a percentage of your income . . . and you're going to be like the McIntyres and Make It Automatic. The secret is really no secret at all: It's your company retirement plan.