### Personal finance**[**[**edit**](https://en.wikipedia.org/w/index.php?title=Finance&action=edit&section=2)**]**

*Main article:*[*Personal finance*](https://en.wikipedia.org/wiki/Personal_finance)

**Personal finance**[[2]](https://en.wikipedia.org/wiki/Finance#cite_note-2) is defined as the mindful planning of monetary spending and saving, while also considering the possibility of future risk. The following steps, as outlined by the Financial Planning Standards Board[[3]](https://en.wikipedia.org/wiki/Finance#cite_note-3), suggest that an individual will understand a potentially secure personal finance plan after:

* Purchasing insurance to ensure protection against unforeseen personal events
* Understanding the effects of tax policies (tax subsidies or penalties) management of personal finances
* Understanding the effects of credit on individual financial standing
* Developing of a savings plan or financing for large purchases (auto, education, home)
* Planning a secure financial future in an environment of economic instability
* Pursuing a checking and/or a savings account
* Preparing for retirement/ long term expenses

[Une image contenant personne, homme, complet, rideau

Description générée automatiquement](https://en.wikipedia.org/wiki/File:Warren_Buffett_KU_Visit.jpg)

[Warren Buffett](https://en.wikipedia.org/wiki/Warren_Buffett) CEO & chairman of Berkshire Hathaway, American investor, business magnate, and philanthropist. He is considered by some to be one of the most successful investors in the world.

Personal finance may involve paying for education, financing [durable goods](https://en.wikipedia.org/wiki/Durable_good) such as [real estate](https://en.wikipedia.org/wiki/Real_estate) and cars, buying [insurance](https://en.wikipedia.org/wiki/Insurance), e.g. health and property insurance, investing and saving for [retirement](https://en.wikipedia.org/wiki/Retirement).

Personal finance may also involve paying for a loan, or debt obligations. The six key areas of personal financial planning, as suggested by the Financial Planning Standards Board, are:[[4]](https://en.wikipedia.org/wiki/Finance#cite_note-4)

1. **Financial position**: is concerned with understanding the personal resources available by examining net worth and household cash flows. Net worth is a person's balance sheet, calculated by adding up all assets under that person's control, minus all liabilities of the household, at one point in time. Household cash flows total up all from the expected sources of income within a year, minus all expected expenses within the same year. From this analysis, the financial planner can determine to what degree and in what time the personal goals can be accomplished. Ratios are frequently used on the corporate level to measure a company's ability to cover its cost given the assets it has on hand. This can be paralleled to an individual level as well. Maintaining a ratio of 2:1 or greater is seen as healthy in this respect.[[5]](https://en.wikipedia.org/wiki/Finance#cite_note-5) This means that for every dollar of expenses there is an existing dollar value of assets such as cash to cover that cost.
2. [**Adequate protection**](https://en.wikipedia.org/wiki/Insurance): the analysis of how to protect a household from unforeseen risks. These risks can be divided into the following: liability, property, death, disability, health and long term care. Some of these risks may be self-insurable, while most will require the purchase of an insurance contract. Determining how much insurance to get, at the most cost-effective terms requires knowledge of the market for personal insurance. Business owners, professionals, athletes, and entertainers require specialized insurance professionals to adequately protect themselves. Since insurance also enjoys some tax benefits, utilizing insurance investment products may be a critical piece of the overall investment planning.
3. [**Tax planning**](https://en.wikipedia.org/wiki/Tax_planning): typically the income tax is the single largest expense in a household. Managing taxes is not a question of if you will pay taxes, but when and how much. Governments give many incentives in the form of tax deductions and credits, which can be used to reduce the lifetime tax burden. Most modern governments use a progressive tax. Typically, as one's income grows, a higher [marginal rate of tax](https://en.wikipedia.org/wiki/Tax_rate#Marginal) must be paid. Understanding how to take advantage of the myriad tax breaks when planning one's personal finances can make a significant impact, which can save you money in the long term.
4. **Investment and accumulation goals**: planning how to accumulate enough money – for large purchases and life events – is what most people consider to be financial planning. Major reasons to accumulate assets include purchasing a house or car, starting a business, paying for education expenses, and saving for retirement. Achieving these goals requires projecting what they will cost, and when you need to withdraw funds that will be necessary to be able to achieve these goals. A major risk to the household in achieving their accumulation goal is the rate of price increases over time, or [inflation](https://en.wikipedia.org/wiki/Inflation). Using net present value calculators, the financial planner will suggest a combination of asset earmarking and regular savings to be invested in a variety of investments. In order to overcome the rate of inflation, the investment portfolio has to get a higher rate of return, which typically will subject the portfolio to a number of risks. Managing these portfolio risks is most often accomplished using asset allocation, which seeks to diversify investment risk and opportunity. This asset allocation will prescribe a percentage allocation to be invested in stocks (either preferred stock or common stock), bonds (for example mutual bonds or government bonds, or corporate bonds), cash and alternative investments. The allocation should also take into consideration the personal risk profile of every investor, since risk attitudes vary from person to person.
5. **Retirement planning** is the process of understanding how much it costs to live at retirement, and coming up with a plan to distribute assets to meet any income shortfall. Methods for retirement plans include taking advantage of government allowed structures to manage tax liability including: individual ([IRA](https://en.wikipedia.org/wiki/Individual_retirement_account)) structures, or employer sponsored [retirement plans](https://en.wikipedia.org/wiki/Retirement_plans), annuities and life insurance products. Oftentimes this field of personal finance is overlooked as many individuals see this being something in their distant future. However, the sooner you start [investing](https://en.wikipedia.org/wiki/Investing) the greater likelihood you have for actually being prepared. Accrual compounding from the prime "work years" can create a significant impact down the road as these earlier donation years will have more time to compound on themselves giving the individual more wiggle room in their future for unexpected unforeseen events. With every additional year of missed contributions, this creates more tension on the individual to contribute a greater sum leading up to the maturity date of what they may have always thought would be their [retirement](https://en.wikipedia.org/wiki/Retirement) age. In the same respect an individual who is able to attain a healthy amount of wealth at a young age may then be able to invest it into a [mutual fund](https://en.wikipedia.org/wiki/Mutual_fund) or [stocks](https://en.wikipedia.org/wiki/Stock) accordingly depending on how much they believe they will need to maintain their [standard of living](https://en.wikipedia.org/wiki/Standard_of_living) once retirement arrives. Allocating a portfolio according to your goals is crucial and also needs to be continuously adjusted as your personal needs and desires change. Oftentimes, individuals will allocate 80% of their earnings into stocks while there is still room for error (more time away from retirement) with only 20% being distributed to mutual funds as these are considered more 'steady' streams of investment. As an individual begins to get closer to their retirement, oftentimes they will gradually adjust these allocations to have a greater percentage in their mutual fund section to solidify their gains and only leave 20% to still generate higher returns. This allocation is commonly recommended by financial planners as it allows the individual to build capital in their work years and keep their gains safe in the long run, leaving less room for volatility.[[6]](https://en.wikipedia.org/wiki/Finance#cite_note-6)
6. [**Estate planning**](https://en.wikipedia.org/wiki/Estate_planning) involves planning for the disposition of one's assets after death. Typically, there is a tax due to the state or federal government at one's death. Avoiding these taxes means that more of one's assets will be distributed to one's heirs. One can leave one's assets to family, friends or charitable groups.