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ABSTRACT

This guide is designed to help people of all ages set up a budget and manage their money. It is organized in three sections: the Principles of Managing Your Finances, Financial Tools Used in Money Management, and Coping with Change. Section 1 consists of three chapters. The first chapter introduces the money management process, discusses goal setting, and provides tools to evaluate one's current situation and net worth. Chapter 2 takes the reader through the budgeting process and provides tips on recordkeeping and finding sources of advice. The third chapter suggests ways to economize, weighing the pros and cons of buying versus renting housing, determining food expenditures, saving on clothing, and minimizing use of utilities. It ends with a discussion of the costs of having, raising, and educating children. Section 2 has chapters on sewing and investing, insurance, and consumer credit. Section 3 explains retirement planning; and economic, financial, and household change. Each chapter includes approximately 25 references. Worksheets are provided for net worth, setting goals, estimating income, estimating expenses, monthly expense record, household expenses, retirement income, and retirement expenses. (KC)

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MANAGING YOUR PERSONAL FINANCES

Home and Garden Bulletin No. HG-245

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Managing Your Personal Finances

The Principles of Managing Your Finances

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Preface

Managing Your Personal Finances is a budgeting guide. It is divided into three sections which are available individually or as a set. The total guide is designed to help you develop money management skills. It will teach you how to set goals, how to make a budget for your circumstances, and how to plan for the future. The guide contains information on saving and investing, using insurance and credit, and planning for retirement; and suggests where to go for additional help. Specific information is included on:

- Developing a budget.
- Using financial tools to carry out your budget.
- Recognizing financial and economic conditions that affect your budget.

Section 1: **The Principles of Managing Your Finances**
HG-245-1

Section 2: **Financial Tools Used in Money Management**
HG-245-2

Section 3: **Coping With Change**
HG-245-3

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Introduction

How well are you using resources to manage your finances in today's changing economic environment? Resources available include money, time, energy, skills, talents, and knowledge. Good management habits can help you direct and control these resources so you can have the things you want and need. As a manager, you often substitute one resource for another. To conserve money, it is often necessary to substitute time, energy, or talents. For example, you may be able to save money by using *time* to prepare meals at home instead of eating out. If you can garden or make automotive repairs, you may be able to save money by performing these *skills*. By managing all available resources you can maintain the kind of lifestyle that you want even during periods of financial stress.

Effective management of money is a lifelong process. Whether you are a single person, a single parent, a newlywed, a childless couple, a couple with children, or a retiree, you can still benefit from developing good money management habits.

Good management of time, money, and other resources can help you to:

- Increase household income while decreasing outgo.
- Achieve your goals and those of other household members.
- Protect household members and possessions.

Chapter 1

1.1 Planning To Manage Your Money

Perhaps you have dreamed of suddenly receiving enough money to pay off all your bills and become financially secure for life. Even if your dream came true, you probably would find that simply having a lot of money does not end financial worries. Money problems are not restricted to low- and moderate-income households. When more money is available, there are more alternatives to consider. Many people find that they can control most financial problems by planning how to manage current income and how to set goals for the future. This could work for you, too.

The Management Process

The management process is a way to reach a particular end, objective, or goal. The *basic steps* include:

- Setting goals or objectives.
- Initiating activities to accomplish these goals.
- Evaluating and adjusting the activities.
- Repeating the process until the goals are met.

A plan for money management is important for everyone. However, no readymade plan fits every family, couple, or individual. Every household is different—not only in the number and characteristics of its members, but also in its values, needs, wants, and resources. Only you can decide how your money should be spent, taking into consideration your income, the number and ages of your household members, where you live and work, your preferences, your responsibilities, and your goals for the future. By following a money management plan, you can be confident that expenses will be met and savings will be available. A plan can let you know where you stand financially and prevent emergencies from causing a financial strain.

Remember three basic concepts when developing a personal money management plan:

- *Set realistic objectives.* Objectives set too high may lead to frustrations that could cause you to abandon your plan.
- *Be flexible.* Your plan will require adjustments to keep up with your changing life cycle and financial situation. Do not make a plan so tight that each new development re-

quires an entirely new plan.

☐ *Be specific.* State your objectives concisely. If goals are vague, objectives may never be met and you and other household members may have different ideas of what the end product will be.

Evaluating Your Current Situation With a Net Worth Statement

The first step in developing a money management plan is to evaluate your current situation. An excellent way to do this is to prepare a *net worth statement.* Worksheet 1 on page 1.25 can be used to add together your assets (what you own) and subtract from that the sum of your liabilities (what you owe). Space is provided for you to calculate your net worth statement now and again 1 year from now.

To determine the value of your *assets*, start with cash available. Include your checking and saving accounts, as well as your home bank. Now list all your investments, including bonds, mutual funds, life insurance cash values, and others. List additional assets, using the current market value for your house, real estate, automobiles, jewelry, antiques, and other personal items.

To determine your *liabilities*, list the amount that you owe to all your creditors and lenders. Remember to include current bills, charge accounts, mortgage balance, and loans against your life insurance.

By subtracting liabilities from assets, you can determine your *net worth.* Look closely at your final net worth figure. Do you own more than you owe? Consider what you would like this figure to be a year from now. What do you need to do to achieve that goal?

Prepare a new net worth statement at the same time each year to reflect the changes in your finances. The market value of your assets (house, stock, or cars) may have declined or risen. You may have paid off one loan or gained another. A new net worth statement next year will help you decide if the money management plan you are developing now has helped put you ahead.

Planning To Reach Your Goals

An important step in developing a money management plan is to set household and individual goals. Goals are wants, needs, and future objectives for your household and its members. Goals may be long-term, intermediate, or immediate.

Long-term goals are those you hope to reach in 10 to 20 years or perhaps even longer. Long-term goals are often considered first so they can be incorporated into the plan from the start. They are guided by expected changes in your household's life cycle and must sometimes be adjusted for future expected income and price changes. Long-term goals include such things as paying off a mortgage, putting children through college, or providing for a comfortable retirement.

Intermediate goals are those to be reached within the next 5 years or so. These goals may reflect the changes that will occur due to your increased income or larger family. Intermediate goals might include such things as a downpayment on a house, a new car, or increased life insurance.

Immediate goals are required now - this week, this month, or this year. These are basic needs that must be met even at the expense of some future goals. Immediate goals may include paying current bills, maintaining health insurance, and buying food and clothing.

Addressing goals in this order ensures savings for long-term and intermediate goals and prevents immediate goals from pushing future ones aside. If your income is low, you may be able to meet only immediate goals. But you still should make intermediate and long-term plans which could help you to get ahead in the future.

1.3

Decide Which Goals Are Most Important to You

Think carefully about your financial goals. Many of us would like to be financially secure, own a large home, drive a fancy car, educate ourselves or our children, take long vacations, and so on. Realistically, however, most of us cannot have it all. We must select and work toward those goals that are most important to us and the ones which we will be able to obtain. The following process may help you work through your goal-selection decisions.

Set goals. Keep a listing of the goals that you and your family hope to achieve. Use worksheet 2 on page 1.26.

Rank goals. List your goals in their order of importance to you and your household.

Assign dollar values to goals. You will not be able to assign a dollar value to all goals now, but to most you will. For example, if you plan to buy a new car next year and you know the amount of the downpayment, put this on your worksheet.

Reevaluate your goals. After developing your budget in Chapter 2, take another look at worksheet 2. You may need to drop, postpone, or revise some of your goals. Decide how much change you are willing and able to make. For example, are you willing to change jobs or give up other goals in order to achieve a goal that is more important to you? Think about the tradeoffs of saving for long-term and intermediate goals versus using income for current expenses. How much choice do you have? Can you, and do you want to, cut down on some immediate goals (current expenses) to improve your chances of meeting your long-term goals? Refer to your goals often as you plan.

Common Goals Throughout the Life Cycle

Some goals are universal to all households - such as providing for sufficient food, comfortable shelter, and financial security. But most goals change as household members progress through the life cycle. When you are young and single, goals generally relate to your own personal development. When you are married and have children, your first priorities may switch from yourself to your children—establishing an educational fund, for example. Different types of households use different ways to meet the same goal. For example, a retired couple may provide for their continued financial security during times of high inflation by cutting expenses. A young couple may seek higher paying employment instead.

Look over the following description of household types and determine which group your household resembles. Do you have goals similar to the ones stated for your group? Look at the goals for the other groups. They may help you anticipate future needs. This listing is not meant to be all-inclusive. However, it can be a starting point in determining your current and long-term goals and how those goals may change in years to come.

Household Type 1: Singles. This household type consists of adults who have never married, or who are widowed or divorced. It includes persons from age 18 to 54 who are considered to be self-supporting, even though they may be living with relatives or friends and sharing some household expenses. Income for this group may not be high, particularly for the younger members. Important goals involve their personal, educational, and financial development.

Household Type 2: Single Parents. Members of this household group may also have never married or are widowed or divorced. Unlike Type 1 households, they are parents living with dependent children. The critical financial goals for single parents often relate to the care of their children and themselves.

Household Type 3: Young Couples. This household type is often called the beginning family or the beginning marriage stage. It is a period of personal and financial adjustment for two persons. Ages of couples in this group typically range from about 18 to 34. There are no children and there are often two incomes. Important goals involve setting up a household and adjusting to each other's needs.

Household Type 4: Young Families. In this growing-family stage, parents are typically young—age 18 to 34—and have dependent children in the household. There may be two incomes. Critical goals include protecting the family income and rearing the children.

Household Type 5: Middle Families. This household type is sometimes referred to as the contracting family. Parents are typically 35 to 54 years old. Children are "leaving the nest" for college, careers, and marriage. Unique goals for this household include providing for the children's college or vocational education, weddings, and the parents' eventual retirement.

Household Type 6: Middle Couples. This group consists of persons age 35 to 54 without children. This type of household often contains two earners. Income is often quite high, making investment maximization and tax minimization important financial goals.

Household Type 7: Older Singles. This group contains persons age 55 and older who may be retired. There is no spouse present in the household. The majority of older singles are females. The major financial goal is to provide adequate income and reserves that will last for the balance of the older single's lifetime.

Household Type 8: Older Couples. This group consists of married couples ages 55 and over who also may be retired. Their major financial goal is maintenance of an adequate level of living for both persons for life.

Chapter 2

[illegible] Your Goals Through Budgeting

Do you often find yourself unable to make one paycheck last until the next arrives? Do you meet current expenses but have little or nothing left to save for the future? If so, you are a prime candidate for developing a budget. You may have these problems whether you earn $50,000 a year or $10,000 a year. Even if you rarely face these situations, a budget can probably help you achieve more of your goals.

The Budgeting Process

A budget is a plan for spending and saving. It requires you to estimate your available income for a particular period of time and decide how to allocate this income toward your expenses. A working budget can help you implement your money management plan. A well-planned budget does several things for you and your household. It can help you:

- Prevent impulse spending.
- Decide what you can or cannot afford
- Know where your money goes.
- Increase savings.
- Decide how to protect against the financial consequences of unemployment, accidents, sickness, aging, and death.

A working budget need not be complicated or rigid. However, preparing one takes planning, and following one takes determination. You must do several things to budget successfully.

First, communicate with other members of your household, including older children. Consider each person's needs and wants so that all family members feel they are a part of the plan. Everyone may work harder to make the budget a success and be less inclined to overspend if they realize the consequences. When families fail to communicate about money matters, it is unlikely that a budget will reflect a workable plan.

Second, be prepared to compromise. This is often difficult. Newlyweds, especially, may have problems. Each may have been living on an individual income and not be accustomed to sharing, or may have been in school and dependent on parents. If, for example, one wants to save for things and the other prefers buying on credit, they will need to discuss the pros and cons of both methods and decide on a middle ground each can accept. A plan cannot succeed unless there is a financial partnership.

Third, exercise willpower. Try not to indulge in unnecessary spending. Once your budget plan is made, opportunities to overspend will occur daily. Each household member needs to encourage the others to stick to the plan.

Fourth, develop a good recordkeeping system. At first, all members of the household may need to keep records of what they spend. This will show how well they are following the plan and will allow intermediate adjustments in the level of spending. Recordkeeping is especially important during the first year of a spending plan when you are trying to find a budget that works best for you. Remember, a good budget is flexible, requires little clerical time, and most importantly, works for you.

Choosing a Budget Period

A budget may cover any convenient period of time—a month, 3 months, or a year, for example. Make sure the period you use is long enough to cover the bulk of household expenses and income. Remember, not all bills come due monthly and every household experiences some seasonal expenses. Most personal budgets are for 12 months. You can begin the 12-month period at any time during the year. If this is your first budget, you may want to set up a trial plan for a shorter time to see how it works.

After setting up your plan, subdivide it into more manageable operating periods. For a yearly budget, divide income and expenses by 12, 24, 26, or 52, depending on your pay schedule or when your bills come due. Most paychecks are received weekly or every 2 weeks. Although most bills come due once a month, not all are due at the same time in the month. Try using each paycheck to pay your daily expenses and expenses that will be due within the next week or two. This way you will be able to pay your bills on time. You may also want to allocate something from each paycheck toward large expenses that will be coming due soon.

Developing a Successful Budget

Step 1: Estimate Your Income

Total the money you expect to receive during the budget period. Use worksheet 3 on page 1.27 as a guide in estimating your household income. Total all money you will receive. Begin with regular income that you and your family receive—wages, salaries, income earned from a farm or other business, Social Security benefits, pension payments, alimony, child support, veterans' benefits, public assistance payments, unemployment compensation, allowances, and any other income. Include variable income, such as interest from bank accounts and investments, dividends from stock and insurance, rents from property you own, gifts, and money from any other sources.

If your earnings are irregular, it may be more difficult to estimate your income. It is better to underestimate than overestimate income when setting up a budget. Some households have sufficient income, but its receipt does not coincide with the arrival of bills. For these households, planning is very important.

Step 2: Estimate Your Expenses

After you have determined how much your income will be for the planning period, estimate your expenses. You may want to group expenses into one of three categories: fixed, flexible, or set-asides. *Fixed* expenses are payments that are basically the same amounts each month. Fixed *regular* expenses include such items as rent or mortgage payments, taxes, and credit installment payments. Fixed *irregular* expenses are large payments due once or twice a year, such as insurance premiums. *Flexible* expenses may vary from one month to the next, such as amounts spent on food, clothing, utilities, and transportation. *Set-asides* are variable amounts of money accumulated for special purposes, as for seasonal expenses, savings and emergency funds, and intermediate and long-term goals.

Use old records, receipts, bills, and cancelled checks to estimate future expenses, if you are satisfied with what your dollars have done for you and your family in the past. If you are not satisfied, now is the time for change. Consider which expenses can be cut back and which expenses need to be increased. If you spent a large amount on entertainment, for example, your new budget may reallocate some of this money to a savings account to contribute to some of your future goals.

If you do not have past records of spending, or if this is your first budget, the most accurate way to find out how much you will need to allow for each expense is to keep a record of your household spending. Carry a pocket notebook in which you jot down expenditures during a week or pay period and total the amounts at the end of each week. You may prefer to keep an account book in a convenient place at home and make entries in it. Kept faithfully for a month or two, the record can help you find out what you spend for categories such as food, housing, utilities, household operation, clothing, transportation, entertainment, and personal items. Use this record to estimate expenses in your plan for future spending. You also need to plan for new situations and changing conditions that increase or decrease expenses. For example, the cost of your utilities may go up.

Total your expenses for a year and divide to determine the amounts that you will have to allocate toward each expense during the budgeting period. Record your estimate for each budgetary expense in the space provided on worksheet 4, "Expense Estimate and Budget Balancing Sheet" (pages 1.29-1.39). Begin with the regular fixed expenses that you expect to have. Next, enter those fixed expenses that come due once or twice a year. Many households allocate a definite amount each budget period toward these expenses to spread out the cost.

One way to meet major expenses is to set aside money regularly before you start to spend. Keep your set-aside funds separate from other funds so you will not be tempted to spend them impulsively. If possible, put them in an account where they will earn interest. You may also plan at this point to set aside a certain amount toward the long-term and intermediate goals you listed on worksheet 2. Saving could be almost as enjoyable as spending, once you accept the idea that saving money is not punishment, but a systematic way of reaching your goals. You do without some things now in anticipation of buying what will give you greater satisfaction later.

You may want to clear up debts now by doubling up on your installment payments or putting aside an extra amount in your savings fund to be used for this purpose. Also, when you start to budget, consider designating a small amount of money for emergencies. Extras always come up at the most inopportune times. Every household experiences occasional minor crises too small to be covered by insurance but too large to be absorbed into the day-to-day budget. Examples may be a blown-out tire or an appliance that needs replacing. Decide how large a cushion you want for meeting emergencies. As your fund reaches the figure you have allowed for emergencies, you can start saving for something else. Now, record money allocated for occasional major expenses, future goals, savings, emergencies, and any other set-asides in the space provided for them on worksheet 4.

After you have entered your fixed expenses and your set-asides, you are ready to consider your flexible expenses. Consider including here a personal allowance or "mad money" for each member of the household. A little spending money that does not have to be accounted for gives everyone a sense of freedom and takes some of the tedium out of budgeting.

Step 3: Balance

Now you are ready for the balancing act. Compare your total expected income with the total of your planned expenses for the budget period. If your planned budget equals your estimated future income, are you satisfied with this outcome? Have you left enough leeway for emergencies and errors? If your expenses add up to *more* than your income, look again at all parts of the plan. Where can you cut down? Where are you overspending? You may have to decide which things are most important to you and which ones can wait. You may be able to do some trimming on your flexible expenses.

Once you have cut back your flexible expenses, scan your fixed expenses. Maybe you can make some sizable reductions here, too. Rent is a big item in a budget. Some households may want to consider moving to a lower priced apartment or making different living arrangements. Others turn in a too-expensive car and seek less expensive transportation. Look back at worksheet 2, "Projecting Goals." You may need to reallocate some of this income to meet current expenses. Perhaps you may have to consider saving for some of your goals at a later date.

If you have cut back as much as you think you can or are willing to do and your plan still calls for more than you make, consider ways to increase your income. You may want to look for a better paying job, or a part time second job may be the answer. If only one spouse is employed, consider becoming a dual-earner family. The children may be able to earn their school lunch and extra spending money by doing odd jobs in your neighborhood, such as cutting grass or babysitting. Older children can work part-time on weekends to help out. Another possibility, especially for short-term problems, is to draw on savings. These are decisions each individual household has to make.

If your income exceeds your estimate of expenses—good! You may decide to satisfy more of your immediate wants or to increase the amount your family is setting aside for future goals.

Carrying Out Your Budget

After your plan is completed, put it to work. This is when your determination must really come into play. Can you and your family resist impulse spending?

Become a Good Consumer

A vital part of carrying out the budget is being a good consumer. Learn to get the most for your money, to recognize quality, avoid waste, and to realize time costs as well as money costs in making consumer decisions.

Keep Accurate Records

Accurate financial records are necessary to keep track of your household's actual money inflow and outgo. A successful system requires cooperation from everyone in the household. Receipts can be kept and entered at the end of each budget period in a

"Monthly Expense Record" like the one on pages 1.40-1.41 (worksheet 5). It is sometimes a good idea to write on the back of each receipt what the purchase was for, who made it, and the date. Decide which family member will be responsible for paying bills or making purchases and decide who will keep the record system up to date.

The household business recordkeeping system does not need to be complex. The simpler it is, the more likely it will be kept current. Store your records in one place—a set of folders in a file drawer or other fire-resistant box is a good place. You can assemble a folder for each of several categories, including budget, food, clothing, housing, insurance, investments, taxes, health, transportation, and credit. Use these folders for filing insurance policies, receipts, warranties, cancelled checks, bank statements, purchase contracts, and other important papers. Many households also rent a safe deposit box at their bank for storing deeds, stock certificates, and other valuable items.

Evaluating Your Budget

The information on worksheet 4 can help you determine whether your actual spending follows your plan. If your first plan did not work in all respects, do not be discouraged. A budget is not something you make once and never touch again. Keep revising until results satisfy you.

Where To Go for Help

Management of your personal finances is a lifelong project. The information contained here is not all that you need to know about money management, but it can provide a starting place.

An important step in personal financial planning is deciding which money management tasks you can perform for yourself and which will require some assistance. There are certain aspects of the financial plan that all households can do:

- Setting and evaluating personal goals.
- Determining household income and basic expenses.
- Allocating income to meet expenses promptly.
- Becoming a knowledgeable consumer.
- Managing day-to-day financial records.

However, if you need help with other aspects of your plan, many sources are available.

Publications on money management are available at libraries and bookstores and from private companies and organizations, the Cooperative Extension Service, and local, State, and Federal governments. When using consumer materials from private organizations, realize that although they may provide excellent information, some are not always objective.

Computers can also help you develop your personal financial plan. The increased availability and decreased cost of computers, peripherals (added hardware), and software have made computerized financial management at home a reality. Programs can be purchased to assist in budgeting, recordkeeping, and income tax preparation. More sophisticated software is available that will print checks, balance checkbooks, and track the performance of investments. If owning a home computer is not practical or affordable for your household, you still may be able to have a computerized analysis of your finances, since many local colleges, community governments, libraries, and Cooperative Extension Services sometimes provide computerized financial planning for little or no fee.

Financial planners help you develop a total financial plan for your household. These professionals vary in their educational and occupational backgrounds and in the kind of assistance that they provide. Some have earned the title of Certified Financial Planner (CFP) from one of several colleges that offer financial planning programs; some are appointed financial consultants by the companies for which they work, such as financial planning companies, brokerage firms, banks, insurance companies, or department stores.

Professional financial planning usually requires that you provide the planner with specific information concerning your goals, income, expenses, spending habits, and problems. In return, you receive specific recommendations on how to achieve your goals and correct financial problems, as well as suggestions on tax, insurance, investment, retirement, and estate planning alternatives. Fees are charged on an hourly basis, at a flat rate, or on a scale according to your assets. Following through on the recommendations of a financial planner could also cost you brokerage, insurance, and attorney's fees.

Brokers are agents licensed to buy and sell certain products or services for a commission. Stock brokers help you handle your investments, real estate brokers help you buy and sell property, and insurance brokers help you select insurance plans. A brokerage license often indicates that the person holding the license has more experience or more training than other agents in the field.

Insurance agents sell life, property, automotive or health insurance, and may work for one particular company or as an independent agent (who can submit application for coverage to any one of several companies). Insurance agents, like brokers, work on commission.

Bankers can also be helpful to you in carrying out your financial plan. Become familiar with the manager, tellers, and other personnel at your local branch. Being recognized as a steady customer may be beneficial should you go to them for a loan. You may also want to consult bank personnel when selecting saving and investment options.

Income tax preparer. If your income tax return is complicated, you may need the assistance of an accountant or other professional income tax preparer.

Lawyers can advise you on a variety of legal matters. The legal system is complicated and varies from State to State. If you are planning to write a will, set up an estate, purchase a house, or sign a complicated contract, it is a good idea to consult with an attorney. If you do not know a lawyer, you can often get referrals through your union, credit union, or local legal clinic.

Chapter 3

Economizing In Your Budget

An effective money manager knows how each expense in the budget affects the overall spending plan. Knowing when and how to economize on parts of the budget is important. This chapter will take a closer look at housing, food, clothing, and transportation expenses, as well as the expenses associated with raising children.

Housing

For most households, housing costs make up the largest part of the budget. Whether you rent or buy, or even if your house is paid for, a substantial monthly cash allowance is required for housing. The housing section of the budget includes rent or mortgage payments, utilities, taxes, insurance, repairs, maintenance, improvements, furnishings, and decorating costs.

Determine Your Housing Needs

The amount a family or individual will spend on housing and the kind of housing chosen depends on:

- The household income.
- The size of the household.
- The permanence of household members' jobs.
- The location preferred.
- The family's values and attitudes.
- The extent of nonhousing needs and obligations.
- The stage in the life cycle.

Deciding whether to rent or buy housing is sometimes a difficult decision. The initial cost of purchasing is high, but the cost of renting has also increased. There are also choices to consider in the kind of housing to select: single-family houses, townhouses, duplexes, 112

triplexes, quadplexes, apartments, and mobile homes are all available for renting and buying. The housing decision is not made often, and it will affect everyone in the household, so consider all the alternatives carefully.

Should You Rent?

Renting is often suitable for couples or single persons just starting out, families with low incomes or few assets, retirees trying to cut down on expenses, people with jobs that are unsteady or require frequent moving, or anyone not wanting ownership responsibilities. Renting has several advantages over owning:

- Since there is no large downpayment or capital debt, renting is often less expensive.
- Since renting is more flexible, your family has more freedom to move.
- Since the landlord is responsible for upkeep, rental property should cost you no major repair expenses.
- Since no equity is gained in rental property, a reversal in your financial position will not endanger your investment.

Of course, renting also has disadvantages. As a tenant you:

- Have little or no freedom to improve the property.
- Build no equity.
- Cannot prevent the landlord from raising the rent or forcing you to move once your lease expires.

Price, size, and location are important factors to consider when selecting a rental unit. Units may be modest or expensive, but all usually require initial costs in addition to the first month's rent. Be prepared to make a security deposit and perhaps pay a month's rent ahead as well.

A rental lease involves a financial commitment that usually lasts a year. Before signing, find out if there are expenses not covered by the rent, what the tenants' and the landlord's rights and responsibilities are, what specific rules and regulations tenants must follow, and what kinds of changes tenants are allowed to make on the property. Look over your rental unit carefully for needed repairs before moving in. Consider making a list of all defects and sending a copy to your landlord. This may prevent a deduction from your security deposit when you move out.

Should You Buy?

If you are part of a large family requiring a lot of space, a young family with plans for more children, or anyone wanting to establish ownership—and if you can afford the downpayment, closing costs, and mortgage payments—then you are a prime candidate for homeownership. The decision to purchase must be carefully considered, since this is probably the largest single expenditure that you will make. Before deciding to buy, however, you should analyze future needs, desires, and financial prospects. A large mortgage debt with high monthly payments can become a major hardship to a household experiencing prolonged unemployment, illness, disability, or decreased income. Of course, owning a home has certain advantages:

- Historically, homeownership has been one of the best and safest forms of investment.
- Homeownership has provided protection against inflation, building a sizable equity over the years.
- Homeowners are able to take advantage of income tax deductions for mortgage interest

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and property taxes.
- Homeownership can give the family a feeling of permanence and pride.

Buying also has some disadvantages:
- Purchasing requires a large initial output of funds—more than some people are able to afford.
- The equity in the property is not readily available.
- High interest rates can make monthly payments very high.

If you have decided to purchase a home, you will need to determine how much you can afford to spend. This depends on your current net income, your current nonhousing expenses, and the amount of savings you have available for a downpayment. Total your monthly expenses leaving out all housing-related costs, such as rent and utilities. Subtract this sum from your total monthly net income. The difference between the two is the amount that you have available for housing each budget period. Is this amount enough to allow you new housing? Estimate what your housing expenses would be after purchasing. Add together monthly mortgage payments, condo fees, property taxes and insurance, utilities, and decorating and maintenance costs on the new property. Say, for example, after other expenses you are left with $750 for housing and the home that you want to buy requires $550 in mortgage payments. Is $200 enough to pay your other housing-related expenses—such as taxes, insurance, and utilities—each month? Also take into consideration the cost of moving into a new home. You may have to budget for things like decorating, new furnishings, remodeling, cleaning, and yard equipment.

After determining that you have enough income to purchase a home, the next step is to decide whether now is a good time to purchase. Consider these factors:
- Is your income and family life stable?
- Is your credit record good?
- Is financing available?
- Are current interest rates acceptable?
- Are the housing and real estate markets stable?

If you answered yes to most of these questions, you may be ready to begin the search for your new home. To find the right house, or apartment, consult friends and neighbors, look at newspaper ads, or tour residential areas that appeal to you. You may need a real estate agent to assist you in your search. When deciding on a neighborhood, consider its proximity to schools, recreation and medical facilities, churches and synagogues, public transportation, and stores.

Keep a written record of the properties you inspect to help remember such things as the property's location, asking price, owner's name, number of rooms, utility costs, and special features. Do not hesitate to carefully inspect the property several times before making a decision. Don't be tempted to commit yourself to larger housing payments than you can afford.

Once you have selected the property you want to buy, you will need financing. Again, a reputable real estate company can help you find a loan. If you are buying into a new development, the developers may already have a mortgage lender with whom they work.

In addition to traditional fixed-rate fixed-payment mortgages, various alternative mortgage instruments are used today to enable more households to afford mortgage payments and to shift some of the risk of increased inflation from lenders to borrowers. For example, the payments on a *graduated payment mortgage* (GPM) are low in the early years and gradually increase at a predetermined rate with the age of the mortgage (and, ideally, the family's income). The *adjustable-rate mortgage* (ARM) and the *variable rate mortgage* (VRM) have interest rates and payments that can increase and decrease, within certain limits, depending on economic conditions. A *roll-over mortgage* (ROM), rarely used today for first mortgages, sets up fixed payments for a few years. At the end of that time, typically around 5 years, the loan must be paid off or refinanced.

Review your current and future financial situation carefully before committing yourself to one of these mortgages. If your income should decrease or not increase as fast as the mortgage payments, you could end up with higher monthly payments than you can afford. In some cases, the additional amount that you owe due to an increase in your interest rate is not added to your monthly payments but to your principal. This "negative amortization" causes the loan balance to increase even though payments are made as scheduled. Of course if interest rates go down, payments would decrease. Consider these points when deciding if you are a good candidate for variable-mortgage payments:

- Is your long-term employment secure?
- Does your household income increase regularly?
- Are you unlikely to acquire additional large debts over the next few years?
- Are your other expenses likely to stay somewhat stable?
- Do you have additional assets to draw on in an emergency?
- Do you believe that interest rates will rise slowly or go down?

Ask prospective lenders these questions before making a final decision:

1. What index is used to determine interest rate changes?
   Lenders must base changes on an index over which they have no control. Many use the average rate of return on U.S. Treasury securities.
2. What margin is used?
   A margin is the amount over the index that lenders add to cover costs. For example, if Treasury bills earned an average of 10 percent and your lender uses a 3 percent margin, your new interest rate would be 13 percent. The margin used varies among lenders, so you will want to compare.
3. How often will the interest rate be adjusted?
   1-, 3-, and 5-year ARM's are common. The longer the time between adjustments in payments, the higher the initial interest rate is likely to be.
4. What kind of protection does the loan provide against skyrocketing increases?
   Loans are available with caps (or limits) on how much monthly payments or interest rates can increase monthly, yearly, or over the life of the loan.
5. Will the lender refinance any balloon payments?
   A balloon payment refers to one large final payment, as in roll-over mortgages.

Check with several lenders before deciding on a loan. Compare the benefits of a fixed-rate mortgage with those of the variable-rate mortgage.

Food

The food expenditure is another large part of a family's household budget. Proper purchasing, storage, and preparation of food is very important to the health and well-being of family members. Careful time and money management is necessary to provide economical and nutritious meals.

Everyone needs a well-balanced diet for energy and growth. The body needs certain nutrients. These nutrients can be obtained by serving your family a variety of foods from the four basic food groups daily: (1) meat, poultry, fish, and legumes, (2) fruits and vegetables, (3) bread and cereals, and (4) milk and cheese. Having good eating habits means avoiding too much sugar, fat, and salt in your diet.

1.15

Determine Food Expenditures

The amount that your household will spend on food depends on the number of adults and children in your family, personal tastes, and special nutritional requirements. To help you estimate how you might allocate your food dollars, the U.S. Department of Agriculture has developed four food plans—thrifty, low-cost, moderate-cost, and liberal. They can help you provide a nutritious diet at a price you can afford. The higher cost food plans (moderate-cost and liberal) generally contain greater quantities of meat, poultry, fish, fruits, and vegetables than the lower cost food plans (thrifty and low-cost), which contain more grains. The thrifty food plan is the least expensive. It relies heavily on dry beans and peas, flour, bread, and cereals; it includes smaller amounts of meats, poultry, and fish than families typically use. Households under the thrifty and low-cost food plan purchase lower cost food items within each food group—ground beef instead of porterhouse steak, for example. Households with more to spend on food will probably want to use the moderate-cost or liberal food plan for guidance on food spending.

To decide which food plan is appropriate for your family, use Table 1 to find the food plan for households that have an income and size that is similar to yours. Table 2 on page 1.16 shows the cost of food at home for each cost level. Notice that in June 1985 the weekly food expenditure for a young family with two elementary school age children was $62.00 under the thrifty plan, $78.80 under the low-cost plan, $98.20 under the moderate-cost plan, and $117.80 under the liberal plan.

Clothing

Although the basic purpose of clothing is body protection, it often reflects your personality, confidence, and self-esteem. It is important to select clothing that looks good, fits well, and is durable yet comfortable. A wide range of prices for most clothing allows you to make the most of your clothing budget dollars without sacrificing these qualities.

Table 1. Food Plans by Size and Income of Family[1]

	Family size					
Income before taxes	One person	Two persons	Three persons	Four persons	Five persons	Six persons
Under $5,000	T[2]	T[2]	T[2]	T[2]	T[2]	T[2]
$5,001-$10,000	LC	T[2] or LC	T[2]	T[2]	T[2]	T[2]
$10,001-$15,000	MC	LC or MC	T or LC	T[2] or LC	T[2]	T[2]
$15,001-$20,000	MC or L	LC or MC	LC	T or LC	T or LC	T[2] or LC
$20,001-$30,000	L	MC	LC	LC	T or LC	T or LC
$30,001-$40,000	L	MC or L	MC	LC or MC	LC	LC
$40,001 or more	L	L	MC or L	MC	LC or MC	LC or MC

T Thrifty LC Low cost MC Moderate cost L Liberal

[1]To use this table: Locate the column that corresponds to the number of persons in the family. Then move down this column to the point opposite the family income before taxes are deducted. The plan shown there costs about the amount a typical household (of similar size and income) spends for food. It is the plan a family of that size and income can usually afford.

[2]Many families of this size and income are eligible for assistance through the Food Stamp Program. For further information, contact your welfare department.

SOURCE: Odland, Diane and Carole Davis. 1984. *Your Money's Worth in Foods*, USDA, Home and Garden Bulletin No. 183

Determine Clothing Expenditures

1.16 Clothing expenditures within each household will vary from member to member. The amount to allocate for each person will depend not only on the family income, but also their sex and age (are they still growing?), activities (school, work, sports), standards (and those of their peers), and personal preferences.

Clothing expenses for employed adults usually exceed those for other adults. Clothing expenses for persons who entertain frequently will be greater than those who do not. Clothing expenses for school age children increase with age all during the school years. Preschool children who are still growing may require a new wardrobe each season.

Table 2. Cost of Food at Home Estimated for Food Plans at 4 Cost Levels, June 1985, U.S. Average[1]

	Cost for 1 week				Cost for 1 month			
Sex-age group	**Thrifty plan**	**Low-cost plan**	**Moderate-cost plan**	**Liberal plan**	**Thrifty plan**	**Low-cost plan**	**Moderate-cost plan**	**Liberal plan**
Families								
Family of 2:[2]								
20-50 years	$37.00	$46.40	$57 10	$70.40	$160.20	$201.10	$247 60	$305.20
51 years and over	35 00	44 30	54.40	65 10	151 40	192 20	236 30	282 00
Family of 4: Couple, 20-50 years and children—								
1-2 and 3-5 years	53 80	67 00	81.50	99.50	233.40	289.90	353 30	431 70
6-8 and 9-11 years	62.00	78 80	98 20	117.80	268 50	341 40	425 80	510 80
Individuals[3]								
Child:								
1-2 years	9 70	11 80	13 70	16.40	42 10	51 00	59.20	71 30
3-5 years	10.50	13.00	15.90	19 10	45 70	56 10	69.00	82 90
6-8 years	13 00	17 10	21.40	24.90	56.20	74 20	92.70	108 10
9-11 years	15.40	19 50	24.90	28.90	66 70	84 40	108 00	125 20
Male:								
12-14 years	16 10	22 10	27 40	32.20	69.60	95.60	118 90	139 50
15-19 years	16.70	22.90	28.30	32 80	72 60	99 10	122 40	142 00
20-50 years	17.70	22.50	28 10	33 80	76 80	97 50	121.90	146 50
51 years and over	16.10	21 30	26 10	31.30	69 70	92 30	113 30	135 40
Female:								
12-19 years	16.00	19.00	23.00	27 70	69 10	82 50	99 70	120 10
20-50 years	15 90	19 70	23.80	30.20	68 80	85 30	103 20	131 00
51 years and over	15.70	19 00	23.40	27.90	67 90	82 40	101.50	121.00

[1]Assumes that food for all meals and snacks is purchased at the store and prepared at home. The costs of the food plans are estimated by updating prices paid by households surveyed in 1977-78 in USDA's Nationwide Food Consumption Survey. USDA updates these survey prices using information from the Bureau of Labor Statistics to estimate the costs for the food plans.

[2]10 percent added for family size adjustment. See footnote 3.

[3]The costs given are for individuals in 4-person families. For individuals in other size families, the following adjustments are suggested: 1-person—add 20 percent, 2-person—add 10 percent, 3-person—add 5 percent, 5- or 6-person—subtract 5 percent, 7- or more-person—subtract 10 percent.

Source: U.S. Department of Agriculture, Family Economics Research Group. 1985. *Family Economics Review* 1985(4).

1.17

Save on Your Clothing Budget

You can do some things to cut down on clothing expenses. If you are skilled in sewing and enjoy handiwork, try making some of your family's clothing. Sewing can be a moneysaver for anyone who has the skill, time, and equipment necessary and selects economical supplies and materials. Shopping at yard sales and secondhand stores is another way to save considerably on clothing. However, if your family has bad feelings about wearing recycled clothing, your purchase could be money wasted instead of money saved. When you buy new, readymade clothing, make your money go further by planning wardrobes, shopping wisely, reading labels, recognizing quality clothing, and following care instructions.

Transportation

Dependable transportation is an important asset to every household. Persons who can conveniently depend on public transportation are fortunate. Unless you live in an urban or heavily populated suburban area, however, public transportation may not be available, so most families own a car. Purchasing, owning, and operating a car involves a considerable cost. Car pooling has become a popular way of cutting some of these costs. Several riders travel together sharing the related expenses of driving to work, shopping, church, and even long trips. Walking to nearby locations is another alternative that not only saves money but is good exercise. Renting or leasing a car is an alternative for some people, as is riding a bicycle or motor bike.

The Cost of Owning and Operating an Automobile

If you decide to purchase a car, know the costs involved. Then you can look for a car that will best fit your budget. Know how the size of the car affects maintenance and ownership costs in terms of fuel efficiency, repair costs, and insurance rates. The chart on page 1.18 gives a breakdown of the total cost per mile to drive cars and vans. Information from the U.S. Department of Transportation shows that over a 12-year period the total cost for driving a car 120,000 miles is $36,751 for a large-sized American car, $47,111 for vans, $27,259 for subcompacts, $33,415 for intermediates, and $27,968 for compacts. Depreciation is the largest single expense involved in owning a car. Larger automobiles generally lose value faster than smaller ones do. Other expenses include maintenance, gas and oil, parking and tolls, insurance, and taxes.

What To Consider When Purchasing a Vehicle

To determine how well the purchase of a car will fit into your budget, ask yourself these questions:

What kind of transportation do I need?
What will I use the vehicle for?
Can I afford the cost of maintaining the size vehicle I want?
What price am I willing to pay?
Who else in the household will be driving the vehicle?
What will I have to give up in order to afford the vehicle?
Will a used car or other transportation do?

1.18 Would it be to my financial advantage to save and pay cash or to use credit to buy an automobile?

If I am buying on credit, how much can I afford as a downpayment?

Will my trade-in cover the cost of the downpayment?

How large a monthly payment can fit comfortably into my budget?

Will owning a car make other economic opportunities available to me?

Visiting several car dealerships could result in a considerable savings, since prices may vary widely. Check the price of the model you have decided on and the amount each

Cost of Owning and Operating Automobiles and Vans, 1984

Suburban-Based Operation
total costs: cents per mile

Size	Original Vehicle Cost Depreciated	Maintenance, Accessories, Parts & Tires	Gas & Oil (Excluding Taxes)	Parking & Tolls	Insurance	State & Federal Taxes	Total Cost
Large WITH STANDARD EQUIPMENT, WEIGHT MORE THAN 3,500 LBS. EMPTY	[illegible]	6.0	7.0	0.9	4.9	2.2	30.6
Intermediate WEIGHT LESS THAN 3,500 LBS. EMPTY	8.6	5.2	5.7	0.9	5.6	1.8	27.8
Compact WEIGHT LESS THAN 3,000 LBS. EMPTY	7.3	4.6	4.6	0.9	4.3	1.6	23.3
Subcompact WEIGHT LESS THAN 2,500 LBS. EMPTY	5.9	5.1	4.4	0.9	5.0	1.4	22.7
Passenger Van WEIGHT LESS THAN 5,000 LBS. EMPTY	10.7	6.9	9.1	0.9	8.9	2.7	39.2

SOURCE: U.S. Department of Transportation, Highway Statistics Division, 1984. *Cost of Owning and Operating Automobiles and Vans.*

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dealer will allow on your trade-in. You may also want to check the manufacturer's suggested price and compare it with dealer markups. Test-drive the car and check for comfort and proper handling. Shop around for the best financing terms. Consider not only dealer financing but banks, finance companies, and credit unions. Read your purchase contract carefully before signing. Make sure you understand everything. Check all figures and draw lines through blank spaces indicating no charge.

Once you have your car, observe proper auto maintenance suggestions to help keep ownership and operating costs down.

Utilities

Heating and cooling your home probably accounts for most of your residential energy use In recent years gas, fuel oil, and electricity bills have demanded a larger share of your household's income. Learning to effectively manage your household's energy consumption not only helps to contain costs, but also ensures that these limited resources will be available in future years.

Why not begin managing your household's energy consumption by taking a personal energy audit of your house, mobile home, or apartment? If you want an indepth picture of your energy situation, contact your local utility companies. For a small fee they will usually perform an energy audit of your home. New telephone regulations allow you to review your telephone use practices and arrange for only the equipment and services that you use. Consider, for example, whether to buy or rent telephones and which long distance company would best provide for your needs.

Because utility bills usually vary from month to month, they may be difficult to budget. Check to see if your utility companies offer an even-payment plan in which you pay a set monthly fee. Once or twice a year, adjustments are made to your account, crediting you for overpayments or billing you for additional payments. If you feel this kind of plan would be helpful, call your utility company for more information.

Children

Planning for the costs of raising children is an important part of a family's overall financial plan. Each child represents a long-term financial commitment to parents, usually for at least 18 years. Although a couple's decision to have children will not be based entirely on the financial aspects of raising them, they should be aware of the associated costs and decide early in their financial plans how they will meet these costs.

The Cost of Having a Baby

According to a 1982 study[1], the national average medical cost of having a baby is $2,307. In addition, average costs are $851 for a baby's layette and furnishings and $235 for a mother's maternity wardrobe.

Hospital and medical costs are basically set, depending on which physician and hospital you use, so there is little opportunity to cut costs there. This makes medical insurance with maternity benefits extremely important to would-be parents. However, the baby's layette and furnishings is one area where parents can conserve. Borrowing these items is a good way to cut costs.

[1]Study by the Health Insurance Association of America, reported in *The Cost of Having a Baby*.

The Cost of Child Care

1.20

Many children are growing up in households where both parents work outside the home. For these parents, the cost of child care is an important consideration in the financial plan of rearing children. The cost of child care averages about 3 percent of family spending.[2] Parental care is the most common child care arrangement followed by care by a relative, care by a nonrelative, nursery school, and day care centers. Child care costs vary by the type of care. Care by relatives is the least costly. Day care or nursery school care is more costly. Remember that there is also a wide variety in the fees that individual schools charge and in the services they provide for your children. Costs often depend on the type of care unit you select and the days and hours that your child will need care. Thoroughly investigate several alternatives before making your decision.

Table 3. Current Dollar Estimates of Cost of Raising a Child[1] Born in 1984, at the Moderate Cost Level, in the Urban Midwest Region[2]

Year	Age of child (years)	Total	Food at home[3]	Food away from home	Clothing	Housing[4]	Medical care	Education	Transportation	Other[5]
		Cost of raising a child born in 1984[6]								
1984	Under 1	$ 4,312	$ 571	0	$ 142	$1,876	$278	0	$ 866	$ 578
1985	1	4,664	736	0	149	1,970	292	0	910	607
1986	2	4,561	773	0	254	1,819	307	0	832	576
1987	3	4,789	812	0	266	1,910	322	0	874	605
1988	4	5,327	979	$172	279	2,005	338	0	918	636
1989	5	5,593	1,028	181	293	2,105	355	0	964	667
1990	6	6,118	1,044	190	426	2,095	373	$166	1,012	812
1991	7	6,678	1,352	199	448	2,200	391	174	1,062	852
1992	8	7,012	1,419	209	470	2,310	411	183	1,115	895
1993	9	7,364	1,490	220	494	2,425	432	192	1,171	940
1994	10	8,031	1,863	231	518	2,547	453	202	1,230	987
1995	11	8,431	1,956	242	544	2,674	476	212	1,291	1,036
1996	12	9,456	2,099	305	826	2,911	500	222	1,456	1,137
1997	13	10,175	2,449	321	867	3,057	525	234	1,523	1,194
1998	14	10,685	2,572	337	911	3,210	551	245	1,605	1,254
1999	15	11,217	2,700	354	956	3,370	578	258	1,685	1,316
2000	16	12,933	3,174	371	1,391	3,663	607	270	1,953	1,504
2001	17	13,581	3,333	390	1,461	3,846	638	284	2,050	1,579
Total 1984-2001		140,927	30,350	3,722	10,695	45,993	7,827	2,642	22,522	17,176

[1]Child in family of husband and wife and no more than 5 children.
[2]Formerly the North Central region.
[3]Includes home-produced foods and school lunches.
[4]Includes shelter, fuel, utilities, household operations, furnishings, and equipment.
[5]Includes personal care, recreation, reading, and other miscellaneous expenditures.
[6]Inflated from 1983 constant dollar estimates at annual rate of 5 percent and rounded to nearest $1.

SOURCE: Updated from Table 8 of Edwards, Carolyn, 1981. *USDA Estimates of The Cost of Raising a Child: A Guide to Their Use and Interpretation.* U.S. Department of Agriculture, Miscellaneous Publication 1411.

The Cost of Raising a Child

1.21 The amount that each household will spend to provide a child with food, housing, clothing, ·ducation, and other needs will vary according to how much the household can afford and what they consider necessary. The U.S. Department of Agriculture has developed estimates of the cost of raising a child from birth to age 18 for several cost levels and for each region of the country.[3] Costs are measu~ed for: food at home, food away from home, clothing, housing, transportation, medical care, education, and all other items.

The cost per year for raising a child increases as the child ages. Clothing and food expenses account for much of this increase. Housing, transportation, and other costs (such as recreation and personal items) are shared expenses based on the spending patterns of the whole family. Medical costs fluctuate and depend largely on the child's health and family standards. Educational costs (including supplies, lessons, and so on) from elementary school through high school are basically stable. Table 3 shows the cost per year of raising a child born in 1984. Table 4 on page 1.22 shows the total costs of raising urban and rural children.

Based on these estimates, USDA calculates the total cost of raising a child to age 18 to range from $38.027 to $104,532.

[2]According to Marsha Freeman Epstein and Cynthia L. Jennings, 1979, Child Care: Arrangements and Costs, *Family Economics Review*, Fall issue, p. 3. Updated to 1983 figures.

[3]USDA Estimates of *The Cost of Raising a Child: A Guide to Their Use and Interpretation*. U.S. Department of Agriculture, Miscellaneous Publication 1411.

Table 4. Total Cost of Raising a Child[1] to Age 18 (June 1985 Price Levels)

Region	Economy	Low	Moderate
Urban			
Midwest	$47.744	$65,130	$89,957
Northeast	42,315	55,482	94,832
South	44,709	61,126	97,889
West	48,817	67,520	100,004
Rural Nonfarm			
Midwest	$38,027	$55,732	$83,847
Northeast	42,489	66,720	101,924
South	38,765	60,554	98,273
West	50,847	72,138	104,532

[1]In family of husband and wife and no more than 5 children

SOURCE: Updated from Edwards, Carolyn S. 1981. *USDA Estimates of The Cost of Raising a Child: A Guide to Their Use and Interpretation*. U.S. Department of Agriculture, Miscellaneous Publication 1411.

1.22

The Cost of Educating a Child

A child's need for education beyond high school is a concern of many parents. Some parents make financial plans for their children's college or vocational education while the children are still young. The amount necessary for a child's continued education depends on:

- Type of education chosen (college or vocational).
- Type of institution selected (public or private).
- Kind of training required.
- Length of training needed.
- Whether or not the student will live at home.
- Personal needs of the student.

Table 5 shows that the estimated cost of 1 year of public education at a 2-year institution begins at $2,560.

There are several ways to meet these education expenses:

- Set up an educational fund in advance.
- Take educational expenses from current income as required.
- Borrow funds.
- Have student apply for financial assistance at the educational institution.
- Have student seek employment—many employers offer educational opportunities.

Table 5. Estimated Undergraduate Tuition and Fees and Room and Board Rates in Institutions of Higher Education, 1983-84

Type and control of institutions	Tuition and required fees	Board	Dormitory rooms	Total tuition and room and board
All public institutions	$ 870	$1,210	$1,080	$3,160
Universities	1,270	1,250	1,150	3,670
Other 4-year	1,020	1,180	1,060	3,260
2-year	510	1,240	810	2,560
All nonpublic institutions	4,880	1,390	1,270	7,540
Universities	6,140	1,610	1,560	9,310
Other 4-year	4,750	1,320	1,160	7,230
2-year	3,300	1,260	1,260	5,820

SOURCE: Grant, W. Vance, and Thomas D. Snyder. 1983. *Digest of Education Statistics 1983-1984*. U.S. Department of Education, National Center for Education Statistics.

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U.S. Office of Consumer Affairs. *How To Buy a Telephone.* 1-page pamphlet. (Published in cooperation with the Electronic Industries Association).

_________. *Your Keys to Energy Efficiency.* 20 pp. (Published with the assistance of Gulf Oil Corporation).

Children

U.S. Department of Agriculture, Agricultural Research Service, Family Economics Research Group. *USDA Estimates of the Cost of Raising a Child.* Misc. Pub. No. 1411. 57 pp.

U.S. Department of Education. *Federal Financial Aid.* Publication No. E-82-15003. 19 pp.

_________. *The Student Guide: Five Federal Financial Aid Programs, 1983-84.* 17 pp.

_________, National Center for Education Statistics. *College Costs: Basic Student Charges, 4-Year Institutions, 1982-83.* NCES 83-317. 13 pp.

_________. *College Costs: Basic Student Charges, 2-Year Institutions, 1982-83.* NCES 83-321. 10 pp.

Where to Go for Help

U.S. Office of Consumer Affairs. *How To Choose and Use a Lawyer.* 1-page pamphlet. (Published in cooperation with the American Bar Association)

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Current Government Publications

Over 200 free or moderately priced consumer publications are available from the Consumer Information Center. To obtain a free catalog, write to: Cata' g, Pueblo, CO 81009.

The U.S. Government Printing Office sells over 15,000 Federal publications. Many titles of consumer interest are listed in Subject Bibliography No. 2, *Consumer Information.* To obtain a free copy, write to the Superintendent of Documents, Government Printing Office, Washington, DC 20402.

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Worksheet 1: Net Worth Statement

Assets (What you own)	First year	Second year	Liabilities (What you owe)	First year	Second year
Liquid					
Cash			Current bills		
Bank			Charge accounts		
Checking			Credit cards		
Savings			Taxes		
Certificates			Installments		
Other			Mortgages		
Savings bonds			Other		
Other bonds					
Corporate					
Municipal					
Utility					
Life insurance					
Mutual funds					
Other					
Other assets					
Retirement plans					
Private pension plan					
Profit-sharing plan					
Home					
Other real estate					
Car(s)					
Furniture					
Large appliances					
Antiques and art					
Jewelry					
Silverware					
Stamp or coin collection					
Debts others owe you					
Other					
Total Assets			**Total Liabilities**		

Net Worth (Total assets minus total liabilities)

First Year: _____ – _____ = _____

Second Year: _____ – _____ = _____

1.26 Worksheet 2: Projecting Goals

Long-Term and Intermediate

Goal	Cost of goal	Number of years before needed	Amount already saved	Amount to save each year	Amount to save each month
1.					
2.					
3.					
4.					
5.					
6					
7.					
8.					
9.					
10					
Total					

Immediate

Goal	Cost of goal	Month money will be needed	Amount already saved	Amount to save each month	Amount to save each pay period
1.					
2.					
3.					
4.					
5.					
6.					
7					
8					
9.					
10.					
Total					

1.27 Worksheet 3: Estimating Your Income

Worksheet 3: Estimating Your Income

Source	January	February	March	April	May	June	July	August	September	October	November	December	Yearly totals
Net salary *													
Household member 1													
Household member 2													
Household member 3													
Household member 4													
Social Security payments													
Pension payments													
Annuity payments													
Veterans' benefits													
Assistance payments													
Unemployment compensation													
Allowances													
Alimony													
Child support													
Gifts													
Interest													
Dividends													
Rents from real estate													
Other													
Monthly Totals													

* Net salary is the amount that comes into the household for spending and saving after taxes, Social Security, and other deductions.

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Worksheet 4:
Expense Estimate and Budget Balancing Sheet, Fixed Expenses

Worksheet 4: Expense Estimate and Budget Balancing Sheet, Fixed Expenses

	January			February			March			April			Subtotal
	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	
Rent													
Mortgage													
Installments													
Credit card 1													
Credit card 2													
Credit card 3													
Automobile loan													
Personal loan													
Student loan													
Insurance													
Life													
Health													
Property													
Automobile													
Disability													
Set-asides													
Emergency fund													
Major expenses													
Goals													
Savings and investments													
Allowances													
Education													
Tuition													
Books													
Transportation													
Repairs													
Gas and oil													
Parking and tolls													
Bus and taxi													
Recreation													
Gifts													
Other													
Total Fixed Expenses for Month													

Worksheet 4: Expense Estimate and Budget Balancing Sheet, Fixed Expenses (continued)

	May			June			July			August			Subtotal
	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	
Rent													
Mortgage													
Installments													
Credit card 1													
Credit card 2													
Credit card 3													
Automobile loan													
Personal loan													
Student loan													
Insurance													
Life													
Health													
Property													
Automobile													
Disability													
Set-asides													
Emergency fund													
Major expenses													
Goals													
Savings and investments													
Allowances													
Education													
Tuition													
Books													
Transportation													
Repairs													
Gas and oil													
Parking and tolls													
Bus [illegible] taxi													
Recrea[illegible]													
Gifts													
Other													
Total Fixed Expenses for Month													

Worksheet 4: Expense Estimate and Budget Balancing Sheet, Fixed Expenses (continued)

	September			October			November			December			Subtotal	Total Fixed Expenses for Year
	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference		
Rent														
Mortgage														
Installments														
Credit card 1														
Credit card 2														
Credit card 3														
Automobile loan														
Personal loan														
Student loan														
Insurance														
Life														
Health														
Property														
Automobile														
Disability														
Set-asides														
Emergency fund														
Major expenses														
Goals														
Savings and investments														
Allowances														
Education														
Tuition														
Books														
Transportation														
Repairs														
Gas and oil														
Parking and tolls														
Bus and taxi														
Recreation														
Gifts														
Other														
Total Fixed Expenses for Month														

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Worksheet 4:
Expense Estimate and Budget Balancing Sheet,
Flexible Expenses

Worksheet 4: Expense Estimate and Budget Balancing Sheet, Flexible Expenses

	January			February			March			April			Subtotal
	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	
Food													
At home													
Away from home													
Utilities													
Gas/fuel													
Electricity													
Telephone													
Water													
Household													
Maintenance and supplies													
Furnishings													
Decorating													
Clothing													
Household member 1													
Household member 2													
Household member 3													
Household member 4													
Health Care													
Doctors													
Dentist													
Other													
Medicines and prescriptions													
Personal care													
Other													
Total Flexible Expenses for the Month													

Worksheet 4: Expense Estimate and Budget Balancing Sheet, Flexible Expenses (continued)

	May			June			July			August			Subtotal
	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	
Food													
At home													
Away from home													
Utilities													
Gas/fuel													
Electricity													
Telephone													
Water													
Household													
Maintenance and supplies													
Furnishings													
Decorating													
Clothing													
Household member 1													
Household member 2													
Household member 3													
Household member 4													
Health Care													
Doctors													
Dentist													
Other													
Medicines and prescriptions													
Personal care													
Other													
Total Flexible Expenses for the Month													

Worksheet 4: Expense Estimate and Budget Balancing Sheet, Flexible Expenses (continued)

	September			October			November			December			Subtotal	Total Flexible Expenses for the Year
	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference	Amount estimated	Amount spent	Difference		
Food														
At home														
Away from home														
Utilities														
Gas/fuel														
Electricity														
Telephone														
Water														
Household														
Maintenance and supplies														
Furnishings														
Decorating														
Clothing														
Household member 1														
Household member 2														
Household member 3														
Household member 4														
Health Care														
Doctors														
Dentist														
Other														
Medicines and prescriptions														
Personal care														
Other														
Total Flexible Expenses for the Month														

Keeping Your Monthly Expense Record

The Monthly Expense Record is provided so you may record your household expenses as they occur. It is probably best if one person is assigned to making entries in your Monthly Expense Record. Photocopy enough sheets for each month of the year. Here are a few points to remember when making your entries.

Fill the month and year in the top right-hand corner of each sheet.

Keep your record book up to date using receipts and check stubs, when possible, to verify amounts.

Put the day of the month that you paid an expense under the date column.

Name the purchase or payment under each expense heading. Be specific, such as the name of the company you wrote the check to, i.e. "National Bank," or what the purchase was actually for, i.e. "books for Tom."

Write the exact amount of that particular expense under the correct expense heading.

Total amounts under each heading at the end of the month.

Transfer each total expense figure to worksheet 4 on pages 1.29-1.39 under "Amount spent" for the correct month. Subtract what you had estimated in an expense category from what you actually spent. Record the difference.

Now transfer each total expense figure to worksheet 6, Total Household Expenses, under the corresponding month.

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Worksheet 5:
Monthly Expense Record

Worksheet 5: Monthly Expense Record

Month ____ Year ____

Date	Expense item	Mortgage/ Rent	Household operation	Utilities	Food	Clothing	Transportation	Child care	Medical	Savings	Debts	Insurance	Education	Personal care	Recreation	Gifts	Business related	Other: Taxes, allowances, legal fees
Total																		

1.43 **Worksheet 6: Total Household Expenses**

Worksheet 6: Total Household Expenses for 19___

Expense item	January	February	March	April	May	June	July	August	September	October	November	December	Total
Mortgage/rent													
Household operation													
Utilities													
Food													
Clothing													
Transportation													
Child care													
Medical													
Savings													
Debts													
Insurance													
Education													
Personal care													
Recreation													
Gifts													
Business related													
Other													
Total													

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Managing Your Personal Finances

Financial Tools Used in Money Management

Prepared by

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Family Economics Research Group
Agricultural Research Service
U.S. Department of Agriculture

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Preface

Managing Your Personal Finances is a budgeting guide. It is divided into three sections which are available individually or as a set. The total guide is designed to help you develop money management skills. It will teach you how to set goals, how to make a budget for your circumstances, and how to plan for the future. The guide contains information on saving and investing, using insurance and credit, and planning for retirement; and suggests where to go for additional help. Specific information is included on:

- Developing a budget.
- Using financial tools to carry out your budget.
- Recognizing financial and economic conditions that affect your budget.

Section 1: **The Principles of Managing Your Finances**
HG-245-1

Section 2: **Financial Tools Used in Money Management**
HG-245-2

Section 3: **Coping With Change**
HG-245-3

Copies of complete sets or individual sections are for sale from

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Contents

Chapter 1

2.1 Saving and Investing

plan for saving and investing is an important part of a household budget. Saving can help you meet emergencies as they occur; investing can help you reach your long-term goals. *Make saving a habit.* Regular savers end up saving far more than occasional savers, even when they save only a small amount at a time.

There are many ways to save. Every payday, try putting money into a savings account first, before paying other expenses. Or have your employer deduct a portion of your earnings and deposit it directly in a savings account. Put your change in a home bank or jar. When it is full, deposit the money in the bank. When a loan repayment ends, save the amount of the old payment instead of putting it back into the budget for spending.

You may want to begin your saving plan by setting up an emergency fund. Many suggestions have been made on the amount of money that should be kept in a savings account emergency fund. For example, it might be 2 to 3 months' take-home pay, 6 months' pay, or an amount equal to 1 year's fixed expenses. You are the only one who can decide. Consider how stable your income is and how fast you could cash in other investments if necessary. When you feel that you have a sufficient amount in your emergency fund, start investing your savings where they will earn higher interest.

The purpose of both saving and investing is to multiply your money. Differences between the two are determined by:

The degree of risk.
The rate and stability of return.
The availability of funds for use.
The amount of protection against inflation.

Money in a savings account is considered to be safe—meaning you get back at least the amount you deposited (less any banking fees). Most savings accounts are convenient, flexible, and easy to obtain. Savings accounts, however, do not usually yield high rates of return. Money needed to meet emergencies and immediate goals must be convenient and readily available. Keep these funds in a savings plan.

While the main attraction of savings is security, the major advantage of investing is high money-growth potential. Since investment plans usually carry a higher rate of return

2.2

than savings plans, they provide better protection against the loss of the value of money during inflationary times. Some investments require that your funds be unavailable for use for a certain period of time. You also may carry a greater risk of losing all or part of your money when investing. Investigate putting the bulk of your money in plans that pay high returns. Consider the risk involved in each plan before you invest.

Saving

You will need to decide where and how to save your money. Many savings institutions—commercial banks, savings and loan associations, mutual savings banks, and credit unions—have developed accounts to attract your savings dollar. You must decide not only which savings institution to use but which savings instrument—passbook account, savings certificate, certificate of deposit, or NOW account—is best for your needs. Answer these questions before making your decision:

How safe is money in this particular institution and savings plan?
Are there minimum-balance requirements?
Are there penalties and fees for transactions?
How convenient is it to make deposits and withdrawals?
At what rate and how often is interest compounded?
What special features or services are offered?
Are there any tax advantages or disadvantages associated with this saving instrument or institution?

Select a Savings Institution

Commercial banks are convenient, flexible, financial institutions that offer a wide variety of services such as providing savings and checking accounts and making loans. Most commercial banks are members of the Federal Deposit Insurance Corporation (FDIC), insuring each account up to $100,000.

Savings and loan associations offer a more limited range of financial services. Traditionally, their main purpose has been to offer savings accounts and to make housing loans. The Federal Savings and Loan Insurance Corporation (FSLIC) insures the safety of your deposit up to $100,000 at participating savings and loan associations.

Mutual savings banks are found in some areas. Like savings and loan associations, their main activities involve savings accounts and mortgage loans. Most of these institutions are also insured by FDIC.

Credit unions are a widely used financial institution. You usually must be a member of an organization in order to use its credit union. The National Credit Union Association (NCUA) insures accounts up to $100,000.

Select a Savings Instrument

NOW and Super NOW (negotiable order of withdrawal) accounts are checking accounts that earn interest. Super NOW accounts require larger minimum balances and pay higher interest rates than regular NOW accounts. Some NOW accounts charge fees that offset any interest you may have earned, however.

Passbook savings accounts require a low minimum balance and are convenient to use, but pay low interest rate. The amount of interest income earned depends on not only the stated interest rate, but also on the method by which the interest is compounded and credited to your account. If stated rates are the same at several places, consider using savings institutions that use the day-of-deposit to day-of-withdrawal method of computing interest to earn the most on your savings account.

Certificates of deposit, savings certificates, and other time accounts generally pay higher interest than passbook accounts. There are many types of certificates requiring different minimum deposits and terms. In some cases, there is a penalty for early withdrawal of funds.

U.S. Government savings bonds are currently issued in Series EE (replacing the old Series E) and Series HH (replacing the old Series H). Series EE are available in denominations ranging from $50 to $10,000 and are purchased for one-half the amount of their face value. Series EE bonds held 5 years or more accrue interest calculated semiannually at 85 percent of the average yield on outstanding 5-year U.S. Treasury marketable securities, guaranteed at a minimum yield. Bonds held less than 5 years accrue interest on a graduated scale. EE bonds reach full maturity at 10 years. Series HH bonds are no longer purchased with cash; they are sold in exchange for Series E or EE bonds in denominations of $500 or more. Series HH bonds are purchased for the full face amount and pay interest semiannually by check at a flat rate. Both series must be held at least 6 months before redeeming.

Government savings bonds tie up your money for a long period of time, but they are a good investment for some people. Accrued interest is exempt from State and local taxes, and Federal tax may be deferred until the bonds are cashed or reach maturity. Payroll deduction for bonds is available through many employers, making them a convenient way to save. Bonds can also be replaced if lost, stolen, or destroyed.

Investing

Deciding how much money you will have to invest regularly for your long-term goals depends on the rate of interest that your money earns and the amount of time before the money is needed. Table 1 on page 2.4 shows how much you would have to save each month (at 6 percent and 9 percent interest) to receive $5,000 to $30,000 at the end of 5 to 25 years. For example, if you will need $10,000 in 10 years, you would need to put $63.13 each month into an investment paying 6 percent interest or $54.86 per month into one paying 9 percent.

Each investment option carries its own amount of risk. Many investors diversify or divide their investment money into several instruments, instead of risking all their money in one investment. To be able to make wise decisions among the many available investment options, you will want to know some of the characteristics of each.

Bonds

A bond represents an agreement between investors and an issuing corporation or municipality. The issuing organization agrees to pay investors a fixed interest rate for a certain period of time. At maturity, the issuer redeems the bond at its face value.

Corporate bonds are sold by private companies for the purpose of borrowing money from a large number of investors. The company must pay the interest and redeem the bonds whether or not it has made a profit. Corporate bonds are traded in the open market and are generally for investors with at least $5,000 to invest. A degree of risk is involved. How prompt a corporation is in making its interest payments will depend on its financial condition. There is also the risk that over time the interest rate paid on the bond will not be as high as the interest available on alternative investments.

2.4 *Municipal bonds* are issued by cities, States, and other local authorities. Interest paid on municipal bonds comes either from taxes paid to the issuing organization or from revenues received from some special project. The most attractive characteristic of municipal bonds is that the earned interest is exempt from Federal income tax. Some risk is involved with the purchase of municipal bonds, as interest payments depend on the financial condition of the issuing municipality. The pretax rate of return on these bonds is often less than for corporate bonds, but the tax advantages make it a good investment for persons with high income.

Stocks

Stock investments should not be expected to make immediate overwhelming profits, but with careful selection they can provide a good rate of return on your investment dollar. Stocks are not without risk, however. Owning stock in a corporation means that you own a part of the company and are entitled to a share of the profits. Earnings may be realized in two ways. First, profits may be divided among shareholders in the form of dividends. Most corporations pay dividends to shareholders quarterly. Second, profits can be made through an increase in the value of the stock on the open market. However, if the market value of the stock goes down, the loss could be considerable. Selecting and managing stock requires study and, often, the assistance of a good brokerage firm.

Table 1. Investing for Long-Term Goals

If you need this amount of money ... in this many years	5	10	15	20	25
You should save this amount each month					
In an investment yielding a 6% annual rate of return					
$ 5,000	$ 74.40	$ 31.57	$ 17.88	$11.32	$ 7.59
$10,000	148.81	63.13	35.77	22.64	15.18
$15,000	223.21	94.70	53.65	33.97	22.77
$20,000	297.62	126.26	71.53	45.29	30.36
$25,000	372.02	157.83	89.41	56.61	37.95
$30,000	444.05	189.68	107.39	67.95	45.57
In an investment yielding a 9% annual rate of return					
$ 5,000	$ 69.68	$ 27.43	$ 14.19	$ 8.14	$ 4.92
$10,000	139.35	54.86	23.38	16.29	9.84
$15,000	209.03	82.29	42.57	24.43	14.76
$20,000	278.71	109.72	56.77	32.58	19.68
$25,000	348.38	137.15	70.96	40.72	24.60
$30,000	418.06	164.58	85.15	48.86	29.52

U.S. Treasury Bills, Bonds, and Notes

2.5

The U.S. Treasury issues bills, bonds, and notes to help finance its debt and raise money. They are sold at a discount and cashed in for the face value at maturity. Bills, bonds, and notes can be bought and sold on the open market; interest rates fluctuate with market conditions. Since they are backed by the U.S. Government, safety is their primary advantage. Those with short maturities also can provide protection against inflation, but on average reflect overall market conditions rather than very high returns.

Treasury bills mature in 1 year or less. The minimum denomination available is $10,000. Bonds are available in denominations of $1,000 with maturities from 10 to 30 years. Notes can be purchased in denominations of $1,000 with maturities from 1 to 10 years. Both bonds and notes pay interest at a fixed rate twice a year until maturity.

Mutual Funds

Mutual funds are professionally managed investment portfolios in which individuals can buy shares. The fund uses the money from the sale of these shares to purchase stocks, bonds, and other investments. Profits are returned to shareholders monthly, quarterly, or semiannually in the form of dividends. Investors also earn money through the appreciation of the shares. Mutual funds allow small investors to enjoy the advantages of professional account management and diversification normally reserved for the large investor. Investment objectives vary. When selecting a fund, choose one whose investment goals are compatible with your own. For example, a fund with a growth objective might invest in stocks, sacrificing current income for long-term growth; a money-market fund would purchase bank certificates or government bonds to provide a safe short-term income.

Other Options

Real estate. There are many ways to invest in real estate. You might, for example:

Buy a house and live in it, with the intention of selling it later at a profit;

Buy a house, apartment, or commercial building and rent it; or

Buy land and hold it until its value rises.

Real estate is a specialized business. Consult with professionals in the field before making a decision. Real estate can be difficult to convert into cash, but it has proven to be excellent protection against inflation.

You can invest in real estate without purchasing property outright. Real Estate Investment Trusts (REIT's) pay dividends to shareholders from rental incomes received from apartment houses, office buildings, shopping centers, hotels, restaurants, warehouses, or other property. REIT's are professionally managed in a manner similar to mutual funds. These trusts are bought, sold, and traded daily on the open market through brokers.

There are two basic types of REIT's. *Equity* REIT's purchase income-producing properties. *Mortgage* REIT's make long-term mortgage and short-term construction loans. Equity REIT's are currently the more common of the two because some mortgage REIT's lost funds during the real estate slump of several years ago. However, mortgage REIT's often pay higher dividends for those willing to assume the risks involved.

A limited partnership is a group ownership of rental properties. Income is earned through dividends and through appreciation of the properties. Purchasing into a limited partnership allows inexperienced investors the benefit of having their money managed by

experts. The major disadvantage of a limited partnership is that the investors' money is
2.6 tied up until the properties are sold and the partnership is liquidated.

Unit trusts. Unit trusts provide investors with a fixed, professionally managed variety of investments called units. These investments, such as tax-exempt and corporate bonds and stock, earn a fixed interest income. This fixed rate could be an advantage if market interest rates fall but a disadvantage if they rise. Units can be redeemed through the trust or sold through a broker. A trust disbands and pays off investors after the majority of its investments have been redeemed.

Precious metals. Precious metal investors buy gold, silver, platinum, diamonds, and other gemstones. Over the past decade many of these investors have reaped large profits. However, investors who are not knowledgeable in the area can lose money. If you are considering investing in precious metals and gemstones, you will want to become familiar with the market. Learn grades, market value, and appreciation potential of the objects you are considering. Realize that precious metals pay no interest while you hold them but do generate some costs for insurance and storage. This is not an investment easily converted into cash—appreciation may take years and resale may not be easy.

Collectibles. Collecting valuable objects of art, antiques, stamps, coins, paintings, books, toys, and rugs is another way of investing. To be successful in this area you must either have expert advice or be familiar with the quality and likely future popularity of the objects in which you are investing. Profits are often very high. One serious drawback of collectibles is that they may not convert quickly or easily into cash.

See table 2 to help you compare some of the investments discussed in this chapter.

Table 2. Savings and Investments

Instrument	Maturity	Risk	Usual minimum balance	Taxable	Comments
Passbook account	Immediate	None	$5	Yes	Safe and convenient. There may be a fee for low balances.
Certificates of deposit	90 days and up	None	$1,000	Yes	
U.S. Savings Bonds				Yes, Federal; no State and local	Safe and convenient. Long maturity.
EE Series	10 years	None	$25 for a $50 bond		
HH Series	10 years	None	$500		
Bonds					Usually for larger investors.
Corporate	5–30 years	Some	$1,000	Yes	
Municipal	1–20 years	Some	$1,000	No Federal; some States	
Stocks	Immediate	Low to high	Varies	Yes	Risky
U.S. Treasury					Partial protection against inflation.
Bills	1 year or less	None	$10,000	Yes	
Notes	1–10 years	None	$1,000	Yes	
Bonds	10–30 years	None	$1,000	Yes	
Mutual funds	Varies	Low to moderately high	$1,000, sometimes less	Yes, except for tax-exempt bond fund	Gives investors the opportunity to have an expert invest their money.

Chapter 2

2.7 Insurance

nsurance protects households against financial loss caused by accidents, illness, death, loss of personal property, and loss of income. When deciding what you need to insure, consider your assets, their respective values, and what risks threaten their safety. You can use insurance to transfer this risk from yourself to the insurance company.

Life Insurance

Life insurance has several important purposes:

To provide money to pay burial expenses and outstanding debts.

To protect survivors against loss of income.

To serve as a form of savings.

Insurance is usually purchased on the lives of the persons who provide the household income and household services. Insurance could also build a savings fund for education, retirement, and other purposes.

The amount of the premium that you will have to pay for a insurance policy is determined by several factors:

The risk or likelihood that you will die.

If you are young and healthy, your premiums are lower than if you are older or ill.

The size of the benefit that will be paid at death.

The larger the face value of the policy, the more it will cost you.

The administrative and sales fees charged by the insurance company.

Fees can vary.

The type of policy you want.

"Pure" insurance costs less than insurance policies with a savings component.

The three basic types of insurance are term, whole life, and endowment. These types can be combined and modified to provide hybrids to meet the needs of all kinds of households.

Term

2.8

Term insurance pays benefits only at the death of the insured. This is the least expensive type of insurance available. It is most useful when a large amount of coverage is needed or income is low. Term insurance provides coverage for a certain period of time—5 years, 10 years, 20 years—or to a certain age. Most term policies are for 5-year periods, after which they can be renewed for another 5-year period at a higher premium.

Term insurance has many variations. A convertible term policy can be converted to a whole life policy without a medical examination. *Level* term insurance premiums stay the same over the life of the policy, but these premiums are higher than with straight term in early years and lower in later years. With *decreasing* term, the amount of coverage decreases each year while the premium stays the same. Mortgage insurance is a form of decreasing term insurance, decreasing to keep pace with the principal balance on your mortgage loan.

Whole Life

Whole life insurance provides protection over your lifespan without an increase in premiums as you age. Policies that provide protection throughout the lifespan are called permanent life insurance. This is in comparison to term insurance, which is temporary, providing coverage for a limited number of years. Whole life insurance has the lowest premium and the smallest cash value accumulation of the permanent type life insurance policies. There are two basic kinds of whole life insurance: *Straight life* requires you to pay premiums during your entire life; with *limited payment* your policy is paid up in a specified number of years. Since whole life policies build a reserve, you can cash in your policy for a lump sum payment or borrow money against it.

Endowment

Endowment insurance is an insured savings plan paying the face value of the policy at the end of a specified period, at which time insurance protection ends The insured receives the face value in a lump sum or by monthly payments. Endowment policies are expensive, but if purchased at a young age, the cash value may exceed the total amount paid. This type of policy is sometimes used for an educational fund or retirement fund.

Hybrids

Insurance hybrids combine some of the characteristics of term and whole life insurance with other investment options. *Universal life* insurance combines a term insurance policy with an interest-earning savings account that is geared to current market rates. The premiums go into a cash-value fund. The cost of the term insurance and fees to the company are deducted from this fund. The remainder of the premium earns interest at a variable rate that is often higher than the fixed rate paid by whole life insurance policies. Universal life policy holders receive yearly statements listing the interest rate they have earned, the amount that has accumulated in their policy, and fees they have been charged. Annual premiums for universal life are not fixed. When money is tight, your premium payments can be taken out of the accumulated cash value. Withdrawals, as well as loans, a be made from the cash-value fund. Interest earned is tax exempt until the money is withdrawn.

A *variable life* insurance policy invests most of your premium payments into investment funds that you select. The death benefit and the cash value vary with your investment. *Joint life* and *survivorship joint life* insurance policies cover two or more persons. These policies can be term or whole life. Joint life pays on the death of the first insured person; survivorship joint life pays on the death of the second. Various *family income* policies provide monthly payments to the survivors of the insured.

For the main purpose of providing income protection for survivors in case of death of the wage earner, term insurance is considered the best buy. It gives the greatest amount of protection at the lowest cost. For persons who would not meet their savings goals without a carefully administered system, whole life, endowment, or hybrid insurance may serve a purpose. Select your insurance plan with care. Often it is cheaper and more profitable in the long run to buy the separate components of the plans and invest elsewhere. See table 3 on page 2.10 for a comparison of policies.

Do You Need Life Insurance?

If your death would cause financial stress for your spouse, children, parents, or anyone you want to protect, then you should consider purchasing life insurance. Your stage in the life cycle and the type of household that you live in will influence this decision. Single persons living alone or with their parents usually have little or no need for life insurance. A two-earner couple may have a moderate need for life insurance, especially if they have a mortgage or other large debts. Households with small children most often have the greatest need for life insurance. Families may also want small amounts of insurance to cover burial expenses for children and other household members or may decide to self-insure for this.

How Much Life Insurance Do You Need?

To estimate the amount of life insurance you need, decide what your family's financial needs would be if you were to die today. Consider how much they would have to spend to pay off your medical expenses and debts and to support themselves until their graduation, marriage, retirement, death, or until they could become self-sufficient. Consider all necessary expenses, such as:

Medical expenses not covered by health insurance.
Burial expenses.
Probate and estate taxes, if your estate is very large.
Debts not cancelled by credit life insurance.
Your family's living expenses, depending on how long each will need support.

Balance these expenses with your family's current assets and income:

Life insurance.
Pensions.
Social Security.
Savings and investments.
Spouse's and dependents' incomes.
Other assets or income.

The difference between your total expenses and total assets represents an approximate

2.10

amount of life insurance that you need. You may decide to purchase additional insurance or to increase your investment to make up the difference. Keep in mind that inflation and interest rates will affect the value of your long-term investments. Athough you may seem to need a lot of life insurance, beware of committing yourself to more than you can afford.

Other Types of Insurance

Health Insurance

Health insurance is used to pay medical expenses. Preventive care, medical examinations and tests, optical and dental work, inoculations, and treatments for physical and mental illnesses are some of the things that health insurance policies may cover. Almost every household will eventually need health insurance. Even young and healthy persons will want to consider purchasing some. Policies can include any or all of the following coverages:

Hospitalization - covers hospital room and board, medications, tests, and services.
Surgical - covers operations.
Medical - covers visits to the doctor's office and diagnostic laboratory tests.
Major medical - covers expenses that exceed the dollar limit of the basic coverage.
Comprehensive - includes all the above.
Dental - covers most dental expenses.
Prescriptions - pays for prescribed medication.

Skyrocketing medical costs have made it necessary for many households to economize when planning for their medical expenses. Consider purchasing your health insurance through a group plan, or self-insuring for routine medical costs and buying insurance

Table 3. Insurance

Type policy	Period covered	Cash value	Insurance protection	Premium	Coverage	Comments
Term:						
Level	For a stated number of years such as 1, 5, 20	None	High	Same until renewal	Stays same	Pure insurance coverage.
Decreasing	For a stated number of years such as 1, 5, 20	None	High	Stays same	Decreases	Least expensive type of insurance.
Whole life:						Part insurance; part savings.
Straight	Whole life	Low	Moderate	Stays same	Stays same	
Limited payment	Whole life	Low	Moderate	Stays same	Stays same	Paid up after certain number of years.
Endowment	For a stated period of time	High	Low	Stays same	Same until paid up	Savings accumulation; no insurance protection after policy is paid up.
Universal life	Varies	Low to high	Low to high	Varies	Varies	Combines renewable term insurance with a market-rate-interest savings account.

against the unexpected, costly illnesses, and emergencies.

2.11 When selecting a health insurance policy and company, here are a few questions you may want to ask:

Is there a waiting period before coverage begins?

Is there a deductible (an amount that you pay before coverage begins)? How much is it, and how many persons in the family would have to pay the deductible per year?

What is the percentage or allowance of medical fees that are paid?

How many days of hospitalization are covered?

Is there a limit to the amount the insurance will pay or to what is considered a "reasonable and customary" fee?

Disability Insurance

At a young age, your chances of becoming disabled are greater than your chances of dying. Disability insurance protects you from loss of income if you are unable to work due to illness or accident. It pays you an income until you are able to return to work or until the benefits run out. If you become unable to work in your current job but would be able to work in another field, some policies provide benefits while you retrain.

When deciding if you need disability insurance, consider how long and how much your employer will pay if you could not work. Check to see if you qualify to receive disability payments from other sources, such as your health insurance policy, Social Security, worker's compensation, veterans' benefits, and mortgage or other loan insurance policies. Determine how much continued income could come from your spouse or other household members. If you can cover 60 to 70 percent of your present income from other sources, you are probably safe. If not, you may want to consider purchasing additional disability coverage. Disability insurance can be purchased as an option on a life insurance policy or as a separate policy. Either way you may want to be sure that:

The policy is renewable.

The company cannot cancel the policy, increase the premium, or lower benefits for a certain period.

The waiting period ends about the time your personal emergency fund runs out.

The premiums can be waived while you are disabled.

Automobile Insurance

Automobile insurance consists of two basic parts: Liability coverage for bodily injuries, property damages, and medical expenses to others when you are at fault; and physical coverage for damage (from collision, fire, theft, and so forth) to your vehicle. How much and which types of these coverages you will need largely depends on local regulations and how much you can self-insure.

Premiums for automobile insurance vary from company to company, but all rates generally reflect these points:

Your age (higher rates for persons under 25).

Your sex (higher rates for males).

Your marital status (higher rates for unmarried drivers).

Your location (higher rates for city drivers).

Your driving record (higher rates for drivers with a history of traffic violations and accidents).

Your car's age and value (higher rates for newer and more expensive cars).

Your frequency of use (higher rates for frequent use).

2.12 You can help to minimize your premiums by checking rates among companies, selecting a higher deductible, purchasing less expensive coverage, and insuring all family cars under one company.

Homeowners Insurance

Homeowners insurance is often purchased in a package plan and can include basic, broad, and comprehensive coverage. You are usually covered for repairing or replacing structures, plants and trees, and personal belongings on your property; removing debris; and any liability or medical costs resulting from lawsuits.

Policies cover such perils as fire, storms, explosions, vandalism, theft, and snow. Floods, earthquakes, and war are not usually included. Similar personal property and liability coverage is also available to condominium owners and renters. Premiums are determined by the value of your property, your location, your type of dwelling, the construction materials, your distance from fire protection, and local regulations.

Save on Insurance Costs

Insurance premiums can account for a substantial portion of the household budget. There are several ways you can reduce the amount you spend on insurance.

Comparison shopping. Insurance premiums for similar coverage vary widely from one company to the next. Check the rates at several before making a decision.

Deductibles. A deductible is the money you must pay toward a loss before the insurance will pay—the larger the deductible, the lower the premium. A large deductible can result in large savings in the premium.

Group Insuring. Group plans usually result in a substantial premium savings over individual plans—especially with health insurance. Consider joining a group insurance plan where you work, through your credit union, or through a social organization.

Self-Insuring. You can sometimes insure yourself against a loss. For example, let us say your car has a low value of about $1,000. You can save on your automobile insurance premium by dropping the collision insurance and putting $1,000 in a savings account where it can earn interest. Later, if you damage your car, money for repairs would come from your savings account instead of from your insurance company.

Fewer payments. You can usually save a few dollars by paying your insurance premiums once or twice a year instead of breaking them down into monthly payments.

Preventive measures. Being a good insurance risk can also result in lower premiums. For example, nonsmokers often qualify for lower life or health insurance premiums. Alarms in a house or apartment may qualify you for a reduction in homeowners insurance rates, and safe driver rates are available from most auto insurers.

When cutting premium costs, beware of underinsuring. Find out if your insurance will rebuild your house and replace your belongings at current prices. Underinsuring could cause considerable financial stress if after a loss you do not receive enough money to return to your prior financial position.

Chapter 3

2.13

Consumer Credit

onsumer credit involves using future income to buy goods and services today. A fee or finance charge is imposed for the privilege of borrowing money for a specified time. When used wisely, credit can be a financial asset to any household. When used carelessly, credit can cause serious financial problems.

Credit use is convenient, makes it unnecessary to carry large sums of money, and serves as a form of forced savings, allowing you to use goods and services while you are paying for them. Credit use also causes goods and services to cost more, ties up future income, and sometimes leads to overspending.

Types of Credit

There are two basic types of credit. *Open-ended* loans are made on a continuous basis for the purchase of products up to a specified limit. Bills are issued monthly for a portion of the loan. Credit cards are examples of open-ended credit. *Closed-ended* credit involves a one-time loan made for the purchase of a costly item, like an automobile or major appliance. The payment period, number of payments, and payment amounts are specified. Installment loans are closed-ended.

Interest rates on closed-ended credit accounts can vary widely, so check rates at several lenders before borrowing. Closed-ended credit lets you know exactly how long you will be indebted and how much you are paying in finance charges. This kind of regular payment is easier to budget for. Should other bills come due in one particular month, however, closed-ended credit does not allow for any flexibility in payment amounts.

Once you have your charge card, open-ended credit makes it easy to make purchases and have them added to your bill. This can be convenient, but you may also be less aware of the finance charges accrued than if you used an installment loan. Generally, the finance charge for credit cards is figured at 1½ percent per month (or about 18 percent annual percentage rate). You could pay more or less depending on the type of credit card you use and its issuing bank. The balance on which the finance charge is computed may also vary. If the interest rate is applied to the balance after recent credits and payments have been subtracted, it is the least costly for you. The most common method is for the interest to be applied to the average daily balance. Some retailers may even figure finance charges on the previous balance before subtracting any payments or credits. This is the least advantageous to you. Regardless of the method used, the creditor must tell you how your finance charge is computed. Periodic statements (bills) for charge accounts require you to make a minimum payment on the balance due. It is advantageous to pay as much as possible each month (rather than the minimum) to avoid finance charges. Unlike installment loans, open-ended accounts give you some flexibility in repaying what you owe. During difficult financial times, you have the option of paying the minimum on your charge account until the next billing period. If you continually pay only the minimum, however, you may eventually pay more in finance charges than you intended.

Building a Good Credit Record

If you want to acquire a loan easily, you will need a good credit record. There are several ways to begin building such a record:

- Acquire steady employment.
- Pay your utility bills promptly.
- Open a savings and a checking account.
- Apply for gas company or department store credit cards (which are relatively easy to get) and make payments promptly.
- Make sure the information in your current credit record is correct.

Many lenders, however, do not limit themselves to considering only these points when deciding whether or not to approve your credit application. Many use computer models and statistics to predict the likelihood of someone with your characteristics repaying the loan promptly. Such things as your profession, employer, age, home ownership, car ownership, length of residence, and length of employment may prove to be just as important as your past credit references. The method of predicting whether you would be a good credit risk varies among lenders. They are not required to disclose their specific predicting model, but they must tell you why you were turned down if you request it.

Consumer Credit Laws

Credit use can be confusing. Several consumer credit laws serve to inform and protect the individual borrower.

Truth in Lending

The "Truth in Lending" section of the Consumer Credit Protection Act has a number of provisions.

Disclosure. Truth in lending requires creditors to tell you, in simple language, the cost of the credit you wish to use. This allows you to make a better comparison of costs among lenders. Specifically, a lender must state the finance charge or the total in dollars and cents of all charges and fees involved. This includes interest and loan fees, carrying charges, credit life insurance, and credit investigation fees. Lenders must state the approximate true percentage cost of borrowing expressed in terms of the *annual percentage rate* (APR). Lenders cannot express this in terms of "add-on" or "discount" percentages.

Credit cards. Truth in lending protects against unauthorized use of credit cards. If your credit card is lost or stolen, you are liable for no more than $50 of charges made by someone else. You cannot be held responsible for any charges occurring *after* you have notified the card issuer. The law prohibits creditors from sending you a credit card unless you have requested it and requires that you be sent periodic statements as to the status of your acount.

2.15 **Advertising.** If a business mentions one credit feature in its advertising, then it must also mention all the other important credit terms.

Cancellations. When your home is used as collateral in a credit transaction, this law allows you 3 business days during which to reconsider the deal and cancel if you wish. The lender must give you written notice of your right to cancel.

Other provisions. Truth in lending allows you to sue any creditor who does not make required disclosures.

Electronic Funds Transfer Act

The Electronic Funds Transfer Act regulates the use of Electronic Funds Transfer (EFT) Systems. The EFT systems refer to a variety of bank and shopping services that are activated through electronic impulses. These impulses replace the cash, checks, and paper normally used in financial transactions.

Several systems of EFT are now in frequent use. *Automated Teller Machines* (ATM) allow banking with a bank debit card at an automatic machine where you can make deposits, receive cash, pay bills, or transfer funds. *Point of Sale Terminals* (POS) are located in some shopping areas and allow purchases through the automatic transfer of funds from your personal bank account to the merchant's account. *Preauthorized transfer* is a method of automatic withdrawal or deposit of funds or bill paying through prior authority given to the financial institution. *Telephone transfer* allows the transfer of funds or the payment of bills over the telephone.

The Electronic Funds Transfer Act spells out rights, responsibilities, and liabilities for EFT users. Specific regulations state that:

- A valid EFT card can be issued only at your request.
- The issuing financial institution must give you written information about your rights and responsibilities.
- You are liable for only $50 of unauthorized transfers if you notify the issuing agency within 2 business days after learning of its loss.
- You can get a printed receipt of your transaction.
- Your bank or other issuing agency must promptly investigate and correct any EFT errors.

Equal Credit Opportunity Act

Under the Equal Credit Opportunity Act you cannot be denied credit on the basis of your sex, age, race, marital status, or intent to have children. A creditor must give a woman the same financial consideration given to a man. The credit history of the family must be taken into consideration when deciding on a loan for either spouse. If denied credit, you have the right to know why.

Fair Credit Billing Act

The Fair Credit Billing Act requires creditors holding open-ended accounts to mail your bill at least 14 days before payment is due. Should you question the bill, the law specifies the procedures for filing grievances with the creditor. You can withhold the amount in

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question—without being penalized by an adverse credit report or undue finance charges—until an agreement can be reached. If you make a complaint to a creditor concerning faulty merchandise or a billing error, the creditor must acknowledge your complaint within 30 days and solve the problem within 90 days. You are entitled to withhold payment until your complaint is resolved. This law also allows retailers to give discounts for cash purchases.

Fair Credit Reporting Act

The Fair Credit Reporting Act deals with the information that credit bureaus sell regarding your credit history. A credit bureau gains information about you in a variety of ways. Such methods as past credit applications and hearsay rep ts are often used. This can lead to erroneous and outdated information. If you are refused credit, you have the right to see your file from the reporting credit agency. If any of the information is found to be in error, the credit bureau must delete this information and notify your potential creditors of this change.

Fair Debt Collection Practices Act

The Fair Debt Collection Practices Act prohibits abuse, threats of harm and harassment by professional debt collectors. This law does not apply to lenders who do their own collecting.

Bankruptcy Law

Persons filing for bankruptcy seek to legally eliminate some or all of their debts. Under Chapter 7 of the Bankruptcy Law, assets are sold in order to pay the debts. Debts that cannot be eliminated through bankruptcy proceedings include child support, alimony, income taxes, and debts incurred under false pretenses. Persons filing are allowed to keep:

Equity in their home ($7,500 for single, $15,000 for joint).
Social Security and veterans' benefits.
Economical car.
Jewelry ($500 for single, $1,000 for joint).
Personal clothing and effects.
Tools of trade up to $750.

Under Chapter 13 of the law, the assets are not sold. Instead, interest and late charges are eliminated and arrangements are made to pay off some or all of the debts over several years. For persons who can repay a portion of their debts, it may be best to file under Chapter 13, rather than Chapter 7. Future creditors may look more favorably upon someone who has made an attempt to honor debts. Consult an attorney on how to get the greatest benefit from the new financial start.

Determining the Cost of Credit

Credit is a service that costs you money. Whenever you consider using credit, evaluate the importance of having the item now rather than waiting until you have saved enough to pay cash for it. The merchandise you buy on credit may have a higher price tag. Stores that offer goods at the lowest prices (discount stores, factory outlets, and so forth) may not of-

2.17 fer credit. Some stores that do offer credit terms may offer a discount for payment in cash.

The extra cost of buying on credit can be calculated by comparing the credit price with the cash price. To determine the dollar cost of credit, you need the following information: The trade-in allowance, if any; the amount of the downpayment; the amount of the regular payments; the number of payments; and the cash price.

When you have the information:

1. Add all costs—trade-in allowance, downpayment, and regular payments multiplied by the number of payments required—to get the total price you will pay.
2. Subtract the cash price.

The difference is the dollar cost of buying on credit.

Suppose, for example, you are planning to buy a washing machine. Under the dealer's installment plan, you make a $50 downpayment and monthly payments of $19.75 for 24 months. The cash price for the same washing machine is $450.

Figure the dollar cost of using credit as follows:

$19.75 x 24 monthly payments	$474.00
Downpayment	+50.00
Total credit cost of washing machine	524.00
Cash price of washing machine	−450.00
Difference	$ 74.00

The dollar cost of buying on the installment plan is $74 in this case.

Dealers sometimes hide part of the cost of credit in a higher price for their merchandise. In figuring the cost of credit, compare the best price you can get on a credit deal with the best price you can get for cash. Also consider how much interest you could receive in a savings account or other investment if you made regular savings deposits with that money instead of using it to repay a loan.

How Much Credit Can You Afford?

The amount of credit you can afford will, of course, vary widely depending on your family's current financial status and future prospects. It has often been suggested that your debt level should not exceed 20 percent of your household income. A more accurate method is to review your household's budget to determine how much money you have left each month that could go toward a credit obligation.

Where to Apply for a Loan

Once you have decided that you want a loan, investigate several credit sources and shop for the best buy, considering these points:

What is the total finance charge?
What is the annual percentage rate?
What is the length of the loan?
What are the monthly payments?
Is a downpayment or collateral required?
Is there a penalty for early repayment?

Banks usually require that a borrower have a very good credit rating. Because of their high standards, a bank's interest rates and other borrowing costs may be moderate. Banks

2.18 usually report to credit bureaus. Your history of repayment to a bank, therefore, can greatly influence your credit standing.

Savings and loan associations originally made loans only to their savers mainly for mortgages and home repairs. Now they are authorized to lend for almost all consumer purposes.

Finance companies make small loans, usually at high interest rates, for short periods of time. If you have a poor credit rating or no credit history record, this may be the only loan source available to you.

Credit unions, in the past, offered lower interest rates than banks and loan associations, but this may not always be the case today. They are still good places to seek a loan, however. Since you must be a member in order to borrow from a credit union, the loan may be easier to obtain. The credit committee members are often friends and coworkers who are familiar with your integrity.

Life insurance policies are often a source of loans that many people overlook. Life insurance loans are easy to obtain and require no loan application or credit check. The maximum amount you can borrow is usually limited to the cash value of the policy you own (plus any interest or dividends). Interest rates are usually low and repayment schedules are very flexible.

Relatives or friends are sometimes willing to make loans, but use this source of credit with care! Bad feelings could arise, damaging relationships. Families may even give the money as a gift. For example, parents sometimes provide part of the downpayment for their newly married children's first home.

What to Do About Credit Problems

The use of credit can lead to budgeting problems. It is easy to be tempted to buy more than you can afford. You can become so overcommitted to debt payments that other demands on your income suffer. Your inability to repay debts now can hurt your chances for obtaining credit in the future. Here are signs that can alert you that debts may be getting out of control:

You allow some bills to hold over to the next month because there is not enough money to go around.

You pay only the minimum due on charge accounts.

You have to charge purchases more than you like because of lack of cash.

2.19 You have to use your savings or cash from credit card advances to pay current expenses.

You take out a new loan before old ones are paid off.

You cut back on necessities in order to pay installments.

If you recognize many of these signs, you may want to take steps now to cut back on your debts.

Many factors can make you unable to meet your credit obligations—financial mismanagement, increased cost of living, unemployment, family emergencies, and overspending are just a few of the perils that can occur. Once you know that you are approaching financial difficulties, contact your creditors before you are late with payments. Explain your situation to them and try to come to some type of agreement, such as reduced payments, refinancing for a longer period, or temporarily skipping a payment until you are able to once again honor your obligations.

Next you will want to try to increase your income. You may want to work extra hours, increase the number of workers in the household, or cut living expenses. You should probably consider taking out a consolidation loan (one large loan used to pay off the smaller ones) only if you are extremely pressed. Bankruptcy should be considered only after all other options are exhausted because of the long-term effects it will have on your financial standing. Most adverse information maintained by the credit bureau may be reported for only 7 years. Bankruptcy, however, may be reported longer. This may make it difficult for you to receive future loans.

Credit counseling services can sometimes help if you are having trouble paying your bills. Check to see if your bank, credit or labor union, local county extension service, or social agency offers credit counseling services. The local U.S. Department of Housing and Urban Development (HUD) office can send you a list of HUD-approved homeownership counseling agencies. Many counseling services are offered free of charge or for a nominal fee. Avoid services that charge large fees based on your income or on a percentage of your debt.

Credit counselors will review your income and expenses and help you set up a spending plan. Once you sign a contract for a credit counseling agency to help you, you must agree not to enter into any more debt. They will contact your creditors and make arrangements for reduced payments on your bills. You may be required to make payments to the agency and let them pay your creditors.

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Current Government Publications

Over 200 free or moderately priced consumer publications are available from the Consumer Information Center. To obtain a free catalog, write to: Catalog, Pueblo, CO 81009.

The U.S. Government Printing Office sells over 15,000 Federal publications. Many titles of consumer interest are listed in Subject Bibliography No. 2, *Consumer Information*. To obtain a free copy, write to the Superintendent of Documents, Government Printing Office, Washington, DC 20402.

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Managing Your Personal Finances

Coping With Change

Prepared by

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Family Economics Research Group
Agricultural Research Service
U.S. Department of Agriculture

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Preface

Managing Your Personal Finances is a budgeting guide. It is divided into three sections which are available individually or as a set. The total guide is designed to help you develop money management skills. It will teach you how to set goals, how to make a budget for your circumstances, and how to plan for the future. The guide contains information on saving and investing, using insurance and credit, and planning for retirement. It also suggests where to go for help and where to find additional reading materials. Specific information is included on:

- Developing a budget.
- Using financial tools to carry out your budget.
- Recognizing financial and economic conditions that affect your budget.

Section 1: **The Principles of Managing Your Finances**
HG-245-1

Section 2: **Financial Tools Used in Money Management**
HG-245-2

Section 3: **Coping With Change**
HG-245-3

Copies of complete sets or individual sections are for sale from:

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Contents

Chapter 1

Retirement can be an exciting phase in your life. However, for a successful retirement you must plan for financial security, for emotional and physical health, and for increased leisure time. Once into retirement you will need to evaluate and adjust your plans. Retirement planning helps you understand the retirement process and gain a sense of control about the future.

Investing for retirement is an important part of a financial plan. The sooner you have your plan established, the more money you are likely to have accumulated at retirement. Investing for retirement early is not only an excellent way of having income available in your later years, but of providing yourself with a tax deduction today.

If you are young, you have the best advantage in retirement planning. The sooner you begin your planning the better. You will be able to estimate your retirement income and make plans now to increase investments if Social Security and pensions will not meet your future living needs. You can develop the job skills necessary to maintain a steady income and select employment that provides a good mix of fringe benefits, including a pension plan.

If you are close to retirement, you have a better idea how financially prepared you are. Focus on determining where your retirement income will come from. If necessary, make plans for supplementing this income. You may have already decided where you want to live and how you want to spend your time, but it is not too late to make adjustments to your plans. If you are already retired and comfortable with your status, you probably have already gone through at least an informal preretirement planning process. If you feel that you are not satisfied with your situation, you can make changes to improve it.

Planning a Successful Retirement

What kind of lifestyle and what kinds of activities do you envision for your retirement years? Would you like to rest, develop a hobby, travel, or start a second career? Would you prefer to move or to continue living where you are? To help answer these questions and others, analyze your long-term retirement goals. Once you have set these goals, you are ready to estimate their costs and decide whether or not your projected retirement income will be sufficient.

Decide When To Retire

The age at which you will retire depends largely on the age at which your pension benefits begin. You may also want to postpone retirement until after your large debts are paid off and your children have finished their education. An early retirement can be costly. Although you can collect Social Security benefits as early as age 62 (age 60 if you are a surviving spouse), these benefits are permanently reduced when you collect them before age 65. You are not eligible for medicare until age 65 unless you become disabled and receive disability checks for at least 2 years. If you are no longer covered by your company's health insurance program, you may find health care extremely expensive between the time of an early retirement and age 65.

If you will be collecting a private pension, the amount you receive may be reduced with an early retirement. Since pension benefits are often based on the average of the top 5 years of salary, an early retirement could reduce the number of high-earning years on which your pension is figured. Legislation has made it easier for you to delay your retirement, prohibiting employers from forcing most employees to retire because of age before age 70 and eliminating mandatory retirement for most Federal employees.

Estimate Retirement Income

To maintain your level of living after retirement, low-income earners will need to replace 75 to 85 percent of preretirement earnings, middle-income earners need to replace 60 to 70 percent, and high-income earners need to replace 45 to 55 percent. Married couples should add about 5 percentage points to these replacement ratios. Most retirees have more than one source of income. Generally, the more sources of income you have as a retiree, the more likely you are to have adequate income. Table 1 lists the major sources of retirement income along with the advantages and disadvantages of each. Use worksheet 1 on page 3.23 to tabulate your retirement income. Do not forget to inflate incomes or investments that increase with the cost of living (such as Social Security) to what they will be when you retire. Table 2 on page 3.4 provides inflation factors you can use.

Social Security. Social Security is the most widely used source of retirement income. Benefits are based on how long you worked, how much you earned, your age at retirement, whether your job was covered under Social Security, and whether you work after retirement. If you are a dependent of a worker who was covered under Social Security, or if you are disabled, you may also be eligible for Social Security benefits.

While you are contributing to Social Security, you may want to check your record of earnings for accuracy every few years. This is especially important if you have changed jobs frequently. If you are age 56 or older, you can also ask for an estimate of what your retirement benefits will be at retirement age. If you are eligible for Social Security, you may collect monthly retirement benefits at age 62 or older (or disability benefits at any age if a severe disability prevents you from working for a year or more). The retirement age for full benefits will gradually increase to 67 between the years 2000 and 2027.

Social Security benefits are not paid automatically. You must file an application when you have decided when you will retire. Phone or visit any Social Security office about 3 months before retirement to file your application. Take proof of your age and a record of your most recent earnings (such as a W-2 statement or tax return).

Social Security benefits are protected against inflation. Benefits automatically increase in January whenever living costs (or wages in some cases) climb 3 percent or more in a previous year.

Other public pensions. The Federal Government administers several other retirement plans for Federal Government and railroad employees. The largest of these is the U.S. Civil Service Retirement System. The Veterans' Administration provides pensions for many military retirees and survivors of men and women who died while in the Armed Forces, as well as disability pensions for eligible veterans. The Railroad Retirement System is the only retirement system administered by the Federal Government for a single private industry. Many State, county, and city governments operate retirement plans for their employees. To learn more details about each retirement system, contact the appropriate administering agency.

Private pension. Another source of retirement income for you may be the pension plan offered by your company. About half of all workers are covered by such plans. Private pension plans vary, so you will need to go to your company's personnel or union

Table 1. Major Sources of Retirement Income: Advantages and Disadvantages

Source	Advantages	Disadvantages
Social Security:		
In planning	Forced savings. Portable from job to job. Cost shared with employer.	Increasing economic pressure on the system as the U.S. population ages.
At retirement	Inflation-adjusted survivorship rights.	Minimum retirement age is specified. Earned income partially offsets benefits.
Employee pension plans:		
In planning	Forced savings. Cost shared or fully covered by employer.	May not be portable. No control over how funds are managed.
At retirement	Survivorship rights.	Plans may not provide cost-of-living increases on a regular basis.
Individual saving and investing (including housing, IRA's, and Keogh plans):		
In planning	Current tax savings (e.g., IRA's). Easily incorporated into family (i.e., housing). Portable. Control management of funds.	Current needs compete with future needs. Penalty for early withdrawal (IRA's and Keogh's).
At retirement	Inflation-resistant. Can usually use as much of funds as you wish, when you wish.	Some sources are taxable. Mandatory minimum withdrawal restrictions (IRA's and Keogh's).
Post-retirement employment:		
In planning	Special earning skills can be used as they are developed.	Technology and skills needed to keep up may change rapidly.
At retirement	Inflation-resistant.	Ill health can mean loss of this source.

office to learn the specifics of your plan. Find out:

- When you will become eligible for pension benefits.
- What benefits you will be entitled to.
- What happens to your pension if you change jobs or die before retirement.

IRA. Individual Retirement Accounts (IRA) have been available since 1975 to workers not in employer retirement plans. The Economic Recovery Tax Act of 1981 opened eligibility to everyone with earned income. You can now contribute up to $2,000 of your earnings into an IRA each year. This figure is $2,250 for a couple with one employed spouse and $4,000 for two-earner couples. Your IRA contribution may be tax deductible. No taxes are due on account earnings until you begin withdrawing funds at retirement—presumably when you will be in a lower tax bracket. You may not withdraw funds before age 59½ without substantial loss of benefits unless you are disabled or switching to another IRA plan, and you must start withdrawing funds no later than age 70½. Banks, credit unions, savings and loan associations, insurance companies, mutual funds, and brokers all offer IRA plans of various merit.

Table 2. Inflation Factor Table

	Estimated annual rate of inflation between now and retirement									
Years to retirement	4%	5%	6%	7%	8%	9%	10%	11%	12%	13%
5	1.2	1.3	1.3	1.4	1.5	1.5	1.6	1.7	1.8	1.8
8	1.4	1.5	1.6	1.7	1.8	2.0	2.1	2.3	2.5	2.7
10	1.5	1.6	1.8	2.0	2.2	2.4	2.6	2.8	3.1	3.4
12	1.6	1.8	2.0	2.3	2.5	2.8	3.1	3.5	3.9	4.3
15	1.8	2.1	2.4	2.8	3.2	3.6	4.2	4.8	5.5	6.3
18	2.0	2.4	2.8	3.4	4.0	4.7	5.6	6.5	7.7	9.0
20	2.2	2.7	3.2	3.9	4.7	5.6	6.7	8.1	9.6	11.5
25	2.7	3.4	4.3	5.4	6.8	8.6	10.8	13.6	17.0	21.1

First, choose from the left-hand column the approximate number of years until your retirement.

Second, choose an estimated annual rate of inflation. This cannot be predicted accurately and will vary from year to year. The 1984 inflation rate was about 4 percent.

Third, find the appropriate inflation factor corresponding to the number of years until your retirement and the estimated annual inflation rate (Example: 10 years, 4 percent inflation, yields a 1.5 inflation factor.)

Fourth, multiply the inflation factor by your estimated retirement income and estimated retirement expenses.
(Example $6,000 × 1.6 = $9,600)
Total annual inflated retirement income $ ____________

Total annual inflated retirement expenses $ ____________

Note: Figures are from a compound interest table showing effective yield of lump-sum investments after inflation. Published in Charles D. Hodgman, Editor, *Mathematical Tables from the Handbook of Chemistry and Physics*. The Chemical Rubber Publishing Company. Cleveland, OH, 1959.

Keogh. If you are self-employed, you can make contributions to a Keogh account by contributing 20 percent of your net earned income, up to $30,000 a year. Keogh plans have the same tax advantages as IRA's. Money can be invested in mutual funds, passbook accounts, stocks, bonds, annuities, certificates of deposit, limited partnerships, or other managed investments.

Annuities. With the exception of straight term, most life insurance polic s have some cash value. Investing in a policy that builds a large cash value is a way of saving for retirement while providing your family with insurance protection. Annuities sold by insurance companies offer the investor a lump-sum settlement or a guaranteed monthly payment for life or for a set number of years. Various annuity options are available. Some pay balances to your beneficiaries if you die before using up your funds; some do not. No income taxes are due on interest earned until the money is withdrawn. The lack of a minimum investment requirement, preferential tax treatment, and the increased rates of return in recent years have made annuities an increasingly popular way to save for retirement. Early withdrawal of retirement annuities (before age 59½) can be costly, not only in contractual penalties but also in income taxes.

Employment. You may be able to work during your retirement to help meet expenses. It may be difficult to use this source of retirement income in future planning. You cannot be sure if work will be available to you several years from now or if you will be healthy enough to work. So unless you are very close to retirement and already have a retirement job set, do not put too much emphasis on this. As you get closer to retirement, include it in your plan. If you are already retired from one job and working at another, of course, you can include this source of income in your plan for as long as you plan to continue working.

Remember that retirement work may reduce your Social Security benefits. As long as you do not earn more than the annually exempt amount, however, your Social Security payments will not be affected. If you do earn more than the annual exempt amount, your Social Security payments will be reduced by one-half the amount over the exemption. (For example, if the exemption is $4,500 and you earned $5,500, your Social Security payment will be reduced by $500.) Beginning in 1990, the rate at which benefits will be decreased will be lowered from $1 for every $2 to $1 for every $3 above the earnings limit of $6,600. After age 70, earnings cause no reduction in your Social Security benefits.

Other income sources. Do not forget any income-producing holdings you may have that will contribute to your retirement income.

Investments—Some investments, such as annuities, interest from savings accounts and bonds, dividends from stocks, and rent from real estate investments, yield a regular contribution to retirement income. Other investments, such as savings bonds or insurance policies, often yield a lump-sum benefit.

Life insurance—Your life insurance may have been set up to provide support and education for your family in case of your death. As you approach retirement, you may want to convert some of this asset into cash or income (an annuity) or cut back on the fa value of your insurance to reduce premium payments. This will give you extra money t pend for living expenses or to invest for additional income. Spend some time learning the retirement possibilities of your insurance.

Real estate—If you own your house, it is probably your biggest single asset. However, the amount of money tied up in your house may be out of line with your retirement income. If it is, you may eventually want to consider selling your house and buying a less expensive one. The selection of a smaller, more easily maintained house can also decrease your maintenance costs. The difference could be put into a savings account or certificates that draw interest or into other income-producing investments. If your mortgage has been largely or completely paid off, you may be able to use a home equity conversion plan to provide extra income during retirement. In this arrangement, a lender uses your house as collateral to buy an annuity, after deducting the mortgage interest payment. The mortgage principal, which was used to obtain the annuity, is repaid to the lender by probate after your death. Home equity conversion plans are fairly new and may not be widely available in your area. Check with your bank or a savings institution about availability and details.

Estimate Retirement Expenses

The exact amount of money that you will need for future expenses is impossible to predict, but you can estimate how some spending patterns will change during retirement. For example, retired households spend a greater part of their income on food, housing, insurance, medical care, gifts, contributions, and leisure activities than younger households and less on clothing, income taxes, and work-related expenses (gas, lunches, and bus fares). List your projected expenses on worksheet 2 on page 3.24.

With inflation, your estimated expenses will not remain fixed between now and your retirement time. Almost everything will cost more. The effect of inflation can be especially severe for retired people who cannot easily increase their income. By using the inflation factors in table 2 on page 3.4, you can approximate what your expenses will be when you retire. You may wish to refigure your inflated retirement income needs several times during the preretirement years, since unforeseen circumstances may change your estimate of inflation or your retirement expenses. Once you retire, use the inflation factor table to help plan ahead.

Determine Additional Income Needs

Compare your estimated retirement income with your estimated retirement expenses. If your estimated income exceeds your estimated expenses, you are in good shape. You probably will want to evaluate your plans every few years between now and retirement to be sure your planned income is still adequate to meet your planned expenses. If, however, your planned retirement income is less than your estimated expenses, now is the time to take action to increase your retirement income or reduce expenses. In addition, if a large portion of your retirement income is fixed and will not increase with inflation, you should make plans for a much larger retirement income to meet your inflating expenses during retirement. Review your investment plans. Decide where you can begin to safely increase your investments to cover all your future needs.

Decide How To Handle Life Cycle Changes

Retirement is a changeable state. Just like your life before retirement, situations will change and you may go through several phases. For instance, you may be in an active phase in the early years of retirement, with a more dependent lifestyle in later years. The active phase of retirement is characterized by good health and independent living. It may be a time for active participation in a new lifestyle, free of the responsibilities of the work years. The dependent phase often occurs in the later years of retirement and usually is characterized by physical or mental limitations and more dependency on others. You can prepare yourself for the various phases of retirement by anticipating health problems or a changed family situation and planning for an adequate financial position to meet these changes.

Health care. Health-related problems increase with age. The rising cost of health care is a major concern of retired persons. Besides the direct cost of medical care, you must plan for the effects declining health will have on you financially in other areas. For example, you may need to hire someone to mow your lawn or do household repair jobs. You may have to change your type of housing--perhaps by living with a relative or staying in a nursing home. You can financially handle health crises if you have adequate health insurance coverage and are aware of the following sources of assistance.

Medicare is a Federal health insurance program. Local Social Security offices take claims and provide information. Almost all people age 65 and older have medicare; so do some disabled people under age 65 and people of any age who need treatment for kidney failure. The two parts of medicare are hospital insurance and medical insurance. The hospital insurance portion of medicare helps pay for inpatient hospital care and for certain followup care after you leave the hospital. Medicare hospital insurance is financed by payroll deductions from employed persons. You are entitled to this hospital insurance if you are at least 65 years old (you do not have to be retired) and are eligible for Social Security or railroad or Federal retirement benefits either as a worker, dependent, or survivor. If you are not eligible for the medicare hospital insurance at age 65, you can buy it, but you must also buy the medical insurance. Applying for your medicare insurance 3 months before your birthday month is a good idea so that you will be protected by the time you reach age 65.

Medical insurance under medicare helps pay for your doctor's services and many other medical items and services not covered under hospital insurance. When you apply for hospital insurance, you will be enrolled automatically for medical insurance, unless you state that you do not want it. If you do choose medical insurance protection, however, you must pay a monthly premium for it. Check with your Social Security office for the latest information on eligibility, monthly premiums, and benefits of medicare.

Medicaid, a Federal-State health insurance program, provides health care for eligible needy and low-income persons. Contact your county Department of Public Welfare for details. Medicaid can pay what medicare does not pay if you are eligible for both programs.

Wills. If you own a house, car, personal property, bank account, real estate, or insurance you should have a will to designate how your belongings will be used, distributed, or divided after your death. A will can provide for the welfare of your survivors, ensure that your wishes are carried out, and avoid conflicts. A will allows you to name guardians for your dependent children and to appoint an executor who will see that your wishes are carried out. Your spouse, children, and other family members may be affected by your will, so you may want them to be aware of your wishes. Have an attorney draw up the will for you and help you adjust it as your circumstances change. Let someone know where your will is kept. If your assets are very large, a will may not adequately meet your needs. Consider developing an estate plan to distribute your estate and minimize Federal and State taxes. Because estate laws are complicated, it is best to get expert advice from a lawyer who specializes in this area.

Chapter 2

Economic Conditions

Families often need to alter their living and spending habits in response to changes in the economy such as increased inflation and revisions in the tax laws.

Inflation

When you notice that it costs more today than before to purchase the same goods or services, you are probably experiencing the effects of inflation. Inflation can be caused by many factors, including increased consumer spending, government deficits, and energy demands; declining worker productivity; and high wage levels. The Consumer Price Index (CPI) is a Federal measure that reflects changes in the prices that consumers pay for goods and services. The CPI is the most widely quoted method of measuring inflation. Weighted averages of the cost of a market basket of several hundred consumer items such as food, clothing, and automobiles are used to determine the CPI.

The high rates of inflation common during the late seventies and early eighties affected everyone—especially households with low, moderate, or fixed incomes. Many households learned to cope with inflation by working additional hours; bargain hunting; cutting back on expensive clothing, food items, and entertainment; and by doing home, auto, and other repairs themselves. Certain byproducts of high inflation may have given some households a false sense of economic growth and well-being. For example, interest rates on investments were high and wage and pension increases, which are sometimes based on the CPI, were up. Also, inflationary times were considered a good time to acquire debt since the loan is repaid in "cheaper dollars" (dollars that buy less). If you borrowed heavily and depend on high investment income, you could very well experience a financial pinch as inflation rates lower.

Low or declining rates of inflation are sometimes referred to as "disinflation." Disinflation has been characterized by stable prices, falling interest rates on loans and investments, and slow appreciation (or depreciation) on fixed assets such as housing. Most families benefit from disinflation.

Comparing your increase (or decrease) in income against the current CPI is one way to get a rough idea of how inflation is affecting your buying power. If, for example, your income has increased by 4 percent over the last year but the CPI has increased more than 4 percent, you will probably have to make some adjustments to your spending plan in order to maintain your level of living. If, however, your income has increased more than inflation, you will want to plan on how to spend or save your extra income.

When taking inflation into consideration, it is not easy for the small investor to find a safe saving or investment plan that will keep pace with high inflation or that will provide a satisfactory return during low inflation. When regular bank passbook savings accounts pay an annual interest rate of 5½ percent and when inflation rises more than 5½ percent, money kept in these accounts loses purchasing value. Short-term securities, bonds, and certificates usually do a better job in matching and sometimes surpassing the inflation rate. During periods of disinflation, interest paid on these investments may also decline. However, investigate carefully before investing in high-risk instruments that promise high yields. Review Chapter 1 in Section II—Financial Tools Used in Money Management—for more on investments.

Taxes

Anyone with income over a certain amount must file a Federal income tax return, usually by April 15 of each year. This includes minors and aliens. If you have overpaid taxes and want to get a refund, you must file a return even though your income is under the stated limit.

Most workers have taxes withheld from their paychecks and only think about tax-savings techniques when it is time to file. Some people pay more taxes than they have to. Careful, year-round tax planning may save you money.

Federal income tax laws are complex and change frequently. Your first job in minimizing taxes is to stay well informed. The Internal Revenue Service (IRS) has many free and low-cost publications about the latest regulations and filing techniques. Once you are aware of current regulations, you can begin a plan of reducing your taxable income.

Exemptions are items for which specified amounts can be subtracted from your gross income. You are allowed an exemption for yourself and spouse, if filing jointly, and for each dependent.

Deductions are expenses which you can subtract from income, such as:

- Medical expenses—a portion of doctor and dental fees, prescriptions, transportation to the doctor, and health insurance premium payments.
- Taxes—Income, property, and sales.
- Contributions to charities—in the form of cash or items.
- Interest—paid on mortgage loans.

Credits can help minimize taxes. These are subtracted from the amount of taxes you are due to pay and include such things as a portion of your child care expenses.

Another important technique of tax planning is to know when to seek competent, professional help. This may be a tax preparer, accountant, lawyer or IRS representative.

Financial Conditions

The condition of the economy has a direct impact on your personal financial condition. For example, if national unemployment is high, you may have trouble finding a job; if the economy is in a slump, your income may not increase as much as you would like. Some people who are unemployed or have low, fixed, or irregular incomes find it hard to manage financially.

Low and Fixed Incomes

Fortunately, few persons have completely fixed incomes. Most elderly persons receive Social Security or other pensions that have cost-of-living increases. However, these increases may not provide enough for some people to live comfortably.

Other types of people, too, may find that their income does not provide adequately for family needs. If you are in this situation, first consider how to increase income. You may need to change jobs, take a second job, or have additional members of your household find employment. You may also qualify for some public assistance. Cashing in some of your assets may be a solution. Elderly people, in particular, may find it beneficial to convert their houses to cash.

Unemployment

Part of the income lost by unemployment may be replaced through various compensations. For most people, however, unemployment means reduced economic well-being. However, serious financial hardship is not always a consequence of temporary unemployment. For a two-earner household with a good emergency fund, for example, the temporary loss of one income may not seriously reduce their level of living. Therefore, during times of economic plenty you may want to prepare your household with an adequate emergency fund. Budgeting wisely is especially important when you are unemployed. You probably will have to reanalyze your situation and set new priorities.

Find temporary income. To get money to tide you over until you find work, you may want to:

- Apply for unemployment compensation through your State Employment Agency.
- Take money from a savings account or an investment.
- Cash in or borrow from a life insurance policy.
- Apply for public assistance
- Borrow from family or friends.

Contact your creditors. Contact creditors right away. Let them know that you are out of work and may need to make special arrangements for paying bills. Most creditors are willing to adjust payments if you will be honest with them. They may allow you to delay payments or pay only the interest on the loan for a while. They may rework the loan to allow for lower payments.

Decide which creditors to pay first. You can decide more easily if you know what will happen if you do not pay. Review your loan contracts to find the answers to these questions:

- Is there a penalty for late payments?
- Can a lender demand full payment once the loan terms are broken?
- Is there a grace period before action is taken against you?
- Can the lender repossess?
- When can the lender foreclose?

Keeping a roof over your head is a basic concern, so you will most likely want to pay your *mortgage or rent payments* first. If you are in default on your mortgage and you hold a VA loan (one insured by the Veterans' Administration) or an FHA loan (insured by the Federal Housing Administration), be aware that both of these agencies have a mortgage assistance program for persons who cannot make payments for reasons beyond their control. Check with VA or FHA to see if you qualify. Make payments on *utility bills*. It is very easy for these companies to cut off your service, and it may be expensive to get it back. If you cannot pay your utility bills, call the company and explain your reasons. They may allow you to pay overdue bills in installments or they may change your due date to the same time of month that you receive income. Think about paying your *automobile loans* next since your vehicle may be repossessed if you do not. Then consider *insurance premiums*. You will especially need to keep up health and automobile insurance. Call your insurance companies. There are probably ways to cut premiums. Pay your *credit card bills* or other obligations, starting with those that charge the highest interest rate, as soon as you can. These creditors usually will not take immediate action against you. Before then, you may be working again.

Cut your expenses. You probably will have to adjust to living on less while unemployed. It is therefore necessary to cut expenses.

Set priorities. You may need to change your priorities. Decide what are "needs" and what are "wants," what can be cancelled or delayed, and what you must do to survive until the crisis is over.

Irregular Incomes

If you are a farmer, seasonal worker, self-employed person, salesperson working on a commission, or anyone with an income that goes up and down, you have a special budgeting problem. A good spending plan will help stretch your money. It will allow you to have funds available when needed.

Begin by estimating your income. You can base this on your last year's income and current prospects, or you can make an educated guess for a month or two. Remember, it is better to estimate too low than too high. As each month passes, compare your estimated income to your actual expenses and adjust your spending plan accordingly. Time your expenditures to coincide with your income as much as you can. For example, if you are a seasonal salesperson and know that your peak sales occur in the summer, then you may want to arrange for your insurance premiums to come due during that time. If your income fluctuates sharply, play it safe by making two estimates. Work out the smallest and largest figures you can reasonably expect. Plan first on the basis of the low-income figure; then consider how you will use additional amounts. On those occasions when income is high and expenses are low, put more money into your savings plan. When income is lower, you will have that extra savings to fall back on until income goes up again. It is also a good idea to have a good source of credit available to use when necessary.

Changing Household Conditions

American households are changing. The number of family households with a husband, wife, and children has decreased over the last decade. Today there is a growing number of single-parent and nonfamily households (those maintained by a person living alone or with others not related). There is also a growing number of unmarried adults living with parents. Similarly, the number of elderly persons maintaining their own household is increasing. Overall, households today are smaller than in the past.

Each household has certain characteristics that make it unique from others and certain characteristics that make it similar to others. The chart on page 3.25, Household Matrix, shows the similarities and dissimilarities in household budgeting goals and the financial tools many families and individuals use to obtain the goals. This chart helps to explain how these goals and tools change as the household progresses through the life cycle, and how different types of households may provide in different ways for the same goal.

The chart is set up by type of family. It begins with young singles and ends with retired couples. In between there are young families and middle families, with children and without. Find your household type and the goals that are typical at your stage of the life cycle. Now look down the left column. Are you using appropriate financial tools, such as investments, credit, and insurance, to meet your goals?

Case Studies

The following case studies provide examples of how households can use budgeting and other money management skills presented in this publication to meet the goals they have set for themselves.

Case #1—single person. Christopher Martin is a 22-year-old recent college graduate in business administration. Even though the job market was tight when he graduated, he was able to get a good job as a management trainee with a local bank. This job has an excellent future, but the starting salary is modest. Christopher, therefore, continues to live at home with his parents, but he wants to save enough money to rent and furnish an apartment.

It is not easy for Christopher to save. He already has several debts, including an educational loan and a bank loan for the purchase of a car. Like many young people, a large portion of Christopher's salary goes toward entertainment, movies, concerts, weekend dates, personal development, and clothing.

Christopher's main goal is to get a place of his own. He has decided that the only way to save enough to rent an apartment is to set up a budget and stick to it. After keeping track of his expenses for several weeks, Christopher can see why he was having problems saving money. This is Christopher's current monthly spending pattern:

Income (after taxes, Social Security, retirement and health insurance	$ 732
Expenses:	
Educational loan	80
Bank loan	150
Contribution to parents' household	100
Lunches	50
Clothing	75
Entertainment	75
Personal care	30
Gas, oil, insurance, and car maintenance	120
Bank savings	40
Total expenses	$ 720

Christopher decides to cut down on his clothing and entertainment expenses and contribute more toward his savings goal. Reallocating his money this way will allow him to have enough money in about 6 months to cover the initial costs of moving. Christopher's parents have promised to let him use their old furniture stored in the basement until he can afford to buy his own.

Also in 6 months Christopher will have been employed at the bank for 1 year and will be due a substantial raise. Christopher can see, however, that even the raise and cutting expenses will not allow him to afford rental payments that run about $300 a month in his area. He decides to investigate the possibility of sharing an apartment with a close friend.

Case #2—single parent. Karen Taylor is a 27-year-old single parent. She and her 4-year-old son, Brian, live in a small two-bedroom apartment. Since graduating from high school, Karen has been employed as a secretary for an insurance company. Brian stays at a day-care center while Karen works.

Karen finds it very difficult to maintain a home for herself and her son on her $13,000 salary. She is often forced to borrow money from her parents. She has a small Christmas savings account in the company's credit union, a $5,000 term life insurance policy, and a $2,000 debt with a local furniture store.

Karen currently has two major goals: (1) To increase her income, and (2) to protect her income should she become unable to work. She approached her employer to find out how she could progress upward in the company. She found out that her company has a special upward mobility program for employees who have been with the company at least 5 years. Interested employees could be given company-paid, on-the-job training and college courses to learn one of several jobs. Karen quickly applied for such a position as a computer operator. Within several months she was able to secure an entry level computer position and the accompanying raise in salary.

Karen then turned her attention toward protecting her income and also providing for Brian's future education. She bought a $25,000 term life insurance policy on herself which has a disability rider that will pay her if she becomes disabled and cannot work. Karen has always had problems sticking to a savings plan—withdrawing money as quickly as she deposited it. So she decided to take out a $5,000 endowment policy on Brian that will come due when he is 18 and contribute to his college education. This will also ensure that he always has life insurance protection as long as premiums are paid.

Case #3—young couple. This first year of marriage is often a difficult period for young couples. It takes time for two individuals of different personalities and values to adjust to one another. This period of adjustment has been especially hard for Barbara and Jeff Donaldson. Things seemed to go wrong from the beginning. Jeff, a warehouse foreman, was laid off from work 6 months after they were married, and Barbara felt suddenly burdened with having to support them both with her job as a store manager. They also neglected to discuss several important decisions:

- Who will earn the income?
  Barbara thought that she would be able to quit work and stay home after they had built a small savings. She resents being the only worker in the family.
- What kind of home will they establish?
  As soon as Jeff returns to work, he wants them to start looking for a house—this would mean that Barbara would have to continue working for several more years.
- Will they have children? When?
  Barbara would like to have children right away; Jeff wants to wait.
- What are their immediate, intermediate, and long-term goals?
  They both agree that the most immediate goal is for Jeff to find employment—after that

there is little agreement.

- Who should handle the money?
  Since she earns the money, Barbara wants to decide how it is spent. Jeff feels it should be a joint decision.

Creditors are beginning to bother the Donaldsons since Barbara's salary and Jeff's small unemployment check are not enough to cover the rent on their large apartment, payments on two cars, utilities, food, clothing, entertainment, and several credit card bills.

The Donaldsons need help both with adjusting to their marriage and straightening out their finances. They seek professional advice on both accounts. They begin seeing a marriage counselor who helps them work through their power struggle and differences—helping them to understand that compromises are needed on both sides. They also consult a credit counselor who contacts their creditors and makes arrangements for them to pay a lower amount on their bills until Jeff is working again. The Donaldsons still have a long way to go in establishing good money management habits, but they now feel that they can discuss and work through their problems.

Case #4—young family. Kyle and Janice Reading have been married about 5 years. This is the second marriage for both. They have two children living with them—3-year-old Justin and 7-year-old Rene, a child from Janice's first marriage. Kyle also has another child from his first marriage, 10-year-old Kevin, who spends most weekends with Kyle and Janice.

Janice is a housewife who was employed as a secretary up until Justin's birth. Kyle is an auto mechanic. Here is how the Readings' income is broken down monthly:

Kyle's job (after taxes, retirement, Social Security, and health insurance)	$ 1,428
Child support from Janice's first husband	250
Total net income	$ 1,678

Both Kyle and Janice feel that financial problems contributed to the breakup of their prior marriages. This time, therefore, they are proceeding cautiously—making few debts and saving as much as they can. They currently have no debts and over $5,000 in savings.

Over the past year they have had two important financial decisions to consider: (1) Should they buy a house, and (2) should Janice return to work?

A new townhouse development built near where the Readings currently live was very appealing to them. From talking to the real estate agent and people already living in the development, this is how much Janice and Kyle estimated it would take in monthly housing costs to own one of the townhouses:

Mortgage principal and interest, property taxes, and insurance	$ 750
Gas	85
Electric	50
Telephone	20
Maintenance and repairs	30
Decorating	20
Total new housing expenses	$ 955

The Readings' other monthly expenses total as follows:

Food	$ 470
Clothing	100
Medical (not including insurance)	35
Personal care	35
Gas and oil for car	140
Recreation	50
Gifts	20
Car and life insurance	60
Savings	100
Child support to Kyle's first wife	300
Total other expenses	$ 1,310

With the new house, the Readings' monthly budget would total $2,265—$587 more than their current income. This was the incentive that Janice needed to justify returning to work. But could she make enough money to make returning to work worthwhile? After searching for several months, Janice was offered a position as a secretary at the nearby university. Net salary for the job is $967 per month. Here is how Janice determined that accepting the job would enable them to buy the house:

Monthly net salary	$ 967
Work-related expenses:	
Child care	200
Bus fare	40
Additional clothing	20
Lunch and coffee breaks	40
Added household expenses (more eating out and convenience foods)	20
Miscellaneous (office collections, etc.)	10
Total work expenses	330
Work income	967
Work expenses	-330
	$ 637

After the work-related expenses Janice would have $637 to contribute to the household budget.

Case #5—middle family. Dennis Blake is a farmer. His small farm has been in Dennis' family for three generations. In the past the farm has provided a good living for the Blakes. However, poor weather conditions and poor price levels have caused profits to decline. Dennis has to do most of the work alone. His family helps out whenever they can—mostly in the evening or on weekends. Conditions are beginning to improve and if they can be cautious, Dennis feels that they will again see rising profits.

When profits started to decline several years ago, Marie (Dennis' wife of 25 years) took a job as a nurse's aid at a nearby nursing home. Dennis and Marie have three children—Marcy, 22; Dennis, Jr., 17; and Gregory, 15. Expenses are high for the Blakes. Marcy is getting married this summer. She has been working part time and attending school part time, and hopes to continue this schedule after she is married. She has managed to save a small amount of money for her wedding, but she and her mother estimate that the family will have to contribute about an additional $2,000 toward the wedding expenses. Dennis, Jr., will start college in the fall. He will work part time while in school but will not have enough money saved to help out with his tuition for at least a year. He estimates that he will need about $5,000 for his first year at college.

Marie does all of the accounting for the farm business and the household expenses. Budgeting for expenses with the variable income that the farm provides has not always been easy, but she has managed to keep all their farm accounts in good standing and their personal savings at around $9,000. She thought they would be able to pay for Marcy's wedding and Dennis, Jr.'s first year tuition without depleting their savings—until their truck quit and required replacement. Dennis figures that he will need an additional $8,000 for a new one. He would like to borrow it from the household savings instead of taking a loan, since they already have a sizable loan with the bank. Suddenly the Blakes are faced with a big decision—what has priority, Marcy's wedding and Dennis' tuition or the truck?

Marcy and Dennis, Jr., are concerned about putting so much financial strain on their parents. Dennis, Jr., contacts the university and applies for a student loan that he can repay after he graduates. Marie remembers a whole life insurance policy that they purchased on Dennis many years ago. This policy now has a substantial cash value. They decide to borrow the $2,000 for Marcy's wedding against this policy and use the household savings to help purchase the new truck.

Case #6—older couple. Margaret and Stuart Maxwell are both public school teachers within 12 years of retirement. The Maxwells have no children. They are at the point in their lives they had always dreamed of reaching—their income is high and their living expenses are low. Their house is paid for and they have additional assets totaling over $25,000. Including both salaries and dividends from some stock, their yearly income is about $65,000. The Maxwells are now finding, however, that taxes are taking a very large part of their income.

The Maxwells have always used debt wisely, paying off one large debt before incurring another. They currently have one loan with a balance of $5,000 taken out several years ago to do some remodeling on their house. The Maxwells also give financial assistance to Margaret's mother, who lives with them and whose only other income is Social Security and a small pension. They enjoy entertaining and vacationing and spend a lot of money on leisure activities.

Stuart and Margaret Maxwell have four main financial objectives:

- Minimizing taxes.
- Caring for Margaret's mother.
- Saving for retirement.
- Providing for entertainment and vacations.

The Maxwells visited a certified financial planner to discuss how best to reach their financial goals. The financial planner recommended that they:

- Sign up immediately for an IRA. (Since both are working, each can invest $2,000 per year.)
- Purchase tax shelter retirement annuities available to teachers.
- Claim Margaret's mother as a deduction on their income taxes, as well as deducting her medical and other deductible expenses (since they provide more than 50 percent of her support).
- Invest $10,000 in tax-free municipal bonds being sold to fund a city hospital.

Case #7—older single. Helen Washington, 66, a resident of the suburban area of a large eastern city, lives alone in the house that she and her husband bought when they were first married. She has three adult children, all living in other parts of the country. Helen's income is modest—she works as a sales clerk in a department store. She took this job soon after her husband's death. She found that she could not support herself and her teenage son, the only one of her children still living at home then, on the insurance and Social Security benefits left by her husband.

Helen has found it increasingly difficult to maintain her large house. The cost of heating and cooling her home has increased, and she must pay for minor repairs and yardwork. Helen spends most holidays and vacations with one of her children. As she gets older, however, she finds that she is quite lonely and misses her children and grandchildren.

Helen will retire soon. She has three financial goals: (1) To maintain enough income to support herself after she retires, (2) to have enough savings to meet emergencies, and (3) to eliminate some of the expense and responsibility of maintaining a large house.

Helen's daughter, Janet, has been trying for several years to get her mother to move in with her and her family. Helen has resisted until recently, afraid of losing her independence and becoming a burden. Now that Janet is divorced and could use day-to-day help with her two children, Helen begins to reconsider. She realizes that by moving in with Janet she could sell her house and use the money for savings and living expenses. However, after careful thought, Helen finds that she is reluctant to sell her house in case the living arrangement with her daughter does not work out. Instead, she arranges for a real estate company to find tenants, manage the property, collect the rent, and mail it to her (minus their fees) each month.

Helen also knows that this is an important time for her to review and update her will so that her property will be handled according to her wishes should she die or become unable to handle her own affairs. Because of the decreased expenses resulting from sharing her daughter's household and the prospect of income from rent and Social Security, Helen is looking forward to retirement.

Case #8—older couple. Frank Kramer, 72, and his wife May, 70, had both been retired for several years. They lived modestly on their income from a private pension and Social Security. From this income they had managed to put aside a good nest egg to help them through emergencies and any other large unplanned expenses. The Kramers enjoyed their active retirement years, spending time traveling and participating in the many activities available for the elderly in their community. They also realized that if they wanted their income and savings to support them throughout retirement, they would have to carefully budget their income.

About a year ago, Frank suffered a heart attack and was hospitalized for several weeks. Medicare paid for most of Frank's medical expenses, but the Kramers had to use their savings to pay a sizable portion. Frank's health has improved a great deal since then, but his increased medical expenses have caused the Kramers to have to cut expenses. They are very concerned about not having much savings now and having to stop many of their activities because of a lack of money. The Kramers want to find a way to replace the money they had to use for Frank's medical bills.

After several months and much discussion, the Kramers decide to acquire a home equity conversion plan. Under this plan they agree to turn over the future appreciation of their $75,000 debt-free house to the bank. In return they receive a loan, paid to them in monthly installments, at an annual percentage rate somewhat lower than current rates. They will continue to live in the house and receive payments of about $300 per month. After their death, the house will be sold to pay off the loan and the appreciation owed to the bank.

Retirement Planning

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U.S. Department of Labor, Labor-Management Services Administration. *How Breaks in Service Can Affect Your Pension Benefits.*

_________. *How Pension Benefits Are Earned.*

_________. *How To File a Claim For Your Benefit.*

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_________. *What You Should Know About the Pension and Welfare Law.*

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U.S. House of Representatives, Select Committee on Aging. *A Guide To Planning Your Retirement Finances.* Committee Publication No. 97-354. 32 pp.

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U.S. Department of Health and Human Services, Social Security Administration, Health Care Financing Administration. *A Brief Explanation of Medicare.* SSA No. 05-10043. 18 pp.

_________. *Guide to Health Insurance for People With Medicare.* HCFA-02110. 4 pp.

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Federal Reserve Bank of New York, Public Information Department. *The Story of Inflation*. 23 pp.
Federal Reserve Bank of Philadelphia, Public Services Department. *Steering a Course Between Inflation and Unemployment*. 15 pp.

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__________. *Should You Choose a Tax Preparer*. 4 pp.
Internal Revenue Service. *Child and Disabled Dependent Care*. Publication 503. 12 pp.
__________. *Credit for the Elderly*. Publication 524. 12 pp.
__________. *Disability Payments*. Publication 522. 8 pp.
__________. *Educational Expenses*. Publication 508. 4 pp.
__________. *Investment Income and Expenses*. Publication 550. 28 pp.
__________. *Tax Benefits for Older Americans*. Publication 554. 48 pp.
__________. *Tax Information for Divorced or Separated Individuals*. Publication 504.
__________. *Tax Information for Homeowners*. Publication 530. 8 pp.
__________. *Tax Information for Unemployment Compensation*. Publication 905. 1-page pamphlet.
__________. *Taxpayers Guide to IRS Information and Assistance*. Publication 910.
__________. *Your Federal Income Tax*. Publication 17. 168 pp.

Low Income and Unemployment

U.S. Department of Housing and Urban Development. *Avoiding Mortgage Default*. HUD-426-PA(5). 1-page pamphlet.

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Over 200 free or moderately priced consumer publications are available from the Consumer Information Center. To obtain a free catalog, write to: Catalog, Pueblo, CO 81009.

The U.S. Government Printing Office sells over 15,000 Federal publications. Many titles of consumer interest are listed in Subject Bibliography No. 2, *Consumer Information*. To obtain a free copy, write to the Superintendent of Documents, Government Printing Office, Washington, DC 20402.

Worksheet 1: Retirement Income

	Income per year	
Source	**In current dollars**	**In inflated dollars**
Social Security		
Other public pension		
Private pension		
Employment		
IRA, Keogh		
Investment dividends and interest		
Life insurance and annuities		
Real estate		
Other		
Total income		

Worksheet 2: Retirement Expenses

	Now		Retirement	
Item	**Per month**	**Per year**	**Per month**	**Per [illegible]**
Fixed:				
Rent or mortgage payment				
Taxes				
Insurance				
Savings				
Debt payment				
Other				
Total Fixed				
Flexible:				
Food and beverages				
Household operation and maintenance				
Furnishings and equipment				
Clothing				
Personal				
Transportation				
Medical care				
Recreation and education				
Gifts and contributions				
Other				
Total Flexible				
Total Expenses				

3.25 **Household Matrix**

Household Matrix

Budgeting Goals — Household Type

1. Singles

Financial Tools		Personal development	Personal care	Financial independence	Establish credit	Protect income	Adequate housing
Liquid assets			●		●		
Investments							
Credit	Installment				●		
	Mortgage						
Insurance	Life						
	Annuities						
	Health		●				
	Disability					●	
Employment		●		●			
Raise or changing jobs							
Housing	Renting						●
	Buying						
	Equity						
Retirement planning							
Wills							
Money management skills							

2. Single Parents

Financial Tools		Childcare & education	Increase income	Reduce expenses	Childcare if you die
Liquid assets					
Investments		●	●		
Credit	Installment				
	Mortgage				
Insurance	Life	●			●
	Annuities				
	Health	●			
	Disability				
Employment					
Raise or changing jobs			●		
Housing	Renting				
	Buying				
	Equity				
Retirement planning					
Wills					●
Money management skills				●	

3. Young Couples

Financial Tools		Divide financial obligations	Purchase durables	Financial consequences of children	Reduce taxes	Adequate housing	Future goals
Liquid assets			●				
Investments					●		●
Credit	Installment		●				
	Mortgage				●	●	
Insurance	Life						
	Annuities						
	Health			●			
	Disability						
Employment							
Raise or changing jobs							
Housing	Renting						
	Buying				●	●	
	Equity						
Retirement planning							
Wills							
Money management skills		●		●	●		

4. Young Families

Financial Tools		Adequate coverage	Removal of debt	Growing expenses
Liquid assets			●	
Investments				
Credit	Installment			
	Mortgage			
Insurance	Life	●		
	Annuities			
	Health			
	Disability			
Employment				
Raise or changing jobs				●
Housing	Renting			
	Buying			
	Equity			
Retirement planning				
Wills				
Money management skills			●	●

5. Middle Families

Financial Tools		College & weddings	Replace durables	Emergencies	Protect family income
Liquid assets		●	●	●	
Investments		●			
Credit	Installment		●		
	Mortgage				
Insurance	Life				
	Annuities				
	Health			●	
	Disability			●	●
Employment					
Raise or changing jobs					
Housing	Renting				
	Buying				
	Equity				
Retirement planning					
Wills					
Money management skills					

6. Middle Couples

Financial Tools		Reduce taxes	Plan for retirement	Care of aging parents	Entertainment
Liquid assets				●	●
Investments		●	●		
Credit	Installment				●
	Mortgage				
Insurance	Life				
	Annuities		●		
	Health				
	Disability				
Employment					
Raise or changing jobs					
Housing	Renting				
	Buying				
	Equity				
Retirement planning			●		
Wills			●		
Money management skills		●			

7. Older Singles

Financial Tools		Expand health care	Adequate income	Cut expenses
Liquid assets				
Investments				
Credit	Installment			
	Mortgage			
Insurance	Life			
	Annuities			
	Health	●		
	Disability			
Employment			●	
Raise or changing jobs				
Housing	Renting			
	Buying			
	Equity		●	
Retirement planning				
Wills				
Money management skills				●

8. Older Couples

Financial Tools		Cut expenses	Liquidate investments	Protect spouse	Readjust self	Help relatives	Vacations & [illegible]	Preparing fo[illegible]
Liquid assets						●	●	
Investments			●					
Credit	Installment							
	Mortgage							
Insurance	Life		●	●				
	Annuities							
	Health							
	Disability							
Employment								
Raise or changing jobs								
Housing	Renting							
	Buying							
	Equity		●					
Retirement planning								
Wills				●	●			
Money management skills		●						