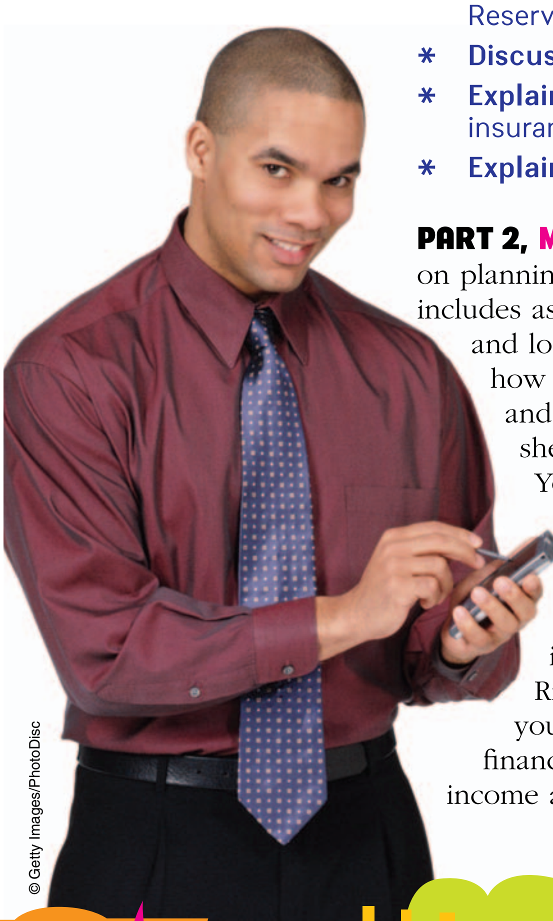
PART 2

Money Management

OUTCOMES

After successfully completing this part, students should be able to:

* **Explain** how resources can limit financial choices.
* **Prepare** a personal income and expense statement, personal balance sheet, and personal budget.
* **Create** a personal financial plan.
* **Prepare** a bank reconciliation and balance a checkbook.
* **List** banking services and fees.
* **Describe** the role of the Federal Reserve System.
* **Discuss** risk management strategies.
* **Explain** provisions of income protection insurance.
* **Explain** coverage for property insurance.



PART 2, MONEY MANAGEMENT, focuses on planning for your financial future. It includes assessing where you are now and looking forward. You will learn how to prepare a personal income and expense statement, balance sheet, budget, and financial plan. You will study banking services and their costs. You will learn how to use a checking account. Keeping good records is an important step in preparing for the future. Risk management will help you to learn to protect your financial resources, including income and property.

CHAPTER 4

Financial Decisions and Planning

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Chapter 4 focuses on the starting point of good money management—assessing your needs and wants. In this chapter, you will learn how your financial resources impact your choices. You will look at where you are now (financially) and prepare a personal balance sheet. You will study strategies you can use to make better financial choices. You will then explore budgeting and create a simple budget. You will learn about budget variances and how to keep good financial records. Finally, you will examine a five-step financial planning process, which begins with setting your personal and financial goals.

Online Resources

Personal Financial Literacy Web site:

- Vocabulary Flashcards
- Beat the Clock: Financial Planning
- Chapter 4 Supplemental Activity

Search terms:

- assets
- financial planning
- fixed expenses
- identity theft
- liabilities
- variable expenses

4-1

Resources and Choices

OUTCOMES

- Explain how basic needs, other needs, and wants differ.
- Describe how limited resources affect consumer choices.
- Prepare a personal income and expense statement.
- Prepare a personal balance sheet.
- Apply a decision-making process to personal financial choices.

MEETING NEEDS AND WANTS

Basic needs include food, clothing, shelter, and medical care. People need these items to survive. People who do not have their basic needs met are not able to provide for other needs or wants. Other needs include things such as more than one pair of shoes, clothing for different purposes,

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A fast, expensive car is a luxury item.

education, or furniture to make life more comfortable. Items to fill some of these needs can be rented instead of purchased. For example, a person can go to a library to borrow books rather than buy them. Other items, such as a washer and dryer, save the owner both time and money as compared to renting their use. While these items are not basic to survival, they are needed to have a comfortable lifestyle.

The term **wants** refers to things people desire for reasons beyond survival and basic comfort. These items allow people to enjoy life more. Examples of wants are new cars, vacation trips, a large wardrobe, dozens of pairs of shoes, and so on. Luxury items, which are very costly, often fill emotional wants rather than physical needs.

Resources Limit Choices

The term **financial resources** refers to money or other items of value that people can use to acquire goods and services. Although their financial resources are limited, wants and needs for many people are unlimited and growing. Every day, new products and services appear to tempt consumers. Because most people do not have enough resources to meet all their needs and wants, people must make choices. For a person who has few resources, the choices available will also be few. This person may need to spend all resources to cover basic and other needs. For a person with more resources, more choices will be available. The amount of money a person has to spend after needs are met is called **discretionary income**. A person who has high discretionary income can consider buying a larger number or higher quality of goods.

Financial Resources

Income is the inflow of money you receive from working, investments, or other sources. You can spend this amount of money without using savings or other assets. **Assets** are money and items of value that you own. Their value is the price you could get if you sold them (for goods, such as a car) or the monetary value (for cash or savings).

Expenses are items for which you must spend money. An income and expense statement lists income received and money spent for expenses for a certain period of time, such as a month or a year. If you have more income than expenses, you have a net income for the period. If you have more expenses than income, you have a net loss for the period. Comparing monthly income and expense statements can help you see whether you are meeting your financial goals. The income and expense statement in Figure 4-1.1 on page 94 shows a net income of $50.00.

Having high discretionary income allows consumers to consider buying expensive products they want.

FIGURE 4-1.1 PERSONAL INCOME AND EXPENSE STATEMENT

ANDREA MCCALL
PERSONAL INCOME AND EXPENSE STATEMENT
April 1-30, 20--

Income		
Work (part-time)	$150.00	
Allowance for doing household chores	40.00	
Lunch money allowance	60.00	
Total Income		$250.00
Expenses		
Gifts	$20.00	
Clothes and shoes	60.00	
Spending money (miscellaneous)	20.00	
Lunches	60.00	
Entertainment	40.00	
Total Expenses		200.00
Net Income		$50.00

A personal balance sheet lists assets you own and their current value on a certain date. The balance sheet also lists debts you owe, called liabilities. A **liability** is any debt that you must repay. The difference between your assets (what you own) and your liabilities (what you owe) is called **net worth**. In the balance sheet shown in Figure 4-1.2, the net worth is $3,351.58.

FIGURE 4-1.2 PERSONAL BALANCE SHEET

JERRY PEREZ
PERSONAL BALANCE SHEET
May 1, 20--

Assets		**Liabilities**	
Cash and checking account	$452.56	Car loan	$1,100.00
Savings account	500.00	Credit card debt	200.98
Savings bonds	300.00	**Total Liabilities**	$1,300.98
Movie collection	100.00		
Computer, iPod, games	300.00	**Net Worth**	
Car, current book value	3,000.00	Assets minus Liabilities	3,351.58
Total Assets	$4,652.56	**Total Liabilities and Net Worth**	$4,652.56

Net Worth

© Comstock Images

Houses may grow in value over time.

Assets that are growing in value are said to be appreciating. Savings bonds and other types of savings will grow over time and will increase in value. The value of land or a house may also increase over time. Other assets, such as cars and electronic items, may be depreciating, or going down in value. These items have temporary value that will be used up over time.

MAKING GOOD FINANCIAL CHOICES

Buying decisions play an important part in managing your money. When you give up a particular benefit or item to get another that you think is more desirable, you are making a **trade-off**. For example, you may choose to buy a music player such as an iPod®. To have enough money to buy the iPod, you must not buy something else that you want. The benefit or item you give up (do not buy) is called the **opportunity cost**. For example, instead of the iPod, you might have bought a bicycle. In this situation, the bicycle is the opportunity cost.

To help you make good financial decisions, use a step-by-step decision-making process.

1. Define the need or problem to be resolved by buying the item or service. For example, you might need access to a computer to use in doing homework and surfing the Internet. Think about all the ways in which the item or service could be used and features it should have to meet your needs.
2. List options for filling the need or solving the problem. For example, you could buy a new computer. You could rent a computer. You could use a computer at a local library. List the cost of each option. Research the features of any items you consider buying.

3. Compare the options you have identified. List the advantages and disadvantages of each one. For example, renting a computer may be more costly in the long term than buying one. Using a computer at the library will be less costly than buying a computer. However, you will have to travel to the library each time you want to use the computer. You can only use the computer during hours the library is open. Think about the opportunity cost of each option.
4. Make a decision based on your research and evaluation of the information you have gathered.
5. Take action based on your decision. For example, buy a computer or plan times to use one at the library.
6. Reevaluate your choices. After some time has passed, think about your decision again. Did the option you chose resolve the problem, or is it filling the need for which it was selected? If the answer is no, or if your needs have changed, follow the process again to make a new decision.

Financial choices you make today will affect your finances tomorrow. If you plan ahead, you will be better prepared to use your resources to fill your needs and wants. Making good financial choices will help prevent worry over financial matters. Follow these strategies to help you make good financial choices:

- Financial choices should be forward-looking. Ask yourself how a choice will affect your future.
- Consider the opportunity cost of each item or service you purchase. Doing so will help you decide whether the item or service selected is the best choice for you.
- When in doubt about whether to buy a particular item or service, do not make the purchase. If you are not sure of a choice, keep asking questions or doing research until you know enough to make a good decision.
- Do not make snap decisions about financial matters. Buyer's remorse occurs when you make a purchase and then later regret it.
- Spend less than your income each month. Set aside money for unexpected expenses.
- Be realistic when deciding which wants you can fill. Learn to enjoy items you have rather than always wanting more items.
- Take enough time to read all financial agreements. Ask lots of questions; be sure you understand what you are agreeing to before you sign a financial document.
- Learn from mistakes that others have made. Listen to the experiences of others to learn about possible financial problems. This will help you avoid the same situations.

Building Communications Skills

Reading Vocabulary

Reading is a basic communications skill. Much of the information people need comes in written form. People read for many reasons. They read to learn new ideas related to school, work, or personal activities. They read directions for doing a task or following a particular route. Many people also read stories, novels, or poems for pleasure.

Your vocabulary is the words you know and understand how to use. Whatever your purpose in reading, improving your vocabulary will help you better understand the material you read. For example, key terms are listed in each chapter of this textbook. Learning these words will help you understand the concepts presented. Use the following strategies to add new words to your vocabulary:

- Try to learn the meaning of a word from the way it is used in a sentence. Then check a dictionary to see if that meaning is correct.
- Divide a long word into parts. If you know the meaning of one part, you may be able to guess the meaning of the entire word. Again, check a dictionary to see if that meaning is correct.
- When you are reading and see a word you do not know, find the meaning in a dictionary at that time, if possible. If you cannot check the dictionary right away, make a note of the word and find it in a dictionary later.
- If you find a word you do not know when reading a textbook, see if the word is defined in a glossary at the end of the book.
- Use new words that you learn in conversation or writing to help you remember the meanings.

4-1 REVIEW

4-1 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. How are other needs different from basic needs? Besides food, clothing, shelter, and medical care, what are some other needs?
2. How are wants different from needs? What are some wants that you have?
3. How do financial resources limit a person's spending choices?
4. What are assets? What are liabilities?
5. How is a person's net worth calculated?
6. What is a trade-off? What is an opportunity cost?
7. Briefly list five steps to follow when making a financial decision.
8. You have given careful thought to buying either a new book bag or a music CD. You decide to buy the music CD. What is your opportunity cost?
9. List some strategies you can use to make good financial choices.

4-1 Activity 2 Personal Financial Statements

Identifying the income, expenses, assets, and liabilities you have now is a good place to begin planning for your financial future. In this activity, you will create a personal income and expense statement and find your net worth or net loss for one month. You will also create a personal balance sheet and determine your net worth.

1. Review the personal income and expense statement shown in Figure 4-1.1 on page 94. Create a similar document using your information. Use spreadsheet software, if available, to create the statement.
2. List all your income—money you receive from any source during one month.
3. List all your expenses—money you pay for goods and services during the same month.

4. Find the total of your income and the total of your expenses. Subtract the two total amounts to find your net income or net loss.
5. Review the personal balance sheet shown in Figure 4-1.2 on page 94. Create a similar document using your information. Use spreadsheet software, if available, to create the balance sheet.
6. List all your assets—money you have or things of value you own.
7. List all your liabilities—money you owe that must be repaid.
8. Subtract your liabilities from your assets to find your net worth. Note that if your liabilities are larger than your assets, you will have a negative net worth.

4-2

Budgeting

OUTCOMES

- Identify the purpose of a budget.
- Prepare a personal budget using the "pay-yourself-first" philosophy.
- Describe recordkeeping methods used in the budgeting process.

THE PURPOSE OF BUDGETING

Budgeting is a critical part of managing your money. The purpose of a budget is to plan how you will spend or save money. A **budget** is a spending and saving plan based on expected income and expenses. It lists expenses and the source of income to pay those expenses. Using a budget allows you to compare your financial resources with your financial needs.

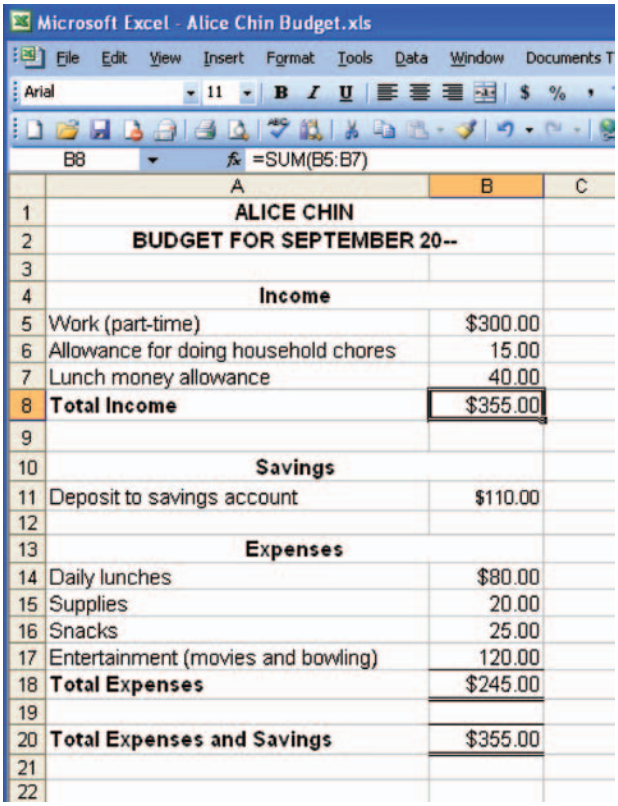
You may need to adjust amounts in a budget several times. Your goal is to create a plan that meets your spending and saving needs with your expected income. Using spreadsheet software, such as *Microsoft® Excel®*, makes adjusting amounts and recalculating totals easy. Using *Excel*, you can record your financial goals and then prepare the budgets that will help you achieve them. A sample budget is shown in Figure 4-2.1 on page 101.

Spreadsheets allow you to insert numbers and then change them later. You can use formulas to compute the amounts of budget variances and the percentage of variances.

Excel also makes changing a budget or a financial plan easy. For example, what if your expenses go up by 8 percent? How will the budget be affected? What if the price of a car you are saving to buy goes up by 10 percent during the time you are saving for it? How much money will you need for the car? Allowing you to answer "what if" questions easily is one of the strengths of a spreadsheet program. When you change a number in *Excel* that is part of a calculation, the result is automatically updated. When you enter a new expense amount, for example, the total expense amount will be updated. Because amounts are calculated using formulas, math errors are eliminated.

BUILDING A BUDGET

A budget should be designed to help meet financial goals such as paying for current expenses and saving for the future. To create a budget, begin by looking at the amount you have available to spend or save. Then



	A	B
1	ALICE CHIN	
2	BUDGET FOR SEPTEMBER 20--	
3		
4	Income	
5	Work (part-time)	$300.00
6	Allowance for doing household chores	15.00
7	Lunch money allowance	40.00
8	**Total Income**	$355.00
9		
10	Savings	
11	Deposit to savings account	$110.00
12		
13	Expenses	
14	Daily lunches	$80.00
15	Supplies	20.00
16	Snacks	25.00
17	Entertainment (movies and bowling)	120.00
18	**Total Expenses**	$245.00
19		
20	**Total Expenses and Savings**	$355.00
21		
22		

FIGURE 4-2.1

Using a spreadsheet will make creating a budget easier.

decide how much of that amount you will save and how much you will spend. You must also choose the items or services for which you plan to spend. Remember that a budget is a plan. Your actual income, saving, and spending may not be exactly as planned. You can compare your actual spending and saving to the budget to see how well you planned. This process will help you create better budgets in the future.

Figure 4-2.2 on page 102 shows a sample budget. Look at each part of the budget as you read the steps for creating a budget in the following sections.

Step 1 Estimate Income

You may have many different sources of income. Whether the money is earned or unearned, you should keep track of where it comes from and how often it is received. Because most budgets are prepared once a year, you should calculate income for an entire year. Locate the total estimated yearly income amount, $2,640.00, in the budget in Figure 4-2.2.

Money you will receive during the year is estimated in a budget. You may receive the money weekly, monthly, yearly, or on some other schedule. No matter when the money is received, it can be accounted for in terms of a monthly budget.

If you receive money weekly, multiply the weekly amount by 4 to see how much that is per month. For example, $10 received per week would be $40 a month. (Rounding is okay as long as your total yearly amount is accurate.) If you get money once a month, you can multiply by 12 to get yearly income. When you look at the big picture—how much money comes in and goes out during an entire year—it may change the way you think about money.

FIGURE 4-2.2 **PERSONAL BUDGET FOR ANDREA MCCALL**

ANDREA MCCALL
BUDGET FOR 20--

	Weekly	Monthly	Yearly
Income			
Work (part-time)	$30.00	$120.00	$1,440.00
Allowance for doing household chores	10.00	40.00	480.00
Lunch money allowance	15.00	60.00	720.00
Total Income	$55.00	$220.00	$2,640.00
Savings			
Deposit to savings account	$5.00	$20.00	$240.00
Expenses			
Gifts	$5.00	$20.00	$240.00
Clothes and shoes	15.00	60.00	720.00
Spending money (miscellaneous)	5.00	20.00	240.00
Lunches	15.00	60.00	720.00
Entertainment	10.00	40.00	480.00
Total Expenses	$50.00	$200.00	$2,400.00
Total Expenses and Savings	$55.00	$220.00	$2,640.00

Step 2 Plan Savings

Pay yourself first—put money into savings before you consider other expenses. If you plan what you want to spend first, you may have no money left for savings. Enter an amount that you would like to save. After entering expenses, you may need to adjust this amount. You might not be able to save as much as you want and still pay for all expenses. Plan to save some money, however, if at all possible. Savings allow you to plan for the future. You can identify items you would like to purchase at a future time with savings. Savings can also be used to pay for unexpected expenses that you may have in the future. Locate the yearly savings amount, $240.00, in the budget in Figure 4-2.2.

Step 3 Estimate Expenses

Expenses are items for which you spend money. Clothes, lunches at school, and bus fares are examples of expenses. You may make payments on an asset you purchase, such as a car. Other expenses are related to living costs and entertainment. Keeping track of what you spend will help you estimate expenses for the future. If you are trying to control expenses, seeing exactly how much you spend for each expense can be helpful. Locate the expense amounts in the budget in Figure 4-2.2.

© Getty Images/PhotoDisc

Eating at a fancy restaurant is entertainment, a variable expense.

VARIABLE EXPENSES

Expenses that can go up and down each month are called **variable expenses**. Examples of variable expenses are food, entertainment, and clothing. These expenses go up or down as you need more or fewer items. For example, when the weather is cold, the heating expense may go up. Expenses can also vary due to changing prices. For example, as the price of gasoline rises, the transportation expense will also rise. Some variable expenses can be decreased when you have less income or higher expenses than expected. For example, you could spend less than planned on entertainment. You can spend more on variable expenses, such as clothes, if you have more income or fewer expenses than expected. For example, if you receive a gift of cash for your birthday, you can use the money to make an unplanned purchase.

FIXED EXPENSES

Expenses that do not change each month are called **fixed expenses**. Examples of fixed costs are rent, insurance, and car payments. Renters typically have a contract that states a monthly rent amount. The rent does not change each month. Although rent and insurance expenses do go up periodically, these increases typically occur on a yearly basis. Monthly car payments are usually fixed for the term of the car loan. Fixed expenses remain constant each month and must be paid even when income is less than expected. If income continues to be less than planned, a fixed expense may have to be eliminated. For example, suppose Terry's income goes down because he loses his job. Terry may have to sell his car and pay off his car loan to eliminate this fixed expense that he can no longer afford.

Step: 4 Balance the Budget

Find the total of each category in the budget—income, savings, and expenses. Find the total of savings and expenses. This amount should be the same as the total income amount. When these amounts are the same, the budget is in balance. Locate the total income, total savings, and total expenses amounts in the budget in Figure 4-2.2.

PREPARING A BUDGET ANALYSIS

A budget is a plan for saving and spending. You should not expect income, savings, and expenses to be exactly as you planned in a budget. Looking at differences between planned income or spending and actual income or spending, called **variances**, can help you plan better when creating budgets in the future.

Technology Corner

Internet Research

Many people use the Internet to do all types of research, from reading about a new medical breakthrough to finding a plumber. One valuable type of research is product and price comparisons. You can look at products for sale and compare their features. You can visit several sellers' Web sites and compare their prices and services offered. This saves you both time and money. You will save time by not driving from one business to another. That saves on gasoline as well.

Internet search engines, such as Google and Yahoo!, allow you to enter keywords and find all types of information. This includes historical facts and data, as well as what's happening in the world today. Keywords should be nouns—persons, places, or things—that are likely to be found on the Web pages you want to view. When the search is complete, a list of links, also called hits, will appear. Clicking a link will take you to a Web page with information related to the search keywords.

Try using keywords, such as *Mall of America*. Look at some of the sites in the hits list and the information that is available to you.

Sometimes you will earn or save more than you estimated. This is a favorable variance. If you earn or save less than you estimated, it's an unfavorable variance. The same is true with expenses. If you spend less money than you planned to spend, this is a favorable variance, but if you spend more than you planned to spend, it is an unfavorable variance. Figure 4-2.3 on page 105 shows budget variances—both in dollar amounts and in percents. To compute the percents for income and savings, subtract the budgeted amount from the actual amount; then divide the difference by the budgeted amount. To compute the percents for expenses, subtract the actual amount from the budgeted amount; then divide the difference by the budgeted amount.

By looking carefully at variances, you can see where you spent more or less than the estimated amounts. Any variance that is more or less than 10 percent of what you had planned should be looked at carefully. For example, Andrea had planned to spend $60 on clothes and shoes for the month, but she actually spent $70. That is $10 more than budgeted, or a 17 percent difference. Andrea should think about why this happened. She may decide that she needs to revise the budget or change her spending habits. Analyzing variances will help you understand and better estimate your income and expenses.

RECORDKEEPING METHODS

Keeping good records will help you prepare a better budget. Good information will also help you do a better job analyzing your budget. There are several methods you can use as you keep track of what you are earning, spending, saving, and investing.

FIGURE 4-2.3 **VARIANCES FOR A MONTHLY BUDGET**

ANDREA MCCALL
BUDGET VARIANCES FOR AUGUST

	Budgeted Amount	Actual Amount	Dollar Variance	Percent Variance
Income				
Work (part-time)	$120.00	$110.00	-$10.00	-8% U
Allowance for doing household chores	40.00	50.00	10.00	25% F
Lunch money allowance	60.00	60.00	0.00	0%
Total Income	$220.00	$220.00	$0.00	0%
Savings				
Deposit to savings account	$20.00	$20.00	$0.00	0%
Expenses				
Gifts	$20.00	$18.00	$2.00	10% F
Clothes and shoes	60.00	70.00	-10.00	-17% U
Spending money (miscellaneous)	20.00	22.00	-2.00	-10% U
Lunches	60.00	55.00	5.00	8% F
Entertainment	40.00	35.00	5.00	13% F
Total Expenses	$200.00	$200.00	$0.00	0%
Total Expenses and Savings	$220.00	$220.00	$0.00	0%

Percents are rounded to the nearest whole number.

Manual Records

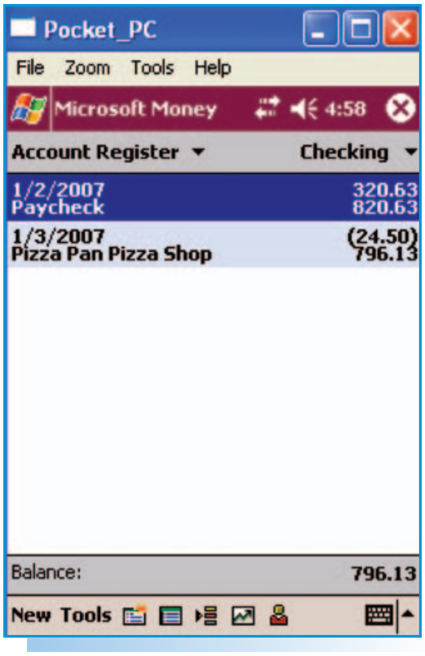
You can keep logs or journals on paper that list types and amounts of income, savings, and expenses. You can manually compute your variances and make notations about what to change. You will want to keep these journals over time so you can compare them. For example, you can look at the previous year's budget and see how your income has grown. You can also see how your spending habits have changed.

Computerized Records

Software packages such as *Quicken*® or *Microsoft Money* allow you to keep financial records using a computer. The software will retain the data and will allow you to print reports, such as a personal balance sheet. It will also allow you to quickly reference expense information. Versions of programs such as *Microsoft Money*, shown in Figure 4-2.4 on page 106, are available for use on handheld computers. Using such a program on a handheld computer makes recording data quick and easy at any location.

FIGURE 4-2.4

Keeping good records is essential to good financial planning.



You can also use spreadsheet programs, such as *Microsoft Excel*, for data entry and budget analysis. The program will allow you to compute variances in dollar amounts as well as percentages. You can set up worksheets and link them together. This will allow you to make estimates and change amounts easily.

Success Skills

Dealing with Conflict

Conflicts are bound to happen sooner or later. People you know will not be able to get along with each other. Maybe you will have a hard time working out a problem with another person. The ability to deal with conflict is an important personal skill—it will help you both in your personal life and in your work life.

When faced with a conflict, stop and take a ten-second time out. For those ten seconds, ask yourself, "What is happening here?" Listen rather than talk. Think about who is speaking and why that person is upset. Repeat a short summary of the problem or complaint to acknowledge that you understand the issue and confirm what you have heard.

If the person is upset or angry and not speaking rationally, suggest that you continue your talk later. This will give you and the other person time to think about the issue. Resume talking when you are both calm and can speak in a courteous manner.

Focus on the problem, not on the person. Be objective. Do not let your personal feelings—whether you like or dislike the person—cloud your judgment. Look for positive ways to address the issue. Be willing to compromise, when appropriate, to reach a solution that will be acceptable to all parties.

The next time you must deal with conflict, practice these skills. Reflect on a past situation—how could you have handled it differently?

4-2 REVIEW

4-2 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. What is the purpose of a budget?
2. What three types of amounts are included in a "pay-yourself-first" budget?
3. How are variable expenses different from fixed expenses?
4. Why is it important that a budget be balanced? If your budget does not balance, what can you do to bring it into balance?
5. What is an unfavorable variance?
6. Describe ways to keep financial records manually.
7. Name three software programs that can be used to keep financial records.
8. List steps you can take to help resolve a conflict in a positive manner.

4-2 Activity 2 Personal Budget

In this activity, you will create a personal budget. You will keep track of your finances for one month and then compute budget variances. In 4-1 Activity 2, you created a personal income and expense statement. Refer to that document to see income and expense items you have already identified.

1. Review the personal budget shown in Figure 4-2.2 on page 102.
2. Create a similar budget for yourself for the coming month. Use spreadsheet software to prepare the document, if it is available.
   - Enter your expected income from all sources during the month.
   - Enter an amount you want to save for the month.
   - List all your estimated expenses for the month.
   - Total the sections of the budget to see if the budget is in balance. If it is not, change the savings or expense amounts to make the budget balance.
3. Keep track of the amount of money you receive, the amount you save, and the amount you spend during the coming month. Continue this exercise after one month has passed.
4. Review the personal budget variance examples shown in Figure 4-2.3 on page 105.
5. Create a similar monthly budget variance report for yourself. Use the budget you created for the month and the actual amounts of your income, savings, and expenses.

4-3

Personal Financial Planning

OUTCOMES

- Explain the purpose of a financial plan.
- List the steps of the financial planning process.
- Describe how financial goals help make achieving personal goals possible.
- Prepare a personal financial plan.

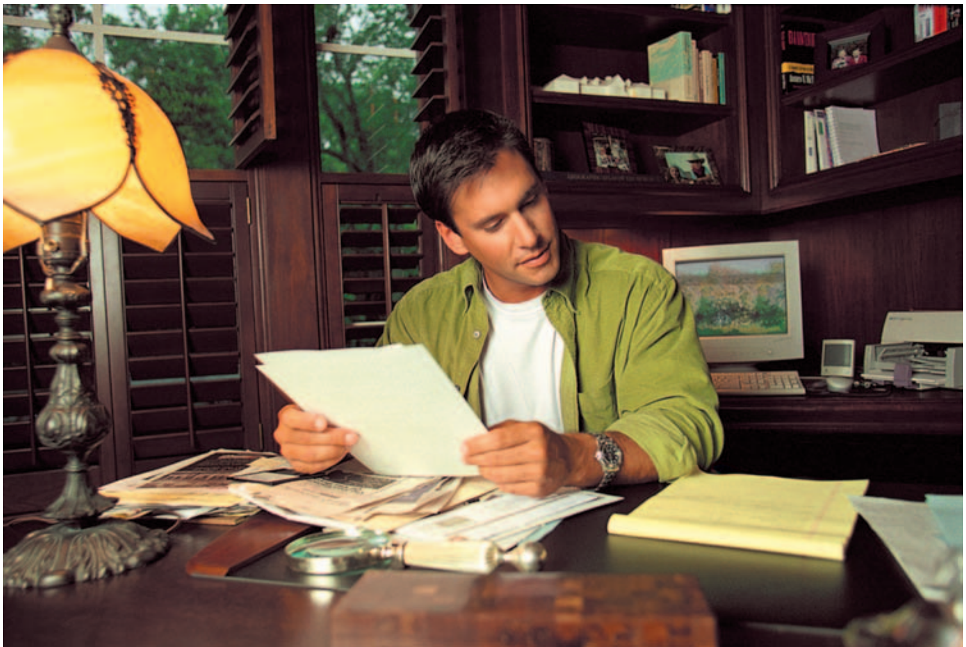
FINANCIAL PLANNING

A **financial plan** contains personal goals you want to accomplish. It also contains a timeline for reaching these goals and methods you will use to finance them. Getting a college education, owning a car, and owning a home are examples of personal goals. For each personal goal, you will have a related financial goal. Paying for living expenses, tuition, books, and other related expenses while in college is a financial goal. Saving for a down payment and having a job that provides enough income to make monthly car payments are financial goals. Saving for a down payment and having a job that provides enough income to make monthly house payments are financial goals. A financial plan is more than a budget. Its purpose is to plan for earning, spending, saving, and investing that will allow you to achieve your personal goals in the present and the future.

A FIVE-STEP FINANCIAL PLANNING PROCESS

Financial planning is a formal process. It involves looking carefully at your current situation and thinking about your future. It also requires a long-term commitment. You must put your plan into action and monitor it periodically. At least once a year, you should review and update the plan. Your plan should contain details, but it should not be too complicated to review and follow.

Some people create a plan by themselves. They may think they do not need help, or they may want to keep their financial information and goals private. Other people hire a financial planner. A financial planner is trained to help people with advice about how to invest earnings, plan for retirement, and manage other financial matters. Whether you do planning by yourself or with help from others, you will need to complete five steps.



Financial planning begins with getting organized.

Step 1 Gather Information

The first step in financial planning is gathering information. Everything related to your finances should be considered. The purpose of gathering information is to look at the state of your finances now—your starting point. The following list shows examples of items you may need to gather. You may not have all the items listed at this time in your life. However, you can gather or prepare the first three items. Other items may become part of your plan in later life.

- Personal income and expense statement
- Personal balance sheet
- Personal budget
- Checkbooks
- Current bank account statements
- Investment account statements
- Insurance policies
- Current paycheck stub
- Tax returns
- Will
- Trusts
- Financial contracts for items purchased on credit
- Other legal documents related to your finances

At some point when you review your plan, you will need to think about how to finance your retirement. You may want to gather data about your medical history and the medical history of family members. This data may help you estimate your life span, which affects the amount of income you will need over your lifetime. For example, many people may live until age 85 or 90 and should plan how to meet financial needs through that age.

Focus on . . .

PHISHING

When providers of financial products contact you directly by e-mail or using Web sites, you should be careful. There are many scams on the Internet. Web pages that appear to be genuine may not be posted by the company indicated.

One common Internet scam is called **phishing**. In this scam, a person is sent an e-mail saying, for example, that there is a problem with his or her bank account. The individual is asked to confirm a Social Security number, account number, password, or other sensitive information. The From field of the e-mail may have the real name of your bank. The real company logo may be shown. However, the message is not from the real bank. Do not respond to such an attempt to get personal information. The message is most likely from a phisher. The phisher wants to use your information illegally. **Identity theft** occurs when someone uses your personal information without your permission to commit fraud or other crimes.

If you think that a message regarding your bank account or other financial matters may be real, contact the bank or other business by phone. Ask if there is a problem with your account. Do not reply to the e-mail message or go to the link provided.

Step 2 Analyze Information

Take a careful look at the documents and information you have gathered. Find out if any data are missing, and take steps to get the data. Carefully look at each document, and make notes about what you see. Review your income and expense statement to see what your current sources of income are. Look at your expenses. Do you have enough income to pay for your expenses and save for the future? If not, try to find ways to increase income and decrease expenses.

Review your personal balance sheet. What are your assets? What liabilities do you have? What is your net worth? Review a current monthly or yearly budget. Look at the items for which you spend money. Is there a way you can spend less and save more to meet long-term goals?

As you review your financial plan each year, consider the following questions. Some of them may apply now. Others may not apply to you for a few years or for many years.

- Is your income steadily growing over time? If so, by what amount and percentage? For example, you may have $2,000 more in income this year than last year. This is a favorable trend that will help you reach your goals.
- Is your net worth growing over time? When you compare the current balance sheet to previous ones, do you see growth? If so, by what amount and percentage?
- How are your spending habits changing? What types of things are you buying (needs versus wants), and what are your purchasing plans over time?
- Who else depends on your income? Do you have a spouse or children that will be affected by your financial plan? What will they contribute?

- What new goals do you need to add and plan for? Do you need a plan to pay for a college education for your child? Is it time to plan for retirement? Does your will need to be updated to include a new grandchild?

Step 3 Set Goals

Two types of goals should be considered when creating a financial plan—personal goals and financial goals. **Personal goals** are the things you want to achieve. Living in your own apartment, owning a car, and taking a two-week vacation are personal goals. Personal goals should be set first because your financial goals will be based on them.

Financial goals describe how you will pay for your personal goals. Financial goals may be short-term, intermediate, or long-term. Short-term goals include what you will do this week, this month, and this year. A financial plan for the short term tells you on a week-to-week or month-to-month basis what you would like to achieve. Perhaps you would like to save $40 by the end of the month. Perhaps you want to add $200 to your savings account by the end of the year. Short-term financial goals are usually for between 1 week and 2 years. Using monthly and yearly budgets can help you achieve short-term goals and save for long-term goals.

Intermediate goals include what you want to achieve up to 3 or 4 years from now. You may wish to save money for college or for a future purchase or need. You may want to increase your yearly income by $100 a month within 3 years. Intermediate goals are usually for between 2 and 5 years.

Long-term goals typically include what you want to achieve more than 5 years from now. You may wish to save enough money to buy a car

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Expensive vacations require planning and financial resources.

or go on an expensive vacation. You may want to repay loans for money you borrowed to complete college. When you begin working full-time, you may contribute to a 401(k) to save money for your retirement.

Achieving intermediate and long-term goals may require that you save money for a long time. Doing without an item you would like to buy now in order to save money for a long-term goal is an example of delayed gratification. For instance, you may have a goal of saving $30 per month to help pay for your college education. This month, you would like to buy a music CD. However, if you do so, you will not be able to make your savings goal. Doing without the CD now in order to be able to pay for college later is an example of delayed gratification.

Step 4 Develop a Timeline

Plan a time to put your goals into action. How soon do you need or want to achieve a certain goal? For each personal goal, there may be a financial goal you must first achieve. Financial goals can further be divided into parts or steps. For each step, consider how long it will take to complete. Then set a target date for completion. The record of what you intend to accomplish is your financial plan. Once you clearly understand your current finances and the goals you want to accomplish, you can then take steps to reach your goals. A sample timeline for one goal is shown in Figure 4-3.1.

FIGURE 4-3.1 **ONE GOAL IN A FINANCIAL PLAN**

BILL WONG FINANCIAL PLAN
Updated April 1, 20--

Net Worth on April 1, 20-- $525.56

Personal Goal	Financial Goal	Steps to Take	Timeline
Live in my own house in the country	Own a house in the country	1. Save money for a down payment ($12,000)	5 years
		• Set aside $200 per month	Once per month
		• Open a separate account for money saved	April 8 (next week)
		• Talk to a mortgage broker to get prepared	Make an appointment for April 15
		2. Have a job that provides enough income to make monthly payments	5 years

Step 5 Implement and Evaluate the Plan

Once you have decided on your personal and financial goals, begin working toward achieving them. Check off the items on your timeline as they are completed. Set new steps as you learn about other or better ways of meeting your goals. Most importantly, take a look at your financial plan often. At least once each year, you should evaluate the financial plan and update or revise it as needed.

Your financial plan represents your personal and financial goals at one point in time. Those goals are likely to change over time. For example, you may inherit money, or you may have children. You may have a job opportunity overseas, or you may wish to spend more time on a hobby or a side business. As your personal and family goals change, your financial plan should be updated to reflect new goals. The financial plan is a work in progress; it is never finished. As one goal is accomplished, another personal goal is defined.

Keep your financial plan and all the related documents in a safe place where you can work on them regularly.

Ethics

Financial Planners and Commission Earnings

A **financial planner** is a person who provides financial advice to individuals. Financial planners help people develop financial plans in a very formal setting. If you work with a financial planner, you will share your personal information. Data about your assets, liabilities, and net worth are examples of the information you will share. The financial planner should guard your information and should not share it with others or use it for personal benefit. To do otherwise would be unethical. You must be able to trust the planner with your most sensitive personal data.

Some financial planners work for commission income. That means they make money when they sell financial products to their customers. When planners sell products that earn higher commissions, rather than products that customers really need, they are being unethical. For consumers, it can be hard to tell whether or not they are buying the best product at the lowest price. To avoid this kind of dilemma, hire a financial planner who does not work on commission. Instead, pay for the advice separately from buying any financial products, such as insurance.

Every year, people are cheated out of their money by dishonest advisors. Be sure you can trust your financial planner. Find out if he or she has been in business long, whether complaints have been filed against her or him, and if he or she has a criminal background. Ask what measures the planner will take to keep your data secure.

4-3 REVIEW

4-3 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. What is the purpose of a financial plan?
2. List the five steps in creating a financial plan.
3. What types of information or documents are needed to create a financial plan?
4. What information should you be able to learn from your personal balance sheet?
5. Why are personal goals set before financial goals? How do financial goals help make achieving personal goals possible?
6. How are short-term goals different from long-term goals?
7. What does the term *delayed gratification* mean?
8. How often should you review your financial plan at a minimum?
9. Why might you choose a financial planner who does not work on commission rather than one who does?

4-3 Activity 2 Personal Financial Plan

1. Review the example of one goal in a financial plan shown in Figure 4-3.1 on page 112.
2. Gather the personal income and expense statement, the personal balance sheet, and the personal budget you created earlier. Gather any other financial documents you have. See the list under Step 1 Gather Information on page 109 for examples.
3. Use spreadsheet or word processing software for this activity, if it is available. If not, complete the work using paper and pen. Center the following heading at the top of the document:

   (YOUR NAME) FINANCIAL PLAN
   Updated (current date)

4. Refer to your personal balance sheet created earlier to find your net worth amount. Enter this amount below the headings. For example:

   Net Worth on (current date) $525.56

5. Below the net worth information, create a table with four columns as shown in Figure 4-3.1. Enter the following column headings:

   Personal Goals
   Financial Goals
   Steps to Take
   Timeline

6. Think of a personal goal you would like to accomplish within the coming year. List this short-term goal in the table under Personal Goals.
7. Think of the financial goal or goals you will need to meet in order to achieve the personal goal. List these goals in the table under Financial Goals.
8. Determine the steps you will need to take to achieve the financial goals. Refer to your budget and income and expense statement. Do you need to increase your income or savings to meet the goals? Do you need to decrease expenses? List the steps you will take to meet the goals in the table under Steps to Take.
9. Set a time for completing each step you listed. Enter the completion time for each step in the table under Timeline.
10. Repeat steps 6 through 9 to list other goals. List at least one more short-term goal to be achieved in 2 years or sooner. List at least two intermediate goals to be completed within 3 to 5 years. List at least two long-term goals to be completed in more than 5 years. You may list as many other goals as you wish. For the long-term goals, the steps to take may be more general than for the short-term or intermediate goals. Having long-term goals that you do not yet know exactly how to accomplish is fine.
11. Work toward achieving your goals by taking the steps you have listed. Refer to your timeline often to see if you are accomplishing the steps or goals when planned.
12. At least once a year, review and revise your financial plan. Check off goals that you have achieved. Add new goals as your needs and wants change over time. Refine the steps to take in achieving your long-term goals as the steps needed become clearer.

EXPLORING CAREERS IN SCIENCE, TECHNOLOGY, ENGINEERING, AND MATHEMATICS

Do you always want to understand how things work? Are you inventive and curious? Do you like to find new and better ways to build things? Are you fascinated by technology? If the answer is yes, a career in science, technology, engineering, and mathematics might be right for you. Jobs in this area are varied. Some workers in this field do scientific research or testing. Others are engineers who design products or buildings. Some workers in this area develop new technologies that are used in consumer and business products.

Jobs in this career area are found in government and businesses. Some inventors and engineers are entrepreneurs and have their own small businesses. The need for some jobs in science, technology, engineering, and mathematics is expected to grow. The need for other jobs will stay about the same or decrease. The outlook varies by job.

Skills Needed

Some of the skills and traits needed for a career in science, technology, engineering, and mathematics include the following:

- Math and science knowledge
- Analytical skills
- Communications skills
- Computer/technology skills
- Decision-making skills
- Problem-solving skills
- Leadership skills

Job Titles

Many jobs are available in science, technology, engineering, and mathematics. Some job titles for this career area include the following:

- Biological scientist
- Civil engineer
- Conservation scientist
- Drafter
- Economist
- Engineering technician
- Physicist
- Science technician
- Technical writer

Explore a Job

1. Choose a job in science, technology, engineering, and mathematics to explore further. Select a job from the list above, or choose another job in this career area.
2. Access the *Occupational Outlook Handbook* online. A link to the site is provided on the Web site for this textbook.
3. Search for more information about the job you selected to answer these questions:
   - What is the nature of the work this job involves?
   - What is the job outlook for this job?
   - What training or qualifications are needed for this job?
   - What are the median annual earnings for this job?

Review

CHAPTER 4

Summary

- Many people have unlimited wants and needs but limited resources to meet those wants and needs.
- Because resources are limited, people must make choices. Every choice is a trade-off between the item or benefit you get and an opportunity cost (the item or benefit given up).
- Income and assets are financial resources that can be called on to meet our wants and needs.
- A personal income and expense statement lists income, expenses, and net income. A personal balance sheet lists assets, liabilities, and net worth.
- Budgeting helps you manage your financial resources.
- Building a budget requires you to estimate income, plan savings, and estimate expenses.
- A budget analysis shows how planned spending (budget) compares to actual spending. Any differences are called variances.
- Manual and computerized recordkeeping methods will help you keep organized and prepare better financial records.
- A financial plan contains personal goals and financial goals that allow you to achieve personal goals.
- Five steps in financial planning are gathering information, analyzing information, setting goals, setting steps with a timeline, and implementing and evaluating the plan.

Key Terms

assets
budget
discretionary income
financial goals
financial plan
financial planner
financial resources
fixed expenses
identity theft
liability
net worth
opportunity cost
personal goals
phishing
trade-off
variable expenses
variances
wants

ACTIVITY 1
Review Key Terms

Use the key terms from Chapter 4 to complete the following sentences:

1. Your next best choice, called the ____________, is what you give up when you make a decision to buy an item.
2. The amount of your assets minus your liabilities is called your ____________.

3. ______________ is the amount of money a person has to spend after needs are met.
4. A spending and saving plan based on expected income and expenses is called a(n) ______________.
5. Rent or insurance payments are examples of ______________ because they do not change each month.
6. An overall plan called a(n) ______________ contains your personal and financial goals.
7. ______________ are things you want to achieve.
8. A(n) ______________ is a person who gives financial advice to individuals.
9. When you choose to give up one item to buy another, you are making a(n) ______________.
10. Items of value that you own, called ______________, may be appreciating or depreciating.
11. ______________ are expenses that can go up and down each month.
12. Differences between planned and actual income or expenses are called ______________.
13. ______________ describe how you will pay for achieving your personal goals.
14. ______________ occurs when a person's personal information is used without permission to commit fraud or theft.
15. A debt you owe, called a(n) ______________, must be repaid.
16. ______________ is a scam that uses an e-mail message to get a person to give out personal information.
17. Things we desire to buy, called ______________, go beyond filling survival needs and basic comforts.
18. ______________ are money and other items of value that can be used to acquire goods and services.

ACTIVITY 2
Math Minute

Complete these problems to build your math skills. You may use spreadsheet software or complete the problems manually.

1. Michael makes $127 a week and gets paid four times a month. What is his monthly pay? His yearly pay?
2. Rachelle makes $96 a week and gets paid 52 weeks a year. What is her yearly pay? Her monthly pay?
3. Maria's planned income for July was $539. The actual amount she earned was $522. Compute the variance amount and percent. Note if the variance is favorable (F) or unfavorable (U). Round to the nearest whole percent.

4. Chin's planned entertainment expense was $125. The actual amount he spent was $106. Compute the variance amount and percent. Note if the variance is favorable (F) or unfavorable (U). Round to the nearest whole percent.

ACTIVITY 3
Make a Financial Decision

Critical Thinking TEAMWORK

You belong to a school club that has ten members and two teacher advisors. The club members and advisors are planning to attend a conference in your state capital. Apply the decision-making process you learned in this chapter to help you decide how your club should travel to the conference. Work with a classmate to complete this activity.

1. Define the need clearly. Write a statement that says exactly what you need to decide.
2. List options for filling the need. What methods of transportation might your club use to reach the state capital? (If you live in the state capital, assume you will need to travel 20 miles to the meeting site.) Do research as needed to find the cost of each option. Remember to consider the distance both to and from the state capital. Record detailed notes to show how the cost for each item was calculated.
3. Compare the options you have identified. List the advantages and disadvantages of each one.
4. Make a decision based on your research and evaluation of the information you have gathered. Explain why you choose one option over the others.
5. Describe how you would take action based on your decision if this were a real situation.

ACTIVITY 4
Create a Household Budget

Critical Thinking

In this chapter, you created a realistic budget that applies to your needs now. In this activity, you will pretend that you have graduated from high school and are living on your own. You will create a household budget that would provide for your needs in that situation.

1. Review the personal budget shown in Figure 4-2.2 on page 102. You will prepare a household budget for next month. Use spreadsheet software to prepare the budget, if it is available.
2. Use the budget in Figure 4-2.2 as an example of how to set up and format the document.

3. Assume you work 40 hours per week 4 weeks per month. You earn $8.00 per hour. Your take-home pay (after taxes and other deductions) is $224 per week. Calculate your monthly take-home pay. Enter this amount in the Income section of the budget. Enter **$60** per month that you earn doing odd jobs such as mowing grass or babysitting for a friend. Calculate the total income.
4. Enter an amount you want to save for the month. Use an amount that you think is realistic. You may need to adjust this amount later.
5. In the Expenses section, list your estimated expenses for one month. Think of all the expenses you would have if you were living on your own. Assume that health insurance premiums have been deducted from your paycheck. Also assume that the taxes you have withheld from your paycheck are all the taxes you have to pay. You do not need to list these items as expenses. A list of typical expenses for a household budget follows. You may add other items that you think would be realistic. You may leave out items that you think you would not want to have, such as satellite TV.
   - Rent
   - Car payment
   - Telephone
   - Cell phone
   - Electricity
   - Water
   - Groceries
   - Clothing and shoes
   - Internet access
   - Gasoline
   - Lunches at work
   - Satellite TV
   - Other entertainment
   - Car license and maintenance
   - Auto and renter's insurance
   - Miscellaneous
6. Do research to find typical monthly costs for these items in your area. For example, look at advertisements for apartments in a newspaper to find rent costs. Ask your parents or other adults how much they usually pay for items such as electricity and water. Calculate the total expenses.
7. Calculate the total savings and expenses. Is the budget in balance? If it is not, change the savings or expense amounts (within realistic limits) to make the budget balance. Some ideas to help balance your budget follow.
   - Can you find an apartment where the water or electricity is included in the rent?
   - Perhaps you cannot afford a car. If you take the bus to work and other places instead, you will not have a car payment, gasoline costs, or car insurance costs. Instead, add the cost of bus fares and an occasional taxi fare.

- Perhaps you cannot afford both a cell phone and a house phone. Can you do without one of them to save money?
- Consider getting a two-bedroom apartment and sharing it with a friend. Your friend would pay half of the rent, electricity, and water expenses.

ACTIVITY 5
Research Identity Theft

INTERNET www.thomsonedu.com/school/pfl

1. Access the Internet. Using a search engine, search using the term *identity theft*.
2. Read several articles you find about identity theft.
3. Make a list of steps consumers can take to avoid being the victim of identity theft.
4. Make a list of steps consumers should take if they learn they are the victim of identity theft.
5. For each site you used to find information, list the article or Web page name, the Web site, the Web address, and the date you accessed the site. For example: "Welcome to the Federal Trade Commission, Your National Resource about Identity Theft," Federal Trade Commission Web site http://www.consumer.gov/idtheft/ (accessed May 12, 20--).

ACTIVITY 6
Evaluate a Financial Plan

Critical Thinking

Take a look at the financial plan on the next page, and answer these questions:

1. Do you think the personal goals are realistic for a student who is currently a sophomore in high school?
2. Label each personal goal as short-term, intermediate, or long-term.
3. If this student gets a job, how much will she have to earn in take-home pay in order to meet her financial goals?
4. How can you add to or refine this plan to make it better?

GLORIA CADIZ FINANCIAL PLAN
Updated January 1, 20--

Net Worth on January 1, 20-- $150

Personal Goals	Financial Goals	Steps to Take	Timeline
1. Get a degree in landscape architecture	• Save $1,050 for college tuition, books, and fees	• Save $35 per month	• 30 months
	• Get financial aid to cover the balance	• Apply for financial aid	• January 20-- (next year as a junior)
		• Apply for a scholarship	• April 20-- (next year)
2. Own a car	• Save $500 for a car down payment	• Save $25 per month	• 20 months
	• Borrow money from bank	• Get a job so I will qualify for a loan	• Get a summer job and a part-time job by January 1, 20--
3. Take a vacation in Hawaii before starting college	• Save $1,500 for a vacation	• Save $50 per month	• 30 months
	• Buy new clothes for trip	• Make reservations early to get the best deal	• January 20-- (in 2 years)

CHAPTER 5

Banking Procedures

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Chapter 5 discusses banking activities for consumers and banking in the United States. Many benefits and services for consumers are available from financial institutions. Some accounts have fees or restrictions of which consumers should be aware. Banking in this country is centralized through the Federal Reserve System. In this chapter, you will explore how this system works and what it means to you as a consumer.

ONLINE RESOURCES

Personal Financial Literacy Web site:

- Data Files
- Vocabulary Flashcards
- Sort It Out: Banking Procedures
- Chapter 5 Supplemental Activity

Search terms:

- bank reconciliation
- online banking
- U.S. savings bonds
- Federal Reserve System
- monetary policy

5-1

Checking Accounts

OUTCOMES

- Explain the purpose and use of a checking account.
- Prepare a checkbook register.
- Write a check and prepare a deposit slip.
- Prepare a bank reconciliation.

INTRODUCTION TO CHECKING ACCOUNTS

Banks offer various types of accounts that consumers may find useful. Checking accounts, savings accounts, certificates of deposit, and money market accounts are popular choices. In this part of the chapter, you will learn about checking accounts. You will learn about other types of accounts in the next part of the chapter.

A **checking account** is a demand deposit account in a bank. Its purposes are to provide a safe place to keep money and to allow users easy access to the money in the account. The account holder may withdraw money from the account at any time. The account holder is also able to write checks on the account. A **check** is a written order to a bank to pay the stated amount to the person or business named on the check from an account. Checks can be used to pay bills by mail or to purchase items in stores. Writing a check for a major purchase is safer than carrying a large amount of cash to a store. A canceled check (one that has been cashed) also serves as proof of payment for bills or purchases.

A checking account provides a safe place to keep money. Checking accounts at banks generally are insured by the Federal Deposit Insurance Corporation (FDIC) up to the legal limit of $100,000 per depositor per bank. The FDIC is an agency of the federal government. By insuring deposits in banks, the FDIC helps to promote public confidence in the U.S. financial system. Consumers should confirm that a checking account will be insured by the FDIC before opening an account.

Opening a Checking Account

To open a checking account, the account holder will need some money (cash or checks). Often, as little as $50 or $100 is needed to open an account. The account holder will be given some checks when the account is opened. These checks have blank spaces in which to write information about the account. Personalized checks, which have the account holder's

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Financial institutions offer checking accounts and many other financial services.

name and other data printed on them, are provided a short time later. A checkbook register and a checkbook cover are usually included with the checks. With a typical account, the account holder is charged a fee for the personalized checks. The account holder may also be charged a monthly fee for the account or for each check written. These fees may not apply if a certain minimum balance, such as $1,000, is kept in the account.

When opening a checking account, the account holder will need to provide personal data. An address, a phone number, and a Social Security number are usually required. The account holder may be asked to show a picture ID such as a driver's license for identification.

Some banks request that the account holder answer a security question, such as "What is your pet's name?" Others ask for a code word, such as your mother's maiden name. The purpose of a security question or code word is to identify the account holder when he or she calls on the phone.

The account holder will sign a signature card. This card provides an official signature that the bank can compare to the signature written on checks. A bank account can be a joint account owned by two or more people. Each person who is authorized to write checks on the account must have a signature card on file with the bank. The account holder should sign her or his name on the signature card the way it will appear on signed checks.

Focus on . . .

Check Cashing Services

Exchanging a check written to you for money is called cashing the check. The money received can be in currency (bills and coins). It can also be a credit (increase) in your checking account if the check is deposited.

Some banks will not allow a person to cash a check unless he or she has an account with the bank. A very profitable business is cashing checks for people who may not have their own checking accounts. Check cashing businesses charge a fee for this service. Some states regulate the fees that may be charged. Fees vary by state and, in some cases, by the type of check being cashed. For example, the fee for a Social Security check might be 3 percent or $2, whichever is greater. The fee for a personal check might be 10 percent or $5, whichever is greater. If you have your own checking account, you do not have to use a check cashing service, and you can keep the full amount of the check.

Some check cashing companies also make short-term loans. An individual is given an advance, often called a payday loan, based on proof of employment. The borrower writes a check to the lender for the amount to be borrowed plus a fee. The lender agrees to hold the check (not cash or deposit it) until after the borrower's next payday. A high fee is charged for this service. For example, to get an advance of $100 for 14 days, a borrower might have to pay a fee of $15. This fee is in addition to repaying the $100. In this example, the cost of the loan is a $15 finance charge at a 391 percent annual percentage rate.

Payday loans can be helpful to consumers. However, consumers should use this service sparingly. Getting payday loans regularly can lead to a cycle of borrowing money at a high cost. For example, a consumer may not have enough money to pay bills this month. A payday loan can help provide the money needed. However, the next month, the consumer may have even less money with which to pay bills. This happens because part of the money earned this month must be used to repay the loan from last month. The consumer is again short of money after repaying the loan. Borrowing money from other sources at a lower rate may be a better short-term solution for the consumer. Developing a budget that allows the consumer to pay all expenses with the available income is a better long-term solution.

Keeping a Checkbook Register

Keeping accurate records of checking account transactions is very important. Account holders should verify that the amounts deducted from the account and the amounts added to the account are correct. A **checkbook register** is a tool that can be used to track checking account transactions. The register can also provide a record of payments made for bills or purchases.

A **deposit** is money added to a checking or savings account. The money can be in the form of currency, checks, or electronic transfers. All deposits, checks, other withdrawals, and fees should be recorded in the checkbook register. The purpose of the transaction can also be recorded.

FIGURE 5-1.1

CHECKBOOK REGISTER

CHECK NO. OR TRANSACTION CODE	DATE	DESCRIPTION OF TRANSACTION	PAYMENT/ DEBIT (–)		FEE (–)	✓	DEPOSIT/ CREDIT (+)		BALANCE	
									$800	00
581	7/1/--	Food Mart	$ 36	12	.20		$		36	32
		Groceries							763	68
DEP	7/15/--	Deposit Paycheck					220	50	220	50
									984	18
WD	7/16/--	ATM Withdrawal	20	00					20	00
									964	18
582	7/20/--	Bellvue Apts.	600	00	.20				600	20
		Rent							363	98
ON	7/22/--	Metro Gas & Electric	32	50					32	50
		Online Payment							331	48
SC	7/31/--	Monthly Account Fee			5.00				5	00
		July							326	48

A running balance in the register shows the amount of money in the account. By carefully entering all data related to the account into the register, you will be sure to know how much money is in your account at all times. A register can be kept manually or using a computer program such as *Excel* or *Quicken*. A manual register is shown in Figure 5-1.1.

Always complete the register entry for a check first. Then write the check. This process will help ensure that you do not forget to enter the item. Checking the balance in the account before writing a check is a good practice. You want to be sure you have enough money in the account to cover the check.

In the first column of the register, list the check number or a code to identify the transaction. For example, enter a code such as DEP to stand for *deposit*. Enter a code such as WD to stand for *withdrawal*. The check number, 581, is entered on the first line of the register in Figure 5-1.1.

In the Date column, enter the current date. (The characters -- are used in Figure 5-1.1 to represent the current year.) In the Description of Transaction column, enter the name of the person or business to which the check is written. You can also enter the purpose for the check. For example, Groceries is entered on line 2 of the register in Figure 5-1.1.

In the Payment/Debit column, enter the amount of the check or other withdrawal. If there is a check fee, enter that amount in the Fee column. In the register in Figure 5-1.1, $0.20 is entered as the check fee. When making a deposit, enter the amount in the Deposit/Credit column. Carry the amount of the payment plus any fee or the deposit to the Balance column. Subtract the payment or add the deposit amount to find the new balance.

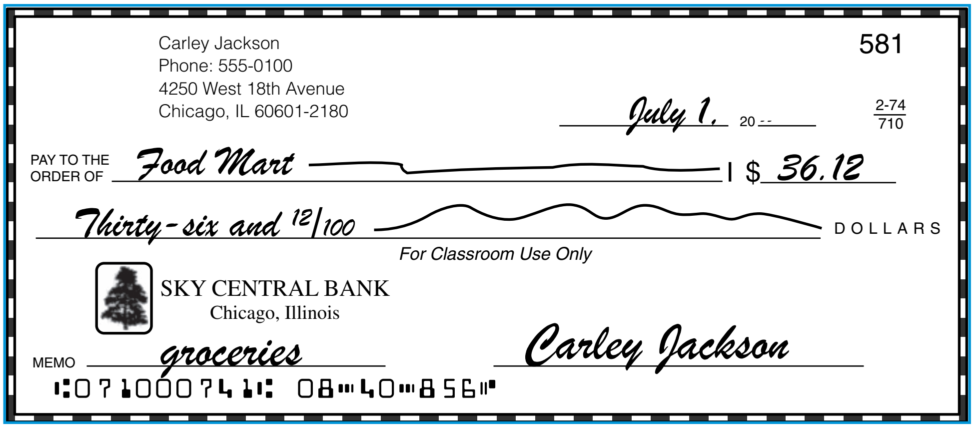
CHECKS AND OTHER DEBITS

An advantage to a checking account is that the money is easy to access. The account holder can write checks to use money to pay bills or make purchases. Many banks offer debit cards that can also be used to make purchases or get cash. Automated teller machines (ATMs) are provided by many banks. Bank customers and others can use an ATM card to withdraw money from a checking account.

Some accounts offer the option of automatic withdrawals. With an **automatic withdrawal**, money is deducted from your account and

FIGURE 5-1.2

PERSONAL CHECK



transferred to another party. For example, insurance premiums could be deducted from your account and transferred to the insurance company. The main advantage is that you do not have to write a check each month to pay this bill.

Writing Checks

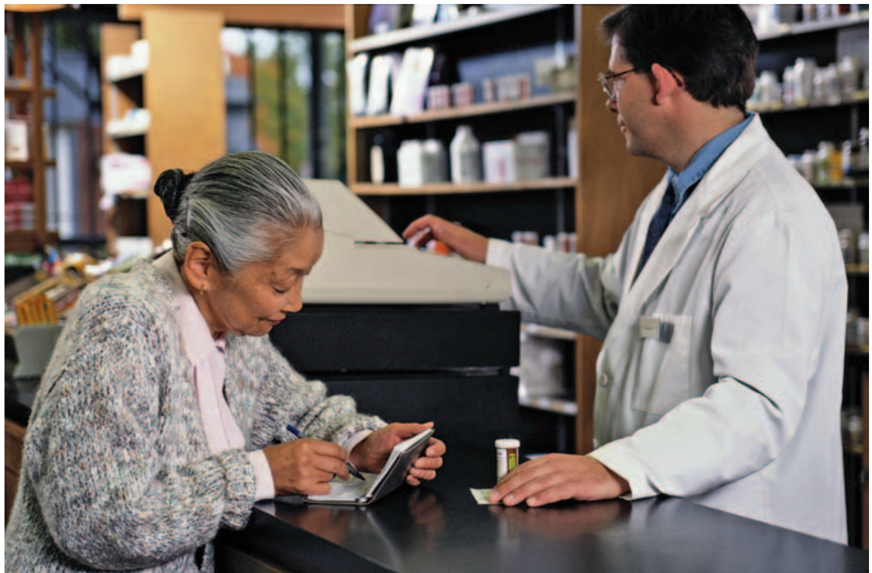
A check is a legal document used to transfer money. When you write a check, you are telling the bank to pay money to the person or company named on the check. This person or company is called the payee. The payee can cash the check or deposit it into a bank account.

Figure 5-1.2 shows an example check. Notice that the account holder's name and address are printed on the check. The check number, 581, appears near the top right of the check.

Checks should be written in ink. Use dark ink, such as navy blue or black. Write legibly so that your handwriting can be read. Fill in the spaces, and do not leave space before or after your writing. Follow these steps as you write checks:

1. Enter the current date. Checks should not be postdated. A **postdated check** is a check written with a date that will occur in the future. Banks will not hold postdated checks until the future date; they will process them at once without regard to the date.
2. Enter the name of the payee on the Pay to the Order of line. Do not leave this line blank. If you do so and lose the check, anyone can cash the check by simply writing the word *Cash* or her or his own name in the blank.
3. Enter the amount of the check in numbers after the dollar sign. Fill the space, separating dollars and cents clearly.
4. Write the dollar amount in words. Do not leave extra space anywhere on the line. Draw a line to the end if the space is not filled. Use the word *and* to separate dollars and cents, such as "Fifty-five and 35/100"____________ Dollars.
5. Sign your name exactly as you signed it for the signature card at the bank. Do not leave the signature line blank. An account holder authorized to write and sign checks is called a drawer.
6. Enter a note on the Memo line, if desired, to give the purpose of the check.

If you make a mistake when writing a check, begin again with a new check. On the check with the error, write VOID in large letters. In the checkbook register, write VOID over the entry in the Description of Transaction column. Draw a line through the check amount and the balance amount. Record the check data again, using the new check number.



© Getty Images/PhotoDisc

Using a checking account means that you do not have to carry as much cash.

Using Debit Cards and ATM Cards

A **debit card** allows the account holder to withdraw cash from an account at an ATM. The card can also be used to make purchases. The effect is the same as writing a check, but the withdrawal is made electronically. The money is taken out of the account very quickly. To use a debit card, the account holder passes the card through a card reader of some type. The account holder must also enter a personal identification number (PIN) or password. In some systems, a signature is also required. The PIN gives access to the account, so it should be guarded carefully.

An ATM card is similar to a debit card; however, the ATM card can be used only at an ATM. The account holder cannot make a purchase using an ATM card. At an ATM, the ATM card can be used to get cash from an account or to make deposits to an account.

© Getty Images/PhotoDisc

Automated teller machines make personal banking easy and convenient.

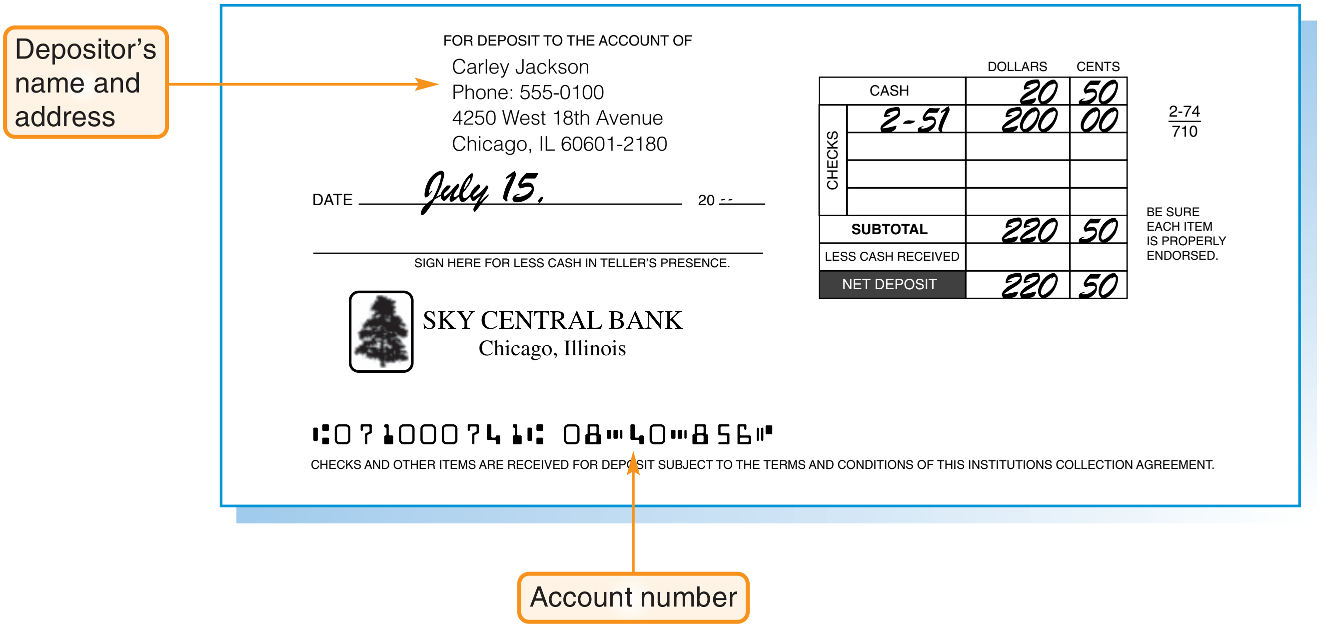
Protecting Your Account Data

When someone alters a check to get money from another person's account, that is a crime called check fraud. When someone signs another person's name on a check, it is the crime of forgery. Identity theft occurs when someone uses your data without your permission to make purchases, withdraw cash, or borrow money. To help protect yourself from crime, take good care of your supply of checks. Keep them in a safe location. When using a debit card or an ATM card, protect your PIN or password and account number. Do not give out your bank account number unless you are sure the person or company receiving it is reputable.

MAKING DEPOSITS

A short time after opening an account, the account holder will usually receive personalized deposit slips, along with checks. Blank deposit slips, available at the bank, can also be used. Figure 5-1.3 on page 130 shows

FIGURE 5-1.3 **DEPOSIT FORM**



a deposit slip for a checking account. Note that the depositor's name and address are printed on the slip. The account number appears at the bottom of the slip.

Checks that are to be included in a deposit must be properly endorsed. An **endorsement** is a signature or instructions written on the back of a check. It authorizes the bank to cash or deposit the check. If a check is not properly endorsed, it may be returned by the bank to the customer and not included in the deposit. Some endorsements provide more instructions than others. The most commonly used forms of endorsement are blank, restrictive, and special. Look closely at Figure 5-1.4 on page 131 as you read about each form of endorsement.

Many checks have an endorsement area printed on the back of the check. Be careful to write the endorsement within this area. If the back of the check is blank, place the check face up. Turn the check over, keeping the same edge at the left. Write an endorsement on the left edge of the check or other marked endorsement area.

For a blank endorsement, the signature of the payee is written on the back of the check. The signature must be in ink. This endorsement provides little protection. Anyone who has the check can cash it. This endorsement should be used only when you are at the bank ready to cash or deposit the check.

In a restrictive endorsement, the purpose of the transfer of the check is given. For example, *For deposit only* may be written on the check above the name of the payee.

In a special endorsement, the words *Pay to the order of* and the name of the person or company to which the check is being transferred are placed before the signature of the payee. In some instances, a special endorsement is referred to as an *endorsement in full*.

Once the checks are endorsed and the cash is totaled, you are ready to complete the deposit slip. Follow these steps to prepare a deposit slip. Refer to Figure 5-1.3 as you read the instructions.

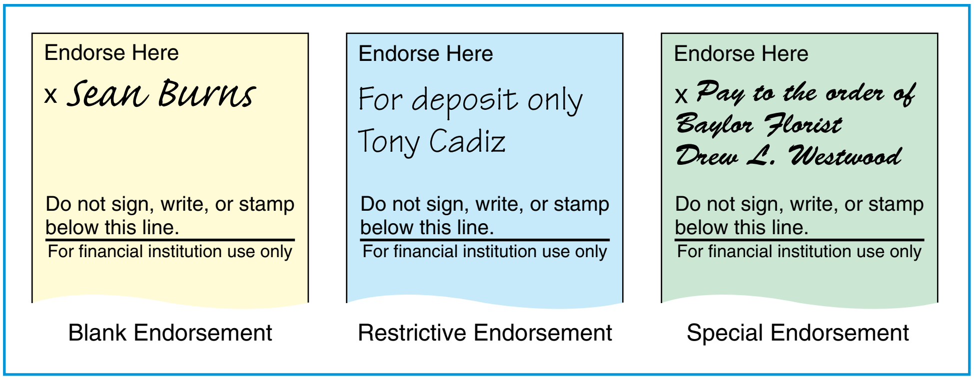


FIGURE 5-1.4

Endorsements provide varying levels of protection.

1. Enter the current date on the Date line.
2. Enter the amount of cash (bills and coins) in the Cash section.
3. Enter checks in the Checks section. Enter the bank's American Banking Association (ABA) number, shown at the upper-right-hand corner of most checks, beside each check. A deposit may contain more checks than can be listed on the front of the deposit slip. When this is the case, list the other checks on the back of the slip in the spaces provided. Carry the total of the checks to the front of the deposit slip.
4. Enter the total amount of cash and checks in the Subtotal section.
5. Enter the amount of cash received at the time of deposit, if any, in the Less Cash Received section, and sign on the line indicated.
6. Enter the total deposit amount in the Net Deposit section.
7. Make the appropriate entry in your checkbook register to record the deposit.

Deposits can be made at one of your bank's ATMs. If you make a deposit at an ATM, follow the instructions on the screen, and get a receipt. Verify that the receipt shows the correct amount of the deposit.

When checks are deposited in person, by mail, or at an ATM, it can take a few days for the deposit to be processed. The account holder may not have access to the money deposited for several days.

Automatic deposit is an option with many accounts. With **automatic deposit**, money is electronically placed in an account. Many people receive Social Security payments in this manner. Many businesses provide this service for their employees. If payday is the first of the month, the amount of the employee's net pay will be deposited electronically and is usually available on that day. The main advantage for account holders is that they have instant access to their money. This method is also safer and more convenient than carrying checks to the bank for deposit.

RECONCILING A BANK STATEMENT

Once a month, you will receive a statement from the bank. The statement may be on paper and arrive by mail, or it may be sent to you electronically. You may also receive cleared checks that your have written or photocopies of the checks. The statement will list checks, other withdrawals, and deposits made to the account. It will show the account beginning balance and ending balance. Any service charges or other fees that have been debited (charged) to the account and any interest earned will also be listed.

When you get a bank statement, you should compare it to your checkbook register. You will adjust the balance shown in the checkbook register to record interest earned or fees charged. You will adjust the balance shown on the bank statement for checks or other withdrawals and deposits that have not yet been processed by the bank. After adjustments are made, the two balances (register and statement) should be the same. This process is called reconciling a bank statement. A form may be provided on the back of the bank statement for use in reconciling the account. You can also use programs such as *Excel* to prepare a reconciliation. A sample bank reconciliation is shown in Figure 5-1.5 on page 133.

Refer to Figure 5-1.5 as you read the following steps for reconciling a bank statement:

1. Enter the date of the reconciliation and the account number on the reconciliation form.
2. Enter the ending balance date and amount from the bank statement on the reconciliation form. The amount probably will not be the same as the balance shown in your checkbook register.
3. Compare your checkbook register with the bank statement. Verify that the amount of each deposit made is shown correctly on the bank statement. Place a check mark in the check mark (✓) column of the register by each deposit that is shown on the bank statement.
4. On the reconciliation form, list the date and amount of any deposits you made that do not appear on the bank statement. These are called deposits in transit. Total the amounts. Add the total deposits in transit to the bank statement ending balance. Place this amount on the Subtotal line.
5. Compare your checkbook register with the bank statement. Verify that the amount of each check you wrote and each ATM or debit card withdrawal you made is shown correctly on the bank statement. Place a check mark in the check mark (✓) column of the register by each check or other withdrawal that is shown on the bank statement.
6. On the reconciliation form, list the check number or code, date, and amount of any checks and other withdrawals you made that do not appear on the bank statement. Checks written that have not yet been processed by the bank are called outstanding checks. Total the amounts. Subtract the total from the Subtotal calculated in step 4. The amount left is called the adjusted bank balance.
7. Enter the balance date and amount shown in your checkbook register on the reconciliation form.
8. On the reconciliation form, list any fees or charges shown on the bank statement that are not recorded in the register. Total the amounts. Subtract the total from the checkbook register balance on the form. Record the fees and charges in your checkbook register, and update the balance.
9. On the reconciliation form, list any interest or other credits (additions) shown on the bank statement that do not appear in the register. Total the interest and other debits. Add this total to the amount calculated

FIGURE 5-1.5 BANK STATEMENT RECONCILIATION

RECONCILIATION OF BANK STATEMENT

Date: August 3, 20--
Account No.: 942869

Bank Statement Balance on July 31, 20-- $ 966.68

Add Deposits in Transit and Other Credits

Date	Amount
7/31/20--	220.50

Total Deposits in Transit/Credits 220.50

Subtotal 1,187.18

Deduct Outstanding Checks/Withdrawals

Check No.	Date	Amount
580	7/2/20--	20.00
581	7/29/20--	36.12
ATM	8/1/20--	40.00

Total Outstanding Checks/Withdrawals 96.12

Adjusted Bank Balance $ 1,091.06

Checkbook Register Balance on August 3, 20-- $ 1,096.06

Deduct Bank Charges

Description	Amount
Service charge, monthly fee	5.00

Total Bank Charges 5.00

Subtotal 1,091.06

Add Interest or Other Credits

Description	Amount

Total Credits 0

Adjusted Checkbook Register Balance $ 1,091.06

in step 8. Record the interest or other credits in the register, and update the balance.

10. Compare the adjusted bank statement balance and the adjusted checkbook register balance. The two amounts should be the same. If they are not, complete the steps again and check your calculations carefully. If the numbers still are not the same, check your calculations in the checkbook register. If you find that a mistake has been made, add or subtract the amount of the mistake to correct the checkbook register balance.
11. In the checkbook register, enter a note in the Description column to indicate that the balance in is agreement with the bank balance on this date; for example, "Register and statement are in balance on August 3, 20--."
12. Store the bank statement and the completed reconciliation form for future reference. Organize the documents by date so you can find a particular statement easily.

CHECKING ACCOUNT FEES

Some checking accounts do not have monthly service fees. To get this type of account, you may have to meet some criteria. For example, you may be required to keep a minimum balance in the account. Some checking accounts pay interest to you on the money you keep in the account. You might choose to have an account that pays a lower interest rate on the deposited amount in order to have no monthly fee.

Some accounts charge a fee for each check you write, such as 20 cents. In other accounts, you might be allowed ten checks at no charge and then have a set charge for each check after that. Fees and rules for checking accounts vary. Consumers should compare accounts and banks to find the best value for the type of account desired.

Credit unions are not-for-profit financial organizations. Members of a credit union may be offered free checking accounts with no minimum deposit. Some banks offer free checking accounts to senior citizens or others. Students or people under age 18 may also qualify. Accounts with monthly fees often cost \$5 to \$10 a month. This charge is in addition to charges for checks and fees for other services.

5-1 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. What are the purposes of a checking account?
2. What information will a person typically be required to provide when opening a checking account? What form of identification and other information might also be required?
3. Checking accounts at banks generally are insured by the FDIC for up to how much?
4. What is the purpose of a signature card?
5. What does the term *cashing a check* mean?
6. Why should consumers use payday loans sparingly?
7. What is the purpose of a checkbook register? What types of data should be in a register?
8. List the six steps in writing a check.
9. What should you do with a check on which you make an error?
10. What is the difference between a debit card and an ATM card?
11. Why is it important to protect your bank account number and PIN or password?
12. What is the purpose of a check endorsement? How does a blank endorsement differ from a restrictive endorsement?
13. What procedure should you follow when completing a deposit form if you have more checks than can be listed on the front of the form?
14. What are some advantages for account holders of having automatic deposit for money received?
15. What is the purpose of completing a bank statement reconciliation?

5-1 Activity 2 Manage a Checking Account

Managing your checking account is a responsibility. You should write checks and complete deposit forms and the checkbook register carefully to avoid errors. In this activity, you will update a checkbook register, complete a deposit form, write checks, and reconcile a bank statement. Use the current year for dates. Refer to Figures 5-1.1, 5-1.2, 5-1.3, 5-1.4, and 5-1.5 for examples as you complete the activity.

1. Open and print the PDF file *CH05 Forms* from the data files. This file contains a deposit form and checks. It also contains a checkbook register.

2. Use the following information to complete the checkbook register and the deposit form. Remember to sign your name on the appropriate line to indicate that you received cash. Show how you would endorse the checks you are depositing using the space provided.
   - Date of the deposit: August 30, 20--
   - Items to be deposited:

Currency	0
Checks	
15-456	$108.66
16-589	$ 50.00

   - Cash received from the deposit: $25.00
3. On August 30, write a check for $15.85 to Quick Pizza for food. Remember to complete the checkbook register before writing the check. Sign your name (first and last) to the check.
4. On August 31, complete the register and write a check for $12.35 to Fresh Cleaners for cleaning services. Sign your name to the check.
5. Open and print the PDF file *CH05 Statement* from the data files. This file contains a bank statement and a reconciliation form.
6. Reconcile the bank statement. Use the checkbook register you completed earlier. You can use the form provided or create a similar form using software such as *Excel*. Use September 3, 20--, as the date for the reconciliation.
7. Check your work. The adjusted bank statement balance and the adjusted checkbook register balance should be $382.29.

5-2
Savings Accounts

OUTCOMES

- Explain the purpose of savings.
- Compute interest on savings at a fixed interest rate.
- List savings options and their advantages.

THE PURPOSE OF SAVINGS

Saving money is important because it means you are providing for future needs and wants. A **savings account** is a demand deposit account that may have some restrictions about how quickly or easily the money can be withdrawn. When an account allows quick and easy access to the money in it, this is known as liquidity. Savings accounts are not as liquid as checking accounts. The purpose of a savings account is to accumulate money in a safe place for future use. Savings accounts at banks generally are insured by the FDIC up to the legal limit of $100,000 per depositor per bank.

Most savings accounts pay interest at a low rate. However, the rate is higher than on money in a checking account. Some banks allow depositors to link their savings and checking accounts. This allows the transfer of money back and forth (by phone or electronically) at the account holder's convenience.

Having a savings account helps you be prepared for emergencies and other unplanned spending. It gives you flexibility so that you can

Savings allow you to make purchases in the future.

make better buying decisions. For example, you may be able to buy items now at sale prices that will be used in the future. Buying at sale prices now saves money in the long run. Savings accounts allow you to accumulate money for large purchases, such a car or house. Setting aside money today for use later is a first step in becoming financially secure.

COMPUTING INTEREST

Money deposited in a savings account will usually earn a set rate of interest. Interest earnings are taxable when they are earned. The sum of money set aside on which interest is paid is called **principal**. Money earned on the principal is called interest. The higher the rate of interest, the more money the account earns.

When interest is computed on the principal once in a certain time period, this is called simple interest. The interest amount is not added to the principal. The simple interest method assumes that one interest payment will be made at the end of the period. Interest rates are usually given in yearly rates. However, the interest may be paid after a certain number of months. In this case, the months must be converted into a fraction of a year. The fraction is shown as a decimal amount in the formula. The formula for calculating simple interest and a sample problem are shown in Figure 5-2.1.

Another way of calculating interest is called **compound interest**. With this method, interest earned is added to the principal. Then, interest will be earned on the principal plus interest that was earned earlier. Figure 5-2.2 shows how interest compounds. The principal, $100, was put into savings at an annual rate of 6 percent. The interest was then compounded quarterly (4 times per year) for 3 years. An interest rate of 6 percent per year is 1.5 percent quarterly.

FIGURE 5-2.1

SIMPLE INTEREST EXAMPLE

SIMPLE INTEREST
Interest (I) = Principal (P) × Rate (R) × Time (T)
Interest = $1,000 × 6% annual rate × 6 months
$30 = $1,000 × 0.06 × 0.5

FIGURE 5-2.2

COMPOUND INTEREST EXAMPLE

QUARTERLY COMPOUNDING (Annual Interest Rate 6%)

Year	Beginning Balance	Rate	Quarterly Interest 1	2	3	4	Ending Balance
1	$100.00	0.015	$1.50	$1.52	$1.55	$1.57	$106.14
2	$106.14	0.015	$1.59	$1.62	$1.64	$1.66	$ 112.65
3	$ 112.65	0.015	$1.69	$1.72	$1.74	$1.77	$ 119.57

SAVINGS OPTIONS

Many people choose to save money using a savings account at the same bank where they have a checking account. This option provides some advantages. Using one bank for both accounts may be more convenient than using two or more banks. Having both accounts in one bank may allow you to use the savings account for overdraft protection. This means that if you write checks for more money than you have in your checking account, the bank will draw the money from your savings account or loan it to you. Without this protection, the check would be returned for non-sufficient funds (NSF). You would probably have to pay fees to your bank and to the person or business to which you wrote the check, as well as the original amount of the check.

Certificates of Deposit

Banks offer other savings options that you should consider in addition to a savings account. A **certificate of deposit**, called a CD, is a time deposit (rather than a demand deposit). This means that the money you deposit is set aside for a fixed amount of time. For example, you may put your money into a 6-month CD at a guaranteed rate of 5.25 percent. If you leave your money in the CD for the entire 6 months, you will earn the full 5.25 percent. If you withdraw part or all of it before the 6 months, you will be penalized. At some banks, you will lose part of your principal, as well as receive no interest on the money deposited.

Money Market Accounts

A **money market account** is another option offered by some banks. This type of account pays the market rate of interest on the money deposited. When interest rates are rising, a money market account will often earn more than a savings account or CD. When rates are falling, however, the interest earned may be less than that paid on a CD. A minimum balance, such as $1,000 or $5,000, is often required to open a money market account. Restrictions may apply to the account. For example, you may be able to write only two or three checks per month on the account. If you do not maintain the balance required, or if you write too many checks, you will be charged fees.

A certificate of deposit or money market account provides a good way to save for education in the future.

U.S. Savings Bonds

If you are able to commit your money for a longer period of time, you have other choices. One good long-term choice is a savings bond. A **U.S. savings bond** is a discount bond issued by the federal government. That means you pay less than face value. For example, you can purchase a $100 (face value) Series EE paper savings bond for $50. As interest is earned on the bond, it will grow to be worth the $100 (the maturity value).

U.S. savings bonds pay a guaranteed rate of interest if you keep the bond for a certain period of time. U.S. bonds are considered to be a safe form of saving. If you cash the

FIGURE 5-2.3

The TreasuryDirect Web site provides information on savings bonds.

Source: TreasuryDirect, Converting Your Paper Savings Bonds Using SmartExchange, http://www.treasurydirect.gov/indiv/research/indepth/smartexchangeinfo.htm (accessed April 27, 2006).

bond before the time is up, the bond will earn a lower rate of interest. U.S. savings bonds can be purchased through banks or at the TreasuryDirect® Web site. You can also see the guaranteed rates currently being paid at the Web site. You can access the TreasuryDirect Web site using the link provided on the Web site for this textbook.

Once a savings bond has matured (has reached face value), it may continue to earn interest. In general, savings bonds earn interest for different lengths of time. Some types earn interest for up to 40 years. Others stop earning interest after 20 or 30 years. Information about the length of time a bond earns interest can be found on the TreasuryDirect Web site. When a bond stops earning interest, it should be cashed in or converted to another type of bond. Interest is not taxable until the bond is cashed in. If the bond is used for education expenses (for yourself or your children), the interest may not be subject to federal taxes. Look for more information about taxes on bonds at the TreasuryDirect Web site.

Individual Retirement Arrangements

Saving for retirement is an important goal for many people. One way to save for retirement is by creating an individual retirement arrangement (IRA). An IRA allows individuals to deposit money into an account during their working years. The money deposited may be tax-deductible. Taxes are paid on the money and interest earned when the money is withdrawn during retirement. Taxes paid then may be at a lower rate than the rate paid during working years.

IRAs can be set up at a bank or another financial institution. IRAs can also be set up through mutual fund companies, insurance companies, and stockbrokers. Different types of IRAs can be created. The amount of money that can be put in the account each year and other rules regarding IRAs are set by the federal government. More information about IRAs can be found in *Publication 590, Individual Retirement Arrangements (IRAs)* from the Internal Revenue Service. A link to the IRS Web site where you can search for this publication is provided on the Web site for this textbook.

Success Skills

Negotiating

Negotiation is the process of reaching an agreement that benefits you or enables you to get what is important to you. You have probably heard the expression "In life you don't get what you deserve; you get what you negotiate." It's true—people who have good negotiation skills get more of what they want!

The first step in negotiating is to understand your own position. What exactly do you want? In clear, unemotional words, be able to state your wants or needs. Have solid reasons for your choices.

The second step in negotiating is to understand your opponent's position. What exactly does he or she want? What needs and motives does this person have? When you know her or his needs, you can find ways to meet them while meeting yours, too.

Third, create a proposed solution. This usually means you give up something minor to get something important to you. It also means the other person will give up something to get what he or she wants.

People with good negotiation skills identify what is important to both sides and what they are willing to give up in order to reach an agreement. Both sides must feel good about what they are getting.

MEETING FINANCIAL GOALS

When choosing a savings option, consider your financial goals. How much money do you want to save and earn in interest for a particular purpose? How much time do you have in which to save? What interest rate can you earn on your savings?

All these factors should be considered when choosing a savings option.

The amount of time you have to save and the interest you can earn determine how much money you need to save each month or year to meet your goals. The amount of interest you can earn and the time the money must be left on deposit affect the savings option you should choose. For example, if you want to save $10,000 to buy a used car, a certificate of deposit might be a good choice. The CD would likely pay higher interest than a savings account, and you would not need immediate access to the money. A money market account might also be a good choice. This type of account typically earns higher interest than a savings account. A U.S. savings bond would probably not be a good choice in this situation. Savings bonds should be used to save for longer periods of time (20 or 30 years) to gain their full value.

A principle called the **Rule of 72** provides a quick way to see how long it will take to double money invested at a given rate. To apply the Rule of 72, simply divide the annual interest rate into 72. The answer is the number of years it will take at that rate to double the amount invested. For example, if $50 is invested at 6 percent interest, then it will grow to $100 in 12 years (72/6 = 12). At 4 percent interest, money invested will double in 18 years (72/4 = 18).

OTHER SERVICES AND FEES

Financial institutions offer a number of services. Some of these are included with a checking account. Others cost additional money, either once a year or as you use them.

Bank Services

Many banks rent safe deposit boxes as a service to customers. A safe deposit box is a secure container located in the bank vault. You can store important documents, such as deeds or stock certificates, there. The safe deposit box protects items from fire or theft. A safe deposit box usually costs from $35 to $100 a year, depending on the size of the box.

Overdraft protection can be a valuable service. If you write a check and your account does not have enough money to cover the check, the bank returns the check for non-sufficient funds. The check is commonly called a **bounced check**. The bank will charge you a fee when this happens—often $30 to $40, or more, per check. When a check bounces, the person or business that deposited it will also be charged a fee. You will be expected to pay that fee as well. A bounced check could cost you $50 or more! If you have overdraft protection, NSF checks will be paid rather than bounced. The money may come from a savings account you have at the bank. The money might also be paid by the bank as a short-term loan to you. You would have to pay the amount of the check plus a fee. However, the fee would be less than if the check bounced.

Ethics

Writing Bad Checks

Having a checking account is not a right; it is a privilege. Banks, credit unions, and others make these accounts available to customers. Using a checking account is a very convenient way to manage money. You should monitor your account carefully. Be certain you have money in your account to cover checks you write.

When you write a check and you do not have money in your account to cover it, you are writing a *bad check*. This is also called a non-sufficient funds (NSF) check. If you do not monitor your account balance carefully, you might write a bad check by mistake. Knowingly writing a bad check is illegal and unethical. Criminal or civil charges can be brought against a person who writes bad checks. Writing bad checks can also affect your credit rating. You may have trouble borrowing money for purchases such as a car or getting a credit card if you have a poor credit rating.

Writing bad checks can be thought of as a form of stealing. Many merchants and individuals who are given bad checks never get the money that is due them. Merchants pass on some of the cost of bad checks to consumers in the form of higher prices.

You should write checks only when you have enough money in the account to cover the check. Do not write a check and plan to deposit money later to cover the check before the check is processed. Checks can be processed quickly. You should not expect that you will have time to deposit money before a check clears.

Another service provided by banks is called stop payment. With a **stop payment**, the bank is instructed not to honor a check you wrote or lost. The bank charges a fee for this service, often $25 or more per check. If the check has not already been processed, it will not be honored by the bank.

A **cashier's check** is a check issued against bank funds. When you buy a cashier's check, the money comes from your account to pay the bank. The money for the payee of the cashier's check comes from the bank's account. Some people prefer to receive a cashier's check rather than a personal check because a cashier's check is more secure. The check will not bounce because the money is set aside and waiting to be paid by the bank.

Some banks issue money orders. A **money order** is a type of check used to pay bills or make a payment for which the money is guaranteed. There is usually a fee for this service, based on the amount of the money order.

Some banks and credit unions also offer personal financial advising services. They look at your goals and resources and sell you financial products, such as mutual funds. Before investing, check options on your own. Be sure the funds and other products have been in existence for a long time and have performed well over time.

Banks offer loans to their depositors. Credit unions offer loans to their members. Because credit unions are nonprofit organizations, members may get lower interest rates on loans. Some examples of the types of loans provided by banks and credit unions are home mortgage loans, car loans, and personal lines of credit.

Technology Corner

Internet Banking

Many banks allow their account holders to have Internet and telephone access to their accounts. An access code or PIN number along with a user name is needed. Customers can view their accounts at almost any time on any day. Banks typically will close access to accounts for several hours on the weekend so that they can update their systems. Accounts cannot be accessed during this time for online banking.

Internet banking may offer other services, such as those in the following list:

- Paying bills electronically
- Transferring money between accounts, such as from checking to savings
- Monitoring activity in an account
- Checking that deposits are posted
- Seeing which checks have cleared (have been processed)
- Seeing interest or fees that have been posted

Many people think that banking via the Internet is as safe as writing paper checks. When deposits and withdrawals are made electronically, nothing can get lost in the mail. Account holders can see when checks and deposits have been processed and exactly how much is in an account at any time.

Some financial institutions offer car buying services. For a fee of about $500, the company will find and buy the new or used car of your choice. This saves you the hassle of negotiating the price for the car. Basically, you are paying the company to negotiate on your behalf. In many cases, the bank or credit union is able to get a better price than you can.

Bank Cards

Banks and credit unions issue several types of bank cards. These cards have special features and are electronically coded. This allows you to use them for purchases, cash advances, and deposits.

Banks may issue credit cards to their customers who qualify and want this service. These cards often have interest rates that are both fixed and low. Because you are a customer, you may also be offered a high credit limit.

ATM cards and debits cards, discussed earlier in the chapter, are two other types of bank cards. Making a purchase with a debit card usually does not involve a fee. Using an ATM card may involve a fee. Many banks will allow you to use their own ATMs free of charge. If you use an ATM from another bank, however, the other bank will charge you a fee of $2 or more. Your own bank may charge you another fee of $2 or more.

Similar to debit and ATM cards, a smart card carries an electronic balance on the card. These cards can also be purchased at stores in the form of gift cards that can be renewed. You deposit money to the smart card electronically when you purchase or renew the card. When the money is spent, you can add more money to the card and continue using it. The advantage of a smart card is that it is not linked to your checking account, and if it is lost or stolen, the thief cannot access your account.

5-2 REVIEW

5-2 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. What is the purpose of a savings account?
2. What is the sum of money set aside on which interest is paid called?
3. What is the formula for calculating simple interest?
4. How does compound interest differ from simple interest?
5. How do a certificate of deposit and a money market account differ from a regular savings account? How are they the same?
6. Why is a U.S. savings bond considered a safe form of saving?
7. What is the purpose of an IRA? What types of companies offer IRAs?
8. How do the amount of time you have to save and the interest you can earn relate to achieving financial goals?
9. What is the Rule of 72 that is related to saving?
10. List some other services banks may provide for customers in addition to checking and savings accounts.

5-2 Activity 2 Compute Interest

1. Selena has placed $500 in an account that pays simple interest of 5 percent annually. How much interest will Selena have earned by the end of the year?
2. Suki has placed $800 in an account that pays 4 percent interest compounded quarterly. What will be the balance in the account at the end of 2 years (8 quarters)? How much interest will Suki have earned during that time? Round your answers to the nearest cent.
3. Jessica is considering putting her money ($50) into a $100 paper U.S. savings bond. Assume the guaranteed rate of interest is 4 percent. How long will it take for the money to double (reach $100)? Use the Rule of 72 to find the answer.

5-3

The Federal Reserve System

OUTCOMES

- Describe the purpose of the Federal Reserve System.
- Define *monetary policy* and discuss goals of U.S. monetary policy.
- Explain how the Federal Reserve System controls the banking industry.
- Identify the types of interest rates controlled by the Federal Reserve System.

INTRODUCTION TO THE FEDERAL RESERVE SYSTEM

The Federal Reserve System is the central bank of the United States. It is commonly called the Fed. The Fed was created by Congress in 1913. Its purpose is to provide the nation with safe, flexible, and stable monetary and financial systems. The system has a seven-member Board of Governors. Its headquarters is in Washington, D.C. The Fed also has 12 regional banks located in major cities across the United States. The 12 Federal Reserve districts are shown in Figure 5.3-1 on page 147.

The seven members of the Board of Governors are nominated by the President. They are confirmed by the U.S. Senate to serve 14-year terms of office. Members may serve only one full term. The President also chooses two members to be the Chairman and the Vice Chairman, for four-year terms. These terms may be renewed by the President.

ROLES OF THE FED

The Fed's activities are in four general areas as listed below. These areas are discussed in the sections that follow.

- Conducting monetary policy
- Providing financial services to the U.S. government, financial institutions, and the public
- Supervising and regulating banking
- Keeping the country's financial systems and markets stable

Conducting Monetary Policy

An important role of the Fed is conducting monetary policy. **Monetary policy** refers to actions of the Fed to influence money and credit conditions

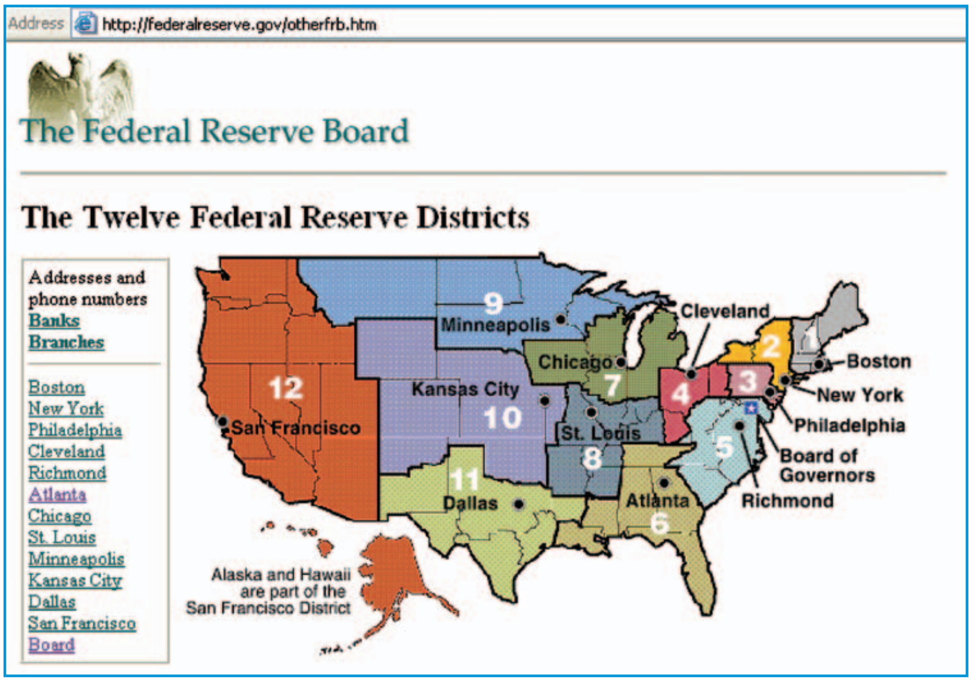


FIGURE 5-3.1

THE FEDERAL RESERVE SYSTEM DISTRICTS

Source: Federal Reserve Board, The Twelve Federal Reserve Districts, http://federalreserve.gov/otherfrb.htm (accessed April 27, 2006).

in the economy. These conditions affect employment levels and prices. The Fed tries to speed up or slow down the economy as needed to keep employment high and prices stable. The Fed watches the economy. When prices are rising too fast, it tries to slow down spending. This helps curb inflation. One way to slow down the economy is by raising interest rates. When interest rates rise, both individuals and businesses find it more expensive to borrow money to buy more goods and services. This slows down spending. (As you may recall from Chapter 3, demand-pull inflation is caused by spending in the economy.)

INTEREST RATES

Several types of interest rates are controlled by the Fed:

- The **discount rate** is the rate that banks have to pay to borrow money from the Fed. Banks borrow money when they have the opportunity to make loans but do not have enough cash on hand. Banks are required to have a certain amount of cash on hand, called reserves. If these reserves go below the required amount, banks must borrow money.
- The **federal funds rate** is the rate at which banks can borrow from the excess reserves of other banks. For example, if one bank has more money than it needs, it can loan that extra money to other banks.
- The **prime rate** is the rate that banks charge to their most creditworthy business customers. When the discount rate increases, the prime rate also rises. The prime rate is often 3 percent (or more) higher than the discount rate or the federal funds rate.

When the Fed raises the discount rate, this causes interest rates to rise on all levels. For example, when the discount rate is 3 percent and the Fed raises it to 3.25 percent, the prime rate may go up from 6 to 6.5 percent or more. Consumers are charged higher interest rates (than the prime rate) on money they borrow. When the prime rate is 6 percent, consumers are probably paying 9 percent or more. Thus, with a 0.25 percent increase in

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Interest rates on loans change as the Fed raises and lowers its rates.

the discount rate, the rate that consumers pay will likely rise from 9 percent to 12 percent. These interest rate increases have a slowing effect on borrowing and thus on spending.

The Fed affects the money supply by changing interest rates. The money supply, also called the money stock, is made up of currency (coins and bills) held by the public. It also includes deposits held by the public in banks and other institutions, money market funds, and other deposits.

When the federal funds rate falls, short-term market interest rates also fall. The short-term market interest rates may be below the rates paid on deposits at banks. This is because changes in bank rates tend to lag behind changes in market rates. The public tends to increase deposits at the banks to get the higher rates. This means the money supply increases. However, when the federal funds rate goes up, so do other short-term interest rates. The rates paid at banks become less attractive, and money growth slows.

OPEN-MARKET TRANSACTIONS

The Fed is also responsible for selling and buying back U.S. government securities such as government bills, notes, and bonds. This activity is called open-market transactions. Consumers can buy bills, notes, and bonds from the TreasuryDirect Web site.

Government bills, also known as Treasury bills, are short-term debt, up to 26 weeks. Buyers of these bills loan money to the federal government at a set interest rate. When the Fed sells Treasury bills to consumers, savings by consumers increase. In other words, people or businesses that buy Treasury bills are saving their money rather than spending it. This slows down the economy. When the Fed buys back Treasury bills, the money is available for spending. This speeds up the economy.

Treasury notes are medium-term debt. Notes are issued for 2, 3, 5, and 10 years. Treasury bonds (like savings bonds) are long-term debt (30 years) at fixed rates. Once again, selling Treasury notes and bonds takes money from the economy, and buying them back puts money into the economy. These open-market transactions are tools used by the Fed to regulate the economy.

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The Fed is in charge of our nation's money supply.

Providing Financial Services

The Fed plays a major role in operating the country's payment systems. For example, the Fed is responsible for printing money. As bills get old and worn, they are destroyed, and new bills are printed.

The 12 reserve banks act as a clearinghouse for checks that are written on banks in the United States. Processing of checks is rapid. Today, you can expect that checks may clear your account the same day they are received by a business. Many businesses turn a check into an electronic deduction from your account. The Fed allows this to happen.

Regulating the Banking Industry

The Fed is empowered by Congress to control the banking industry. All banks that have interstate (in more than one state) operations are required to be member banks of the Fed. Banks that are intrastate (state-chartered) only do not have to belong to the Fed. However, all banks are subject to the rules and regulations of the Fed. These include credit policies, minimum payments, and other lending policies.

One important policy is called the reserve requirement. It means that banks must keep on hand a percentage of deposits by customers. When the reserve requirement is raised, banks have less money to lend. When the requirement is lowered, banks have more money to lend.

Maintaining Stability

Keeping the financial systems and markets in the United States stable is another role of the Fed. This role is carried out through the routine activities of the Fed. Supervising banks helps ensure that the banking system is safe and sound. This promotes consumer confidence in the system. The Fed operates key parts of the payment systems. It also oversees operation of the payment systems in general. This oversight helps keep the systems stable. The Fed uses monetary policy, as discussed earlier, to help keep the economy stable.

Actions of the Fed affect financial decisions made by consumers in this country. By raising and lowering interest rates, the Fed influences how willing people and companies are to buy goods. Will you buy a new car or house? Will you put savings in a bank, buy bonds, or invest

Building Communications Skills

Reading Comprehension

Good reading skills will help you be more productive at school, at work, and in personal activities. Comprehension is the ability to understand what you have read. Reading for comprehension is also called study reading. The goal of this type of reading is to learn and to remember what has been read.

To help improve reading comprehension, read slowly and think about what you are reading. Written material is divided into passages. A passage is a group of paragraphs. Paragraphs are used to introduce and explain ideas. Paragraphs often have a common structure. The first sentence of a paragraph is the topic sentence. It tells you what the paragraph is about. The middle sentences explain the topic. The last sentence of a paragraph sums up or draws a conclusion. To improve understanding as you read, think about the purpose of the paragraph and how it relates to the overall topic of the passage.

Many people take notes of major points in each paragraph. Underlining or highlighting can help identify key points when you are reviewing the material. Comprehension can be improved when you read passages more than once. The first time, look for main ideas and points being made. The second time, focus on vocabulary and details.

in the stock market? Will you start a new company? Will a business expand operations by building a new plant? The answers to these questions are affected by how costly it is to borrow money. They are also affected by what consumers and companies think about the economy. If they think the economy is stable and growing, they are more likely to spend on goods and services.

5-3 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. What is the Fed? When was it created, and what is its purpose?
2. The Fed's activities are in what four general areas?
3. What is the meaning of the term *monetary policy*?
4. What is the discount rate? The federal funds rate? The prime rate?
5. How does the Fed control the money supply in the United States?
6. How do open-market transactions for U.S. government securities affect the economy?
7. What types of banks must be members of the Federal Reserve System? Are banks that are not members also regulated by the Fed?
8. What is a bank reserve requirement?

5-3 Activity 2 The Fed

INTERNET www.thomsonedu.com/school/pfl

1. The Federal Reserve System requires national banks to be members. There are also state-chartered banks and credit unions that are not required to join the Fed. Even though non-member banks do not belong to the Fed, how are you (the depositor) protected at these banks?
2. Refer to Figure 5-3.1 on page 147. In which city is the Federal Reserve bank that serves the area where you live?
3. Who is the chairman of the Federal Reserve System? Access the Internet and search for this information if you do not know the answer.

EXPLORING CAREERS IN ARTS, A/V TECHNOLOGY, AND COMMUNICATIONS

Do you have artistic or musical talent? Is performing on stage your dream? Do you like to write stories with complicated plots? Do you like to find interesting ways to share information in print or video? If the answer is yes, a career in arts, A/V technology, and communications might be right for you. Jobs in this area are varied. Some workers in this field use their talents and skills to write, sing, make music, or perform on stage. Others use print, video, and technology to share creative messages. Artists, sculptors, photographers, and animators also work in this career area.

Jobs in this career area are found in government and businesses. Many people in the visual arts field, such as painters, photographers, and animators, are self-employed. They work on a freelance basis and sell their services or products to businesses and consumers. The need for jobs in arts, A/V technology, and communications varies by career area. Employment in some jobs will grow; in others, it will decline.

Skills Needed

Some of the skills and traits needed for a career in arts, A/V technology, and communications include the following:

- Communications skills
- Computer/technology skills
- Creative writing ability
- Natural talent for performing arts
- Decision-making skills
- Problem-solving skills

Job Titles

Many jobs are available in arts, A/V technology, and communications. Some job titles for this career area include the following:

- Actor/actress
- Camera operator
- Desktop publisher
- Electrical engineer
- Graphic designer
- News reporter
- Playwright
- Sound technician
- Telecommunications equipment installer

Explore a Job

1. Choose a job in arts, A/V technology, or communications to explore further. Select a job from the list above, or choose another job in this career area.
2. Access the *Occupational Outlook Handbook* online. A link to the site is provided on the Web site for this textbook.
3. Search for more information about the job you selected to answer these questions:
   - What is the nature of the work this job involves?
   - What is the job outlook for this job?
   - What training or qualifications are needed for this job?
   - What are the median annual earnings for this job?

CHAPTER 5

Review

Summary

- A checking account is a demand deposit that allows you to access your money quickly and easily.
- A checkbook register is a record of checks written, deposits and other withdrawals made, and other charges to a checking account; it must be reconciled with the bank statement.
- Checks that are to be included in a deposit must be properly endorsed.
- Automatic deposits and automatic withdrawals are the electronic transfer of funds into or from an account.
- Fees charged on checking accounts include fees for ATM withdrawals, monthly fees, fees for checks written, and NSF check fees.
- To protect your account data, keep checks in a safe location. When making a purchase or withdrawing cash with a debit card or an ATM card, protect your PIN or password and account number.
- A savings account is a demand deposit that may have some restrictions about how quickly or easily money can be withdrawn.
- A certificate of deposit or money market account offers higher interest rates than a regular savings account, but it is also less liquid.
- A U.S. savings bond is a good way to save if you can invest the money for a long term.
- A sum of money set aside on which interest is paid is called principal. The Rule of 72 calculates how quickly principal earning interest at a certain rate will double.
- The calculation for simple interest is Interest = Principal × Rate × Time. With compound interest, interest earned is added to the principal and also draws interest.
- Banks may offer services such as safety deposit boxes, overdraft protection, stop payment, cashier's checks, money orders, loans, bank cards, car buying services, and financial advice.
- The Federal Reserve System (Fed) is the central bank of the United States. It controls the money supply in the United States and sets interest rates.
- The Fed sells and buys back U.S. government securities, including notes, bills, and bonds.
- The Fed regulates the banking industry, including credit and lending policies.
- The Fed sets the reserve requirement, which gives banks more money or less money to lend.

Key Terms

automatic deposit
automatic withdrawal
bounced check
cashier's check
certificate of deposit
check
checkbook register
checking account
compound interest
debit card
deposit
discount rate
endorsement
federal funds rate
monetary policy
money market account
money order
postdated check
prime rate
principal
Rule of 72
savings account
stop payment
U.S. savings bond

ACTIVITY 1
Review Key Terms

Use the key terms from Chapter 5 to complete the following sentences:

1. Money electronically added to your checking account is called a(n) ______________.
2. A bank card that allows the account holder to make purchases and to withdraw cash from an account at an ATM is called a(n) ______________.
3. A math formula called the ______________ is used to tell you how long it will take money earning a certain interest rate to double.
4. A demand deposit called a(n) ______________ allows you quick and easy access to your money without penalties.
5. A discount bond issued through the United States government is called a(n) ______________.
6. A(n) ______________ is a convenient way to pay bills if you do not have a checking account.
7. ______________ is interest earned on both principal and previous interest earnings.
8. A(n) ______________ is a check issued by a bank against its own funds.
9. A bank service directing the bank not to honor a check is called a(n) ______________.
10. The interest rate that banks charge to corporations, called the ______________, is for the most creditworthy customers.
11. A record for keeping track of checks written and deposits made is called a(n) ______________.
12. A check written with a future date is called a(n) ______________.
13. The rate at which banks can borrow from the excess reserves of other banks is called the ______________.
14. A(n) ______________ is a signature or instructions written on the back of a check authorizing a bank to cash or deposit the check.

15. A savings option called a(n) ____________ pays interest at the current market rate.
16. A(n) ____________ is a written order to a bank to pay the stated amount to the person or business named from a certain account.
17. The ____________ is the rate banks are charged to borrow money from the Fed.
18. A check returned by the bank, called a(n) ____________, was returned because there was not enough money in the account.
19. Actions of the Fed to influence money and credit conditions in the economy are called ____________.
20. A(n) ____________ is money deposited for a fixed amount of time at a fixed interest rate.
21. An amount of money set aside (deposited or borrowed) on which interest is paid is called the ____________.
22. A demand deposit called a(n) ____________ may have restrictions and/or penalties for taking out money.
23. A(n) ____________ is money added to a checking or savings account.
24. A(n) ____________ deducts money from an account and electronically transfers it to another party.

ACTIVITY 2
Math Minute

When interest is compounded, interest earned is added to the principal before interest is calculated again. Use spreadsheet software to complete these compound interest problems, if it is available. If not, complete the problems manually. Round to the nearest cent.

1. Gloria has an account that draws interest at the rate of 6 percent per year, compounded monthly at 0.5 percent. The following amounts were deposited in the account in the current year. What is the balance in the account on December 31 of the current year?

June 1	\$50
July 1	\$50
August 1	\$50
September 1	\$50

2. Yoshi has an account that draws interest at an annual rate of 5 percent. The interest is compounded quarterly. The following amounts were deposited in the account in the current year. What is the balance in the account on December 31 of the current year (after four quarters)?

January 1	\$450
April 1	\$350
July 1	\$200
September 1	\$300

ACTIVITY 3
Checkbook Register

Open and print the PDF file *CH05 Register* from the data files. For each transaction, record the information in the register. Then write the check or complete the deposit slip if one is needed for the transaction. Use the current year in dates. Keep a running balance, and double-check your work. The ending balance should be $87.38.

1. Beginning balance $218.33
2. Check No. 401 on April 1 to Westside Services $15.00 for haircut
3. Check No. 402 on April 5 to J. Jill $28.50 for new shirt
4. Cash withdrawal at ATM for $20.00 on April 8
5. Deposit of $25.00 cash on April 10 (gift from uncle)
6. Debit card purchase (DC) of $19.50 on April 11 at Rowe's for food
7. Check No. 403 on April 15 to Bill Baxter $35.00 for loan payment
8. Cash withdrawal at ATM for $20.00 on April 18
9. Debit card purchase of $9.95 on April 25 at Aston Theater for movie
10. Bank service charge on April 28 for $8.00

ACTIVITY 4
Saving for the Future

Setting aside money (saving) for the future is known as deferred spending. You are setting aside money today so that you will have it when you need it. Most financial planners recommend you save 10 percent or more of your earnings. This is a good first step toward your retirement. Use spreadsheet software to complete the following problems if available, or complete them manually. Round to the nearest cent.

1. Assume you will earn $25,000 in gross pay the first year you work. Each year after that, you will get a 3 percent increase in pay. How much money will you have earned in 10 years?
2. Assume that during the 10 years discussed in problem 1, you set aside 10 percent of your earnings as savings. You estimate you can get an average of 5 percent (simple interest) yield per year return on your savings. How much money will you have saved in 10 years?

   Example:

Year	Earnings	Savings	Interest	Total Savings and Interest
1	$25,000.00	$2,500.00	$ 125.00	$ 2,625.00
2	$ 25,750.00	$ 2,575.00	$260.00	$5,460.00

ACTIVITY 5
Online Banking

www.thomsonedu.com/school/pfl

Online banking is offered by many banks. Customers may have to pay a fee for online banking services. However, using online banking saves on postage and ensures that bills are paid on time—thus avoiding late fees.

1. Work with a classmate to complete this activity. Access the Internet and enter the term **online banking** in a search engine. This search should return a list of several banks that have online banking. You can also search using the name of a local bank to see if it has a Web site available.
2. Visit the Web sites for three banks or credit unions, and learn about their online banking. Answer the following questions about each bank or credit union:
   - What is the name of the bank?
   - Is online banking available?
   - Does the bank charge a fee for online banking? If so, how much is the fee?
   - What activities can the customer do through online banking?
3. Compare the results of your findings for the three banks. Which bank do you think has the best overall plan or services for online banking? Why?

ACTIVITY 6
Choosing an Account

Read the following descriptions for two types of checking accounts. Which one would fit your needs better? Why?

Special Student Account

- No minimum deposit required
- No monthly service fee
- ATM card provided; no fee for use at this bank's machines; $2.00 fee for use at other ATMs
- 15-cent fee for each check processed
- $2.00 flat fee for talking with a bank teller

Interest Plus Account

- Minimum deposit $1,000.00
- No monthly service fee
- ATM/debit card provided; no fee for use at this bank's machines; $2.00 fee for use at other ATMs
- No per-check fee
- Pays current rate of interest (0.5 percent)
- Automatic paycheck deposit
- No charge for talking with a bank teller

ACTIVITY 7
Bank Reconciliation

Use the following information to prepare a bank reconciliation. Use a format similar to that in Figure 5-1.5 for the reconciliation.

Bank reconciliation date 4/4/20- -

Account no. 589125

Bank statement balance on 3/30/20- - $629.64

Checkbook register balance on 4/4/20- - $687.50

Outstanding checks

4/1/20- -	Check 498	$20.00
4/5/20- -	Check 499	$28.50

Deposit in transit dated 4/2/20- - $97.36

Bank fee for checking account $9.00

ACTIVITY 8
Government Bonds

INTERNET www.thomsonedu.com/school/pfl

Government bonds can be researched and purchased on the TreasuryDirect Web site.

1. Visit the TreasuryDirect site. A link to the site is provided on the Web site for this textbook.
2. Find information for three types of bonds: I Bonds, EE Bonds, and HH Bonds. For each type, find the following information:
   - The bond name
   - A brief description of the bond
   - The current interest rate paid on the bond
   - The minimum purchase amount
   - The maximum purchase amount per year

CHAPTER 6 Personal Risk Management

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Chapter 6 is about managing risks. In this chapter, you will learn about the risks you face, how serious they are, and what you can do about them. Buying insurance is one option you can choose to help protect against risks. When you decide the risk is serious and the possible losses are great, then you might choose to transfer the risk. Income protection is one type of insurance. Health and life insurance are two good ways to protect income. Property can also be protected. Homeowner's or renter's insurance protects against loss of your house and personal items. Car insurance protects you from losses that might occur to your car and because of your car.

ONLINE RESOURCES

Personal Financial Literacy Web site:

- Vocabulary Flashcards
- Beat the Clock: Risk Management
- Chapter 6 Supplemental Activity

Search terms:

- risk
- insurance
- probability
- premiums
- liability insurance

6-1

Risk Assessment and Strategies

OUTCOMES

- Explain the concept of risk.
- List the three types of risk.
- Explain what is meant by *risk assessment.*
- Discuss four risk strategies.

WHAT IS RISK?

Risk is the chance of injury, damage, or economic loss. Driving a car and snow skiing are examples of behaviors that involve risk. When you are driving a car, an accident with another car might occur. This accident could cause personal injury and damage to the car. You might have an accident while snow skiing, such as breaking your leg. There are many types of risk you will face now and in the future. Some risks are avoidable and have a small chance of happening. Other risks are unpredictable and unavoidable. Some risky events may cause serious losses if they happen.

A **loss** refers to some type of physical injury, damage to property, or absence of property or other assets. The loss might be personal in nature, such as a broken leg or an illness. The loss could be damage or removal of money or property. For example, you might lose money or property as a result of theft. Losses could be major and could have a significant effect on your future. Losing your job could mean that you cannot make payments on your house or car. This event could cause you to lose your house or have your car repossessed.

The likelihood of a risk actually resulting in a loss is called **probability**. Just because you take a risk does not mean you will always suffer a loss, nor does it mean you can always avoid a loss. You must decide whether or not the risk and its possible outcome are serious. If the possible loss is serious, you may be able to take steps to lessen the risk or the resulting loss.

Personal Risk

Taking personal risk means you could lose something of personal value to you. For example, you might break your leg and then not be able to participate in an activity you really enjoy. Some personal risks are necessary. If you do not get out of bed in the morning, you can avoid many risks. However, not getting out of bed also means you will accomplish little. If you do not wear your coat and boots when it is cold and raining, you risk getting wet and cold. This may increase your chances of getting sick. The costs and outcomes of getting sick may not be serious if you are young and likely to recover quickly. For some people who have chronic illnesses, however, this personal risk must be taken seriously because the outcome can be deadly.

Risk of Financial Loss

Some risks will result in financial loss. Financial loss refers to a cost in terms of money. The loss can be big or small. Small possible losses should be assessed differently from large possible losses. For example, if you drive without a spare tire, you risk being unable to change a flat tire. Driving without a spare tire could be expensive if you have a flat and must pay someone to help you. The money you could lose must be compared to the cost of buying the spare tire. A large loss might result from driving without car insurance. If you get into an accident, the damage you could do to another vehicle or property could cost thousands of dollars. You might have to pay this money if you have no insurance. In some states, drivers are required to have insurance. If you drive without insurance, you risk being caught and having to pay a fine. Repeated offenses may result in losing your driver's license. Information about mandatory auto insurance for Washington state is shown in Figure 6-1.1.

© Getty Images/PhotoDisc

Snow skiing involves risk of personal injury.

Risk of Financial Resources

Risk of future resources is a serious kind of risk; it could jeopardize your future. With this type of risk, more than current income is threatened. You may lose your ability to earn in the future or assets you acquire in the future. For example, you might do something that causes an injury to another person. That person might sue you and win a financial judgment. This means that the court orders you to pay the person a certain amount of

FIGURE 6-1.1

Many states require drivers to have automobile insurance.

Source: Washington State, Office of the Insurance Commissioner, Mandatory Auto Insurance Law, http://www.insurance.wa.gov/factsheets/factsheet_detail.asp?FctShtRcdNum=5 (accessed May 3, 2006).

money. Because of the judgment, you could have your wages garnished or your assets taken away. This type of risk has a very grave outcome and should always be taken seriously.

RISK ASSESSMENT

The first step toward managing risks is assessing your risks. That means identifying what the risks are and deciding how serious they are. When you understand your risks and what you have to lose, you can make better choices. You may be able to take action to protect yourself from the serious outcomes that you could face.

To assess your risks, you must first understand them. Figure 6-1.2 shows an example of risk assessment. It lists the types of risks faced by Sally Edwards. It shows the probability of each risk, and each risk is rated in terms of seriousness. Finally, the chart lists the worst that could happen if the loss did occur.

RISK STRATEGIES

When the risk is serious, you will want to take some type of action to protect yourself. There are a number of ways to do this, such as reducing risk, avoiding risk, transferring risk, and self-insuring against risk.

Reducing Risks

The first strategy to consider is how you can lower the risk. Reducing risk means finding ways to change actions or events so that your chance for loss is less. For example, when you go snow skiing, you are taking a risk of personal injury. To reduce that risk, you could take skiing lessons. You could reduce your risk of financial loss by having health insurance to pay for any injuries you might suffer.

Avoiding Risks

If you decide that you cannot effectively reduce risk and that the potential harm is serious, you might choose to avoid the risk. Avoiding risk means

FIGURE 6-1.2

RISK ASSESSMENT FOR SALLY EDWARDS

Risk	Probability of Occurrence	Seriousness Rating*	Possible Consequences
Losing my job	Medium	10	Payments could be missed. Credit rating suffers.
Car accident	Unknown	10	Personal injury Lawsuit
Physical injury from snowboarding	Medium	3	Missed work time Medical bills
Having bike stolen	Low	2	Have to buy new/used bike.

* 1 is a low risk; 5 is a medium risk; 10 is a high risk

you stop the behavior or avoid the situation that leads to the risk. In terms of snow skiing, you would choose not to take part in that activity. This would avoid the risk of injury from an accident.

Sometimes, however, avoiding the risk means that you must not do things you really want or need to do. In this case, you might consider other risk strategies.

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Having a home security alarm system may reduce premiums on homeowner's insurance.

Transferring Risks

When you face substantial risk that you cannot or do not wish to reduce or avoid, transferring risk is a good idea. You transfer the risk by buying insurance. The insurance company pays for the loss should it occur. Thus, you are transferring the risk of loss to the insurance company. For example, you could buy a homeowner's insurance policy that provides coverage against theft. If items are stolen from your home, you will be paid for the value of the items taken.

The price you pay for insurance is called a **premium**. The premium could be paid monthly, quarterly, semiannually, or annually. The premium is based on the possible loss to the insurance company. The more risk the insurer must take, the higher the premium. Sometimes the cost of the premium is very high, and you will look for ways to reduce the cost of insurance. For example, your homeowner's insurance premiums might be lower if you have a home security alarm system. Your car insurance premium might be lower if you choose to drive a reliable family car instead of a sports car.

Assuming Risks

When the risk of loss is not great or when the cost of transferring the risk is too great in comparison to what you could lose, you might choose to **self-insure**. To self-insure means to set aside money to be used in the event of injury or loss of assets. Many people cannot afford to be totally self-insured. However, self-insurance is a good way for many people to assume responsibility for part of the risks they face. For example, you could choose not to have full-coverage automobile insurance on an old car. This will make your insurance premiums lower. If the car is destroyed in an accident that is your fault, you must pay to buy another car. However, your auto liability insurance would pay for damages to others that you cause in the accident.

Another option is to choose policies with high deductible amounts. The **deductible** amount is the money you must pay before your insurance company begins to pay. You could choose to have a health insurance policy with a high deductible. This would give you lower premiums. You would pay from your self-insurance fund for doctor visits or other routine care. However, if you have a serious illness that involves high medical expenses, your insurance policy would pay these bills. This allows you to assume the risk for small or routine expenses and have the insurance company assume the risk for large expenses.

Building Communications Skills

Reading Speed

Reading speed affects how much material you can read in a certain amount of time. It also can affect how well you remember or comprehend what you read. To be an effective reader, you must read at a pace that allows you to cover material quickly and still comprehend what you are reading. Use these strategies to help you be a more effective reader:

- Select reading material carefully. Choose material that is likely to be of the most value for your purpose for reading.
- Preview the material before reading.
- Do not skim or skip passages. Read everything in a passage, chapter, or book.
- Read in the order the information is presented.
- Adjust reading speed to suit the material chosen. Technical material or material with a difficult vocabulary may require slower reading. Summaries, review sections, or passages with easy vocabulary allow faster reading.
- Read groups of words at a time.
- Use a pacer to focus your eyes on the page. A pacer is a tool such as a pencil or ruler that you move along under the words being read.
- Read in a quiet place where your concentration will not be interrupted.

6-1 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. What is risk?
2. What are the three general types of risk discussed in this chapter?
3. What is meant by *risk assessment*?
4. List four strategies for dealing with risk.

6-1 Activity 2 Assessing Risks

Critical Thinking

Everyone faces risks—personal risks, financial risks, and resource risks. In this activity, you will think about some of the risks you may face.

1. Create a chart with the headings shown below. In the chart, list four risks that you face.

Risk	Probability of Occurrence	Possible Results	Ways to Reduce Risk

2. Estimate the likelihood of those events occurring. Add this information to the chart.
3. Think about and list the possible results if the risk events should happen.
4. Consider each possible risk that has serious consequences. List what you can do to (a) reduce risks, (b) avoid risks, (c) transfer risks, and/or (d) self-insure for the losses that you might suffer as a result of the risks.

6-2 Income Protection

OUTCOMES

- Explain the need for health insurance and the types of plans available.
- Describe types of coverage available in health insurance plans.
- List ways you can lower costs and manage health care spending.
- Explain the need for disability coverage and the types of plans available.
- Explain the need for life insurance and types of life insurance coverage.

HEALTH INSURANCE

Health insurance is a plan for sharing the risk of medical costs from injury or illness. People need health insurance to help pay high medical expenses. Many people cannot afford to pay medical costs without the help of insurance. Some people have group health insurance bought through their employers. Some people have individual policies.

Types of Plans

Three basic types of health insurance plans are available. Health insurance plans have many characteristics in common. The better the coverage, the higher the premiums will be. Some employers may pay for a part of medical insurance premiums. However, employees are often asked to pay part or all of the cost. This is because of high and rising costs for health care.

FEE-FOR-SERVICE PLANS

A fee-for-service plan allows patients to choose doctors and other providers for medical services. The insurance policy has a deductible. The insured pays expenses equal to the deductible amount. Then the insurance company pays a percent, such as 80 percent, for covered services. The insured must pay the remaining amount. For example, if a policy has a $150 deductible, that means the insured must pay the first $150 of medical expenses. Then the insurance company starts paying for part of the amount above the deductible.

A fee-for-service plan is often called unmanaged care. This type of coverage is often more expensive than managed care plans that offer fewer choices of doctors and other care providers.

PREFERRED PROVIDER ORGANIZATION PLANS

A preferred provider organization (PPO) is a group of health care providers (doctors, hospitals, clinics, and labs) that work together to provide health care services. Patients choose caregivers from approved lists. Lists include doctors, hospitals, clinics, and labs that will bill the PPO for services. If you use a doctor or medical facility that is not on the approved list, the plan may pay reduced benefits or no benefits. Thus, you should review the list of approved caregivers and facilities when considering a PPO. The PPO plan usually has a co-pay. A **co-pay** is an amount you must pay each time you use a medical service. Co-pays are often $15 to $30 per visit.

HEALTH MAINTENANCE ORGANIZATION PLANS

A health maintenance organization (HMO) is a managed care group plan that has prepaid medical care. HMOs usually have their own facilities (clinics and hospitals) and offer a full range of services. Patients must choose doctors on the HMO staff, including one doctor to be the primary care doctor. To see a specialist, patients must get a referral from the primary care doctor. HMOs usually do not have deductibles. Patients pay a co-pay for each visit.

Focus on . . .

Being Uninsured in America

According to the U.S. Census Bureau, 45.8 million Americans did not have health insurance in 2004. That number is about 15.7 percent of the total population.[1] Those numbers are growing every year.

The percentage of working-age Americans with middle-range incomes without health insurance rose to 41 percent in 2005.[2] Many people who are not insured have problems paying medical bills. They do not have insurance companies with negotiated rates and contracts, so they pay higher fees than patients who have insurance.

The term *working poor* refers to Americans who spend some time working but whose incomes fall below the poverty level. Many of these people have no health insurance benefits. They do not make enough money to pay for health insurance. They do not have enough money to access adequate medical care. These people often work for an hourly rate at less than full-time jobs.

The uninsured often do not get adequate health care. They do not get regular screenings or checkups. They often do not take needed medicines because they cannot afford to buy them. Many of these people have chronic health conditions, such as asthma or diabetes.

When you begin to work and support yourself, make having health insurance a priority. This should be an important goal in your financial plan. Having health insurance is a good way to protect against loss from medical expenses and to be sure you can afford the medical treatment you need.

[1] Carmen DeNavas-Walt, Bernadette D. Proctor, and Cheryl Hill Lee, U.S. Census Bureau, *Income, Poverty, and Health Insurance Coverage in the United States: 2004* (Washington, DC: U.S. Government Printing Office, 2005), p. 16.

[2] MSNBC News Services, "Many Middle-Income Americans Lack Insurance," April 26, 2006, http://www.msnbc.msn.com/id/12480260/ (accessed May 8, 2006).

An advantage to HMOs is their emphasis on preventive care. Preventive care includes routine physical exams and wellness programs. The goal is to help keep people healthy. Examples of preventive care include regular exams, dietary counseling, and a focus on healthy living.

Many health plans have call-a-nurse programs. A skilled nurse is available by phone to answer health-related questions. This service helps people make good choices regarding health care. Some health plans also have education programs to inform people about ways to stay healthy.

Types of Health Coverage

Several types of health insurance plans are available. Some plans provide coverage for basic health care. Other plans provided coverage for serious injury or illness. Plans to help pay for dental and vision care expenses are also available.

BASIC HEALTH CARE

Basic health care coverage includes medical, hospital, and surgery services. It pays for doctor fees, office visits, and lab work. Approved hospital costs and surgeries are also covered. Cosmetic and elective surgeries are usually not covered. Elective surgery is surgery you choose to have that is not medically necessary. A face-lift to improve appearance and laser eye surgery to improve vision are examples of elective surgery.

MAJOR MEDICAL

Major medical coverage protects against very serious injury or illness. It pays for services beyond basic health care. The coverage often goes to $1,000,000 or more. Examples of procedures covered include bone marrow transplants, organ transplants, and other care that often costs $500,000 or more.

DENTAL AND VISION

Many group plans provide dental coverage. Dental plans often have deductibles and co-pays. They may have a total yearly benefit, such as $2,000. A typical plan includes services such as exams, x-rays, and fillings. Other services, such as crowns, bridges, and braces, often are covered at a lower rate or not at all. Cosmetic dental work is usually not covered.

Vision coverage often provides for an eye exam and part or all of the cost of glasses. The insurance pays for lenses and frames and may even allow for prescription sunglasses. Some policies cover the cost of contact lenses, but often on a limited basis.

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Health insurance plans often include vision coverage.

CATASTROPHIC ILLNESS

Catastrophic illness policies provide protection should you get cancer or some other disease or condition that might cost hundreds of thousands of dollars to treat. If you have a family history of such a disease, you may not be able to get the insurance. You should buy this type of policy (and all policies) only from a well-known, reputable company. These kinds of policies are sometimes sold as scams. When you try to collect, you find that the company will not pay or no longer exists.

Managing Costs

The cost of health care is rising rapidly, making it difficult to pay rising premiums. Patients are paying higher co-pays and deductibles. Types of services provided are being limited. The cost of medicines is also rising. Many people are concerned about finding ways to manage the costs of health care. Whenever possible, patients should make sure medicines and treatments will be covered by their insurance before agreeing to use them. Some alternative or experimental treatments or medicines may not be covered.

DEDUCTIBLES AND CO-PAYS

When deductibles and co-pays are higher, premiums are often lower. Having higher deductibles and co-pays is one way to reduce health insurance premiums. Money must be set aside, however, to pay for expenses up to the deductible amount.

STOP-LOSS PROVISIONS

A **stop-loss provision** provides 100 percent coverage after a certain amount of money has been paid for medical expenses. For example, a policy may have a $5,000 stop-loss provision. This means that when you have paid $5,000 in deductible plus coinsurance payments in a year, your covered expenses are then paid at 100 percent. This amount is paid rather than the 80 percent or other rate the insurance company would otherwise pay. A stop-loss provision is a good feature to have in a health insurance policy.

HEALTH SAVINGS ACCOUNTS

A health flexible spending arrangement (FSA) allows people to set aside money to pay for qualified medical expenses. The money set aside is not included in the amount on which federal income taxes are paid. The plans are often set up by employers as an employee benefit. Deductions are made from the employee's pay to fund the account. The employer may also contribute. The employee files claims to be paid from the account for qualified expenses. Amounts not used by the end of the year are forfeited.

A health savings account (HSA) may also be set up individually rather than through an employer. This account is available to people with large deductibles, such as $1,000, on health care plans. The account holder puts money into an account (pretax). The money is then used to pay medical expenses. This reserve of money

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Medical emergencies can be very expensive.

is a form of self-insuring with a tax benefit. Money not used in one year is carried forward to the next year and continues to grow tax-free. The major advantage of this type of plan is that people manage their own health care dollars.

DISABILITY INSURANCE

Disability insurance provides money to replace a portion of normal earnings when the insured is unable to work due to an injury or illness that is not job-related. (If a person is injured at work or becomes ill because of work conditions, workers' compensation provides coverage.) If the disability is temporary, short-term disability insurance provides coverage. When the disability is for a longer period, long-term disability insurance provides coverage.

Short-Term Disability Insurance

Short-term disability insurance usually begins after a waiting period of 30 days. The disabled person receives a portion of regular pay (such as 75 percent) for a short period of time. This time usually is 6 months to 2 years.

Short-term disability insurance can be offered as a group policy. This type of coverage may be provided through an employer-sponsored health plan. It can also be bought as an individual policy. The coverage would likely be a part of a comprehensive health care package.

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Being unable to work for a long time can cause financial hardship.

Long-Term Disability Insurance

Long-term disability coverage usually begins in 6 months to 2 years. It continues until retirement. It pays a percentage of regular pay, such as 60 percent. The smaller the payment percentage, the lower the premium will be. Premiums are based on the age of the employee and his or her salary. This insurance may be provided through an employer. Individual policies can also be purchased.

LIFE INSURANCE

Life insurance pays money when the insured person dies. The purpose of life insurance is to provide money to a **beneficiary**, the person designated to receive money. Some types of life insurance also build cash value, acting as a form of savings plan. Some reasons why people buy life insurance follow:

- To pay off a home mortgage and other debts at the time of death
- To provide money for a spouse and children to maintain their lifestyle

- To pay for education for children
- To make charitable bequests at death
- To accumulate savings
- To pay inheritance and estate taxes
- To provide cash value that can be borrowed later

Two common types of life insurance are term and permanent. Term life insurance provides a death benefit only. It does not build cash value. Permanent insurance provides a death benefit and builds cash value. An annuity can also be a type of life insurance policy. It may provide a death benefit, but it is really a type of investment plan.

Term Life Insurance

Term life insurance is a policy that provides a death benefit. It is in effect for a specific period of time, such as 20 years. The insured must continue to pay premiums to keep the policy in effect. When the time period is over, the policy is no longer in effect. Term insurance is also called pure insurance because it does not build a cash value. If you have a 20-year term policy, you will have life insurance for 20 years. If you die within that time, the policy pays the stated sum, called the **face value**, to the beneficiary. If you do not die during the 20-year term, no insurance protection remains at the end of the term.

Renewable term insurance is life insurance that can be renewed every year or for some other time period. The insured has the right to renew the policy until reaching a certain age, such as 93 or 95 years. The age limit can vary by the company and the type of policy. At each renewal, the premium goes up (because the risk of death increases).

With decreasing term insurance, the amount of coverage goes down each year. The premium remains the same. This type of insurance recognizes that as time goes by, the need for insurance is less. This may be because children are now adults, debts such as a home mortgage are paid, and there are fewer needs for the insurance benefit.

With level term insurance, the death benefit does not change. However, the cost of the premiums goes up each year. This is because the policyholder gets older, and the risk of death is greater.

An advantage to term insurance is lower premiums than for a permanent policy. A disadvantage to term insurance is that it does not build cash value that can be withdrawn or borrowed against. However, the policyholder could invest the amount saved on premiums. The money invested would likely grow at a faster rate and result in more savings than the cash value of a permanent policy.

Permanent Insurance

There are several types of permanent life insurance. **Permanent life insurance** provides a death benefit and builds cash value. When a life insurance policy has a cash value, the insured can borrow against the policy. With some policies, the insured can cash in the policy. This means that the policyholder will receive the cash value of the policy, and the insurance benefit will no longer be in effect.

WHOLE LIFE

A common type of permanent insurance is called whole life insurance. It is also known as straight life or ordinary life insurance. The insured pays

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Life insurance can provide benefits for children when a parent dies.

premiums as long as the policy is in effect. There is usually an age limit, such as 93 or 95 years, for how long the policy will remain in effect. The policy pays the face value to the beneficiary at the death of the insured. Life insurance benefits are not taxable to the beneficiary.

The amount of the premium depends on the age of the insured at the time the policy is purchased. The premium is high enough to pay for the death benefit and also to add to the policy's cash value. The cash value can be borrowed against by the insured. This type of loan does not have to be repaid, but it lowers the death benefit when the insured dies. The insured can choose to repay the loan.

LIMITED-PAY LIFE

Limited-pay life insurance is a policy on which the insured pays premiums for a limited period of time, such as 20 years. At the end of the period, the policy is paid up. The insured pays no more in premiums, but the life insurance remains in effect until the age limit of the policy. The policy will pay the face value when the insured dies as long as it is in effect. This type of life insurance also builds cash value.

UNIVERSAL LIFE

Universal life insurance provides a death benefit. However, the premium and death benefit are not fixed. The policyholder can change the death benefit and the premiums during the life of the policy. The advantage of this type of plan is that it allows the policyholder to adjust the death benefit and premiums to fit changing needs.

VARIABLE LIFE

Variable life insurance is a form of permanent insurance that provides a death benefit and builds cash value. The premiums are fixed. Part of the premium is invested in securities chosen by the policyholder. The rest of the premium is used for life insurance. The advantage of this type of policy is that the insured can decide how part of the premiums will be invested. The disadvantage is that the death benefit can vary depending on how well the investments do. However, a minimum death benefit is often guaranteed. Also, the insured cannot withdraw the cash value of the policy.

Group Life Insurance

When a life insurance policy is purchased through an employer or an organization, this is called **group life insurance**. Group life insurance has much lower premiums than individual policies. Individual policies are more expensive because there is more risk to the insurance company. With a group policy, a large number of people are insured. This lowers the risk to the insurance company and thus provides better coverage at lower prices.

Sometimes life insurance policies are portable. **Portable insurance** can be taken with you when you leave your job. In other words, the group policy becomes an individual policy at the same premiums. Having this feature makes it possible for people who would not otherwise qualify to have life insurance.

Success Skills

DEALING WITH PEOPLE IN DIFFICULT SITUATIONS

Whether you in a meeting, at a sporting event, or at a family gathering, you may find yourself in a situation in which someone is causing problems. Usually the problem is about attitude. One person does not want to cooperate or go along with the group activity. Instead, she or he wants to disrupt and ruin the activity for others.

Strategies for dealing with people in difficult situations start with focusing on the person causing the problem. First, consider who the person is. The person may be someone you do not have to see or deal with beyond the current situation. If this is the case, the best option may be simply to ignore the person's negative comments or bad behavior and continue with the activity. Is the person a customer, a neighbor, or a relative? If so, this should affect how you will approach the situation. You may have no choice but to deal with the person. Try to keep the goodwill of the person and continue the activity in spite of the person's poor behavior.

Regardless of who the person is, there are some techniques for dealing with people in difficult situations that work for everyone. Listen to what the person is saying, and repeat the concerns. Meeting the person in a private setting to discuss the issues may be helpful. Ignoring a problem does not make it go away. Deal with the issues head-on. This is a good way to keep the problem from getting worse. Ask the person to explain his or her position or situation. Ask for suggestions about how the problem could be resolved. Talk to others affected by the behavior. Find out what changes they would like to see. Bringing the situation to the front and dealing with it is often the best way to resolve it.

6-2 REVIEW

6-2 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. Why do many people need health insurance?
2. What types of health insurance plans are available?
3. Describe the types of coverage available in health insurance plans.
4. What are some things you can do to help manage health care costs?
5. What is the purpose of disability insurance? How is short-term disability insurance different from long-term disability insurance?
6. List some reasons why people buy life insurance.
7. What is the main difference between term and permanent life insurance?
8. What is the face value of a life insurance policy?
9. Why are premiums for a group life insurance policy lower than for an individual life insurance policy?

6-2 Activity 2 Income Protection

You should consider several factors when deciding what type of insurance to buy. Read the following situations, and identify the type of insurance or insurance plan feature you think is right for each one.

1. You want a health insurance plan that will have low premiums and will allow you to self-insure for routine medical costs. What insurance plan feature should you request?
2. You want a health insurance plan that will pay 100 percent of covered medical expenses after a certain amount of money is paid toward medical expenses. What feature should you request?
3. You want a health insurance plan that will provide coverage should you get cancer or some other disease or condition that might cost hundreds of thousands of dollars to treat. What type of policy should you buy?
4. You want a life insurance policy on which the premiums will be as low as possible for the next 10 years. What type of insurance should you buy?
5. You want to choose how part of the premiums you pay for life insurance will be invested. What type of policy should you buy? What risk do you face with this type of plan?

6. You want a life insurance policy that will stay in effect for 10 years after you retire. However, you do not want to pay premiums after you retire. What type of policy should you buy?
7. You are considering whether to buy a whole life or a term life insurance policy. The death benefit will be the same for each policy. The premiums for the whole life policy will be $600 per year. In 40 years, you will be able to withdraw the cash value of $50,000 from the policy. The premiums for the 40-year term policy will be $200 per year. You can invest the money you save on premiums. You will receive an average annual return of at least 6 percent on the money you save for the next 40 years. Which option would you choose? Why?

6-3

Property Protection

OUTCOMES

- Explain the need for homeowner's insurance and the types of coverage provided.
- Explain the need for renter's insurance.
- Explain the need for automobile insurance and the types of coverage provided.
- Describe the purpose of an umbrella policy.

HOMEOWNER'S INSURANCE

A **homeowner's policy** protects the policyholder from risk of loss in the home. It covers the building and its contents. This includes personal property, such as furniture, appliances, clothing, and home decorations.

Types of Coverage

Policies can be purchased that provide fire insurance only. Most homeowners choose more than just protection from fire. Homeowner's insurance typically includes three types of coverage. This coverage is for fire and other hazards, criminal activity, and personal liability.

Read the homeowner's policy carefully to see the types of items and risks that are covered. Expensive items such as jewelry, furs, antiques, computers, and rare coins may not be covered or may have limited coverage. Earthquake, hurricane, and flood protection often is not included. A special provision, called a rider, can be purchased to provide more coverage for expensive items or special risks.

FIRE AND OTHER HAZARDS

Fire, water, wind, and smoke can damage a house and its contents. The risk of this type of loss is unpredictable, and the consequences can be very serious. For example, if your house burned and you had no insurance, you would still owe a mortgage payment, but you would have no house to live in. For this reason, you may be required to have insurance as part of a mortgage agreement.

Protection extends not just to your home but to a garage or shed, trees, plants, shrubs, and fences. The policy might also cover costs of lodging while your house is being repaired.

CRIMINAL ACTIVITY

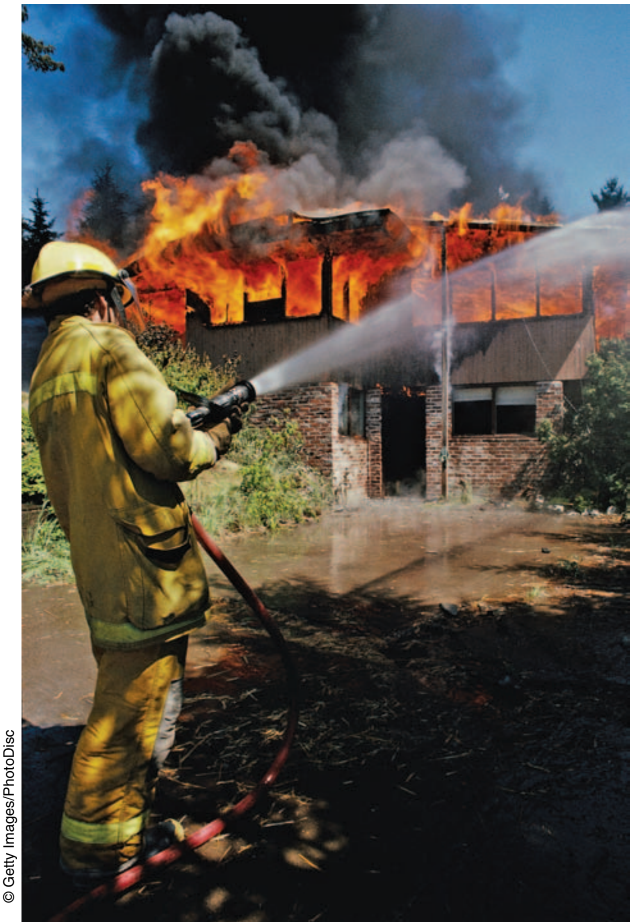
Your house could be broken into, vandalized, or suffer damage as a result of other criminal acts. You may not be able to prevent these things from happening. However, you can reduce the risk by locking windows and doors. You might also get a security alarm system and put your lights on a timer. This type of risk is unpredictable, and the consequences can be expensive.

PERSONAL LIABILITY

If someone is injured on your property, you are responsible for her or his injuries. For example, a guest may break his leg while getting into your hot tub. Your homeowner's policy would pay medical and other costs.

ACTS OF NATURE

Some areas of the country can have hurricanes, floods, volcanoes, and earthquakes. These acts of nature can do a great deal of damage. Sometimes a private insurance company will provide coverage for these risks (at high premiums). You may also be able to buy insurance from the federal government to cover these risks. If you live in an area where you could suffer this type of loss, you should consider buying this type of coverage.



Homeowner's insurance protects you from losses as a result of fire.

Home Inventory

Before buying a homeowner's policy, read it carefully to see how you will be paid for damages. You may be paid for the replacement cost of an item or for the actual cash value of the item. The payment depends on the language in the insurance policy. To ensure that you will be able to replace stolen or damaged items, choose a policy that covers replacement costs.

When items are stolen from your home or destroyed or damaged, you must file a claim with the insurance company in order to be paid for the items. Could you name all the items in your home if it was destroyed by fire? Do you know the value of all the items? Many people would not be able to give an accurate record of home items from memory.

To be prepared in case you need to file a claim, you should create a home inventory. The inventory should list all the items of value in your home. Ideally, the inventory should include the number of items, when they were purchased, and the original cost. Record as much of this information as you can. Attach any receipts that you have for expensive items. Record serial numbers for items such as appliances and computers. The inventory should include a place to list the replacement cost of the item. That amount can be added just before a claim is filed so the price is current. Figure 6-3.1 on page 178 shows part of a home inventory. You may want to list items in alphabetical order; by room location; or by type, such as appliances, furniture, and so on. You may also want to take pictures of or videotape each room in your home to document the items it contains.

Once the inventory is complete, store it in a safe place, such as a fireproof box or a safe deposit box. You could also keep a copy at a

FIGURE 6-3.1

This home inventory was created using spreadsheet software.

	A	B	C	D	E
1	HOME INVENTORY				
2	Updated June 1, 20--				
3					
4	**Item**	**Number**	**Date**	**Original**	**Replacement**
5	**Description**	**of Items**	**Purchased**	**Cost**	**Value**
6	Air cleaner	2	2/12/2006	$110.78	
7	Ionic Pro Model CA-500B				
8	China, place setting including dinner	8	5/25/2000	$114.85	
9	plate, salad plate, cup, saucer,				
10	and bread plate. Pattern: Royal				
11	Albert Old Country Roses				
12	Computer monitor, 17-inch flat panel	1	3/18/2003	$635.25	
13	ViewSonic Model VA7000				
14	Sofa, Brown leather, 83 inches long	1	4/5/2006	$2,150.48	
15	Brand: Ethan Allen #28945				
16	Television, color, flat panel, 23 inches	1	4/23/2005	$989.56	
17	Sony Model KLV S23A10				
18	Serial # 700 4690				
19					

relative's home. Update the inventory regularly. Keeping the inventory in a spreadsheet or database program makes it easy to update. Special programs for creating home inventories are also available.

Reducing Costs

As with medical insurance, you can choose higher deductibles and save money on your property insurance. Of course, this means you are assuming more risk. Some people get discounts because they add security systems or have other features that reduce the risk to the insurance company.

Technology Corner

Buying Insurance Online

Consumers can shop online for almost any product or service. Insurance is no exception. When you are looking for property or income protection, the Internet is a good place to begin.

Many insurance companies have Web sites. Consumers can fill out applications and submit them online. In many cases, rate quotes are received in a few minutes. Consumers can compare prices of policies from different companies. They can buy insurance directly online and be assigned an online agent. Some companies also allow policyholders to file claims using the Internet.

Because consumers do not deal with an agent in person, the cost of these policies may be lower. Before buying insurance online, do research to be sure that the company is reputable and that you can count on it should you need to file a claim.

RENTER'S INSURANCE

Renter's insurance protects renters from the risk of losing personal property. Loss could occur from fire, smoke, theft, freezing, water damage, or other hazards. A renter's policy covers the cost of repairing or replacing personal property. As with a homeowner's policy, check carefully to see what items and risks are covered. Check to see whether the policy pays replacement costs or actual cash value. Purchase a rider if you need coverage for very expensive items, such as jewelry or fine art. Prepare an inventory of items to use if a claim must be filed.

As a renter, you are responsible for the inside of the apartment or house. If someone is injured, renter's insurance will pay for medical costs. Renter's insurance also protects your property in your car or at work. Renter's insurance is not expensive. It is a low-cost way to protect against loss of your personal property.

AUTOMOBILE INSURANCE

When you drive a car, there are serious risks to people and property. All states have financial responsibility laws. These laws require drivers to be prepared to pay for damages caused to others. One way to do so is to have automobile insurance. **Automobile insurance** protects the owner of a car from losses as a result of accidents. The cost of car insurance depends on many things, such as the model and style of car and the age and driving record of the insured.

If your car is stolen or you are in an accident, call the police right away. Get a copy of the theft or accident police report for use in filing a claim. Call your insurance company to begin the claim process. If your car is damaged but can be driven, you may be required to get estimates for the repair work.

Types of Coverage

If you have all of the following types of coverage, you have full coverage on your automobile. Unless you have a car loan, however, you are not required to have full coverage.

LIABILITY

Liability coverage protects against loss as a result of injury to another person or damage to that person's property. It pays nothing for the insured person's own losses. Liability coverage is usually expressed with three numbers, such as 100/300/50. The 100 stands for how much will be paid for injuries to one person ($100,000). The

© Getty Images/PhotoDisc

Renters can buy insurance to protect their personal belongings.


© Getty Images/PhotoDisc

Automobile insurance protects you from serious potential loss.

300 stands for the total that will be paid for all people in an accident ($300,000). The 50 stands for how much property damage will be paid ($50,000).

COLLISION

Collision coverage protects you from damage from being hit by another car or rolling over. It will pay for damage to your car if you are at fault. Collision coverage usually has a deductible. The deductible may be from $50 to $1,000. The higher the deductible, the lower the premium.

Some states have no-fault insurance laws. Under no-fault laws, your auto insurance company will pay for your damages (up to your policy limits), regardless of who was at fault for the accident.

COMPREHENSIVE

Damage to your car from causes other than collision or rolling over is provided by comprehensive coverage. Examples of this damage include fire, theft, hail, water, falling objects, and vandalism. This insurance also has a deductible that can save you money in premiums.

PERSONAL INJURY

Personal injury protection pays for medical, hospital, and funeral costs of the insured, that person's family, and passengers. Discounts are available if you have airbags and other safety devices to reduce injuries.

UNINSURED/UNDERINSURED MOTORIST

When another person is driving while uninsured or without enough insurance (underinsured) and causes an accident, this insurance pays your costs. In other words, the other driver is at fault in an accident with you. This driver has no insurance or not enough insurance. Your policy will then pay your damages. This insurance also covers you when you are a pedestrian and get injured by an uninsured vehicle.

TOWING/RENTAL CAR

Full coverage often provides for towing charges when your car is not in running order. While your car is being fixed, your insurance may also cover the cost of a rental car. These types of coverage cost extra, but the premiums are fairly low compared to other types of coverage.

Reducing Costs

As with other types of insurance, the higher your deductibles, the lower the premiums. Other things you can do to lower car insurance costs include the following:

- Take driver training classes.
- Maintain a good driving record.
- Buy more than one insurance policy (both homeowner's and car insurance) from the same company.

- Get good grades in school.
- Have a car with a high safety rating.
- Install security devices on your car.
- Always pay your premiums on time.

You can also do other things to reduce risks. Drive while rested instead of when you are tired. Keep your car properly serviced to help prevent breakdowns. Avoid heavy traffic situations or driving in bad weather.

UMBRELLA INSURANCE

An **umbrella policy** provides coverage in addition to car and home insurance. It protects you from catastrophic losses. Policy limits are often $1,000,000 or more. Umbrella insurance pays for accidental injuries caused to other persons while you are driving or in your home. It protects you from extraordinary losses. For example, you may be in an accident in which costs for another person's injuries exceed $500,000. This amount might be more than is covered by your liability car insurance.

An umbrella policy is so named because it provides coverage above your other policies. You must have liability coverage on your home and car. When payment limits are reached on those policies, the umbrella policy takes over.

Ethics

DRIVING ACCIDENTS

Most states have financial responsibility laws. These laws may require that drivers be insured or that they be able to pay for damages caused to others. The minimum coverage required in many states is liability insurance. Liability insurance protects others from the results of negligence.

In spite of legal requirements, many people drive without insurance. Some cite the high cost of insurance as their reason. Others say that they are unable to buy reasonable coverage and they have to drive to get to work and other places they must go. There are so many uninsured motorists that drivers can buy extra coverage to protect against losses from an accident with one of them. Driving without insurance or without being able to pay for damages you cause to others is unethical.

When you injure another person in an accident, you can be sued for damages. Sometimes people demand money even though they have not been injured. They fake injuries in order to get money from the insurance company. This practice is both illegal and unethical.

There are people who stage accidents, causing your vehicle to rear-end theirs. When you hit another car from the rear, you are presumed guilty in many states. Always drive very carefully. Leave lots of room between you and the car in front of you. Defensive driving is a type of driving skill that helps you be aware of other vehicles and what might happen in traffic situations. Taking a defensive driving course can help to lessen the risk of loss from automobile accidents.

6-3 REVIEW

6-3 Activity 1 Can You Recall?

Answer these questions to help you recall what you have read. If you cannot answer a question, read the related section again.

1. What is the purpose of homeowner's insurance?
2. Explain the provisions of homeowner's policies.
3. Why do renters need renter's insurance? How is renter's insurance different from homeowner's insurance?
4. Why should renters and homeowners prepare a home inventory?
5. Why do drivers need automobile insurance? What are the basic types of automobile insurance coverage?
6. What is the purpose of an umbrella policy?

6-3 Activity 2 Auto Insurance Quotes

Prices for auto insurance vary depending on the company, the age of the driver, the type of vehicle, and other factors. Descriptions of two drivers follow. For each driver, get an annual quote for full-coverage auto insurance. To find quotes, call a local insurance agent. Identify yourself as a student, and ask for a typical price for the driver described. You might also be able to find price quotes at insurance company Web sites.

Driver A
Sheila Roberts is 18 years old. She makes good grades in school and has taken a driver training course. She has had no auto accidents or tickets. The car she will drive is a 4-year-old midsize sedan in good working order. The car is owned by her parents. Sheila wants to be added to her parents' auto policy.

Driver B
Joe Chung is 19 years old. His college grades are a C average, and he has not taken a driver training course. He has had one traffic ticket for speeding. The car Joe will drive is a 2-year-old sports car. He owns the car. Joe wants to have his own insurance policy (not to be added to his parents' policy).

EXPLORING CAREERS IN INFORMATION TECHNOLOGY

Do you like to develop creative programs or multimedia games? Is creating Web pages your hobby? Are you the person friends come to with software or hardware questions? If the answer is yes, a career in information technology might be right for you. Jobs in this area are varied. Some workers create Web pages, games, or programs. Others design networks and oversee their use. Many equipment installers and repairers are also needed in this career area.

Jobs in this career area are found in government, education, and businesses. The need for jobs in information technology is expected to grow in the next several years. The outlook varies somewhat by job.

Skills Needed

Some of the skills and traits needed for a career in information technology include the following:

- Computer/technology skills
- Communications skills
- Math skills
- Science skills
- Decision-making skills
- Problem-solving skills

Job Titles

Many jobs are available in information technology. Some job titles for this career area include the following:

- Animator
- Computer programmer
- Computer software engineer
- Computer support specialist
- Database administrator
- Graphic designer (Web designer)
- Network administrator
- Technical writer
- Telecommunications equipment installer

Explore a Job

1. Choose a job in information technology to explore further. Select a job from the list above, or choose another job in this career area.
2. Access the *Occupational Outlook Handbook* online. A link to the site is provided on the Web site for this textbook.
3. Search for more information about the job you selected to answer these questions:
   - What is the nature of the work this job involves?
   - What is the job outlook for this job?
   - What training or qualifications are needed for this job?
   - What are the median annual earnings for this job?

CHAPTER 6

Review

Summary

- Everyone takes risks that have potential consequences that may be serious. Risks may involve personal or financial loss.
- Risk assessment is the process of identifying risks, their probability, their seriousness, and how to handle them.
- Risk strategies include reducing risk, avoiding risk, transferring risk, and assuming risk.
- Income protection is provided by health insurance, disability insurance, and life insurance.
- Health insurance can be purchased as a fee-for-service, PPO, or HMO plan.
- Types of health coverage include basic health care, major medical, dental and vision, and catastrophic illness.
- There are many ways to manage health care costs, including use of deductibles, co-pays, and health savings accounts.
- Disability insurance can be short-term (usually 6 months to 2 years) or long-term (to retirement).
- There are two basic types of life insurance: term and permanent.
- Term life insurance provides a benefit at the death of the insured. Permanent life insurance provides a benefit at the death of the insured and also builds cash value.
- Property insurance is for home and automobile protection.
- Homeowner's insurance covers fire and other hazards, criminal activity, and personal liability. Renter's insurance provides similar coverage on the contents of a home but not on the structure. It also includes liability protection.
- Automobile insurance may include liability, collision, comprehensive, personal injury, and uninsured/underinsured motorist coverage.
- Having high deductibles on policies and taking actions to reduce risks can help lower costs for all types of insurance.
- An umbrella policy protects you after your homeowner's or car insurance has paid the maximum amount.

Key Terms

automobile insurance
beneficiary
co-pay
deductible
disability insurance
face value
group life insurance
health insurance
homeowner's policy
life insurance
loss
permanent life insurance
portable insurance
premium
probability
renter's insurance
risk
self-insure
stop-loss provision
term life insurance
umbrella policy

ACTIVITY 1
Review Key Terms

Use the key terms from Chapter 6 to complete the following sentences:

1. Life insurance purchased through an employer is called ____________.
2. The monthly, quarterly, semiannual, or annual payment for insurance is the ____________.
3. The ____________ is the amount you pay before insurance starts to pay.
4. A type of life insurance that provides a death benefit but no cash value is called ____________.
5. ____________ provides money to a beneficiary at the death of the insured.
6. Insurance to protect a tenant's possessions is called ____________.
7. The stated sum, or ____________, is the amount payable at the death of the insured.
8. Coverage for catastrophic expenses, in addition to car and home insurance, is provided by a(n) ____________.
9. ____________ provides income protection when you cannot work due to illness or injury.
10. Insurance you can convert to an individual policy when you leave your job is called ____________.
11. Property insurance to protect the owner of a residence is called a(n) ____________.
12. ____________ protects the owner of an automobile for damage to the car and its occupants, as well as to other cars and their occupants.
13. The person to whom the face value of an insurance policy is paid is the ____________.
14. Physical or monetary injury is called ____________.
15. The chance that a personal or economic loss might happen is known as ____________.
16. The amount a patient pays each time for using a medical service is called the ____________.
17. ____________ is a plan for sharing the risk of medical costs.
18. Life insurance that provides a death benefit and builds cash value is called ____________.
19. The likelihood of risk actually resulting in a loss is known as ____________.
20. When you ____________, you set aside money to be used in the event of injury or loss of assets.
21. A(n) ____________ is a feature of a health care plan that provides 100 percent coverage after a certain amount of money has been paid for medical expenses.

ACTIVITY 2
Math Minute

1. Takashi Chan has health insurance that pays 80 percent of covered charges after a $150 deductible. He received a statement for $350 of covered charges. How much will Takashi have to pay?
2. Merl Jones has health insurance that pays 80 percent of covered charges after a $500 deductible. There is a stop-loss provision of $5,000. The insurance company has paid $16,000 (as 80 percent of the medical expenses after the deductible). Assuming all charges were covered, how much has Merl paid for medical costs?
3. Bob Scully has homeowner's insurance that pays 90 percent of the replacement cost of items damaged in a fire. He had a fire in his kitchen, and the electric stove was damaged beyond repair. Bob paid $350 for the stove 5 years ago. The cash value of the stove before the fire was $100. A new stove will cost $400. How much will his insurance company pay?

ACTIVITY 3
Research Financial Responsibility Laws

TEAMWORK INTERNET www.thomsonedu.com/school/pfl

Financial responsibility laws vary by state. In this activity, work with a classmate to learn what the financial responsibility laws of your state require.

1. Access the Internet. In a search engine, enter your state name and the term **financial responsibility laws**.
2. Read the information you find about the laws for your state. Record the following information:
   - The name and address of the Web site(s) where you found the information
   - People to whom the financial responsibility laws apply
   - Methods that can be used to meet the requirements of the laws
   - Situations in which individuals may be required to offer proof that they are complying with the laws
   - The minimum amount of each type of insurance that must be carried if a person satisfies the laws by carrying insurance
   - Penalties for breaking the laws

ACTIVITY 4
Determine Insurance Needs

Critical Thinking

Ramon Caldez needs your help in determining how much insurance and the types of insurance to buy. Read the information about Ramon and answer the questions that follow.

Ramon is 30 years old. He is married and has one son, who is 3 years old. Ramon's wife cares for their son and does not contribute to the family income. Ramon earns $40,000 a year in gross pay. He and his wife own their home, which is valued at $100,000. Ramon thinks the contents of their home would be valued at about $50,000. They have two cars. One car is 2 years old. The other car is 10 years old, but it is still in good condition.

1. What type of health insurance coverage would you advise Ramon to have for himself and his family?
2. Ramon has short-term disability insurance provided by his employer. Ramon wants to add long-term disability coverage. What amount of monthly benefit would you advise Ramon to have in the long-term disability policy?
3. Ramon's employer provides life insurance for Ramon equal to 1 year's gross salary. Ramon knows that he needs to buy additional life insurance to protect his family. Would you advise that he buy term life insurance or whole life insurance? Why? What do you think is the minimum amount of life insurance Ramon should purchase?
4. What step does Ramon need to complete before deciding how much homeowner's insurance he needs? Ramon's home is in an area with a high danger of flooding. Is flood protection likely to be covered in his homeowner's policy? How can he get flood protection?
5. Ramon has a car loan for his car that is 2 years old. He is required to carry full-coverage insurance on this car. Ramon owns the car that is 10 years old. What type of auto insurance would you recommend Ramon carry on this car?

ACTIVITY 5
Home Inventory

Once you own property, you should take steps to protect it from loss, theft, and damage. Review the example home inventory shown in Figure 6-3.1 on page 178.

1. Create an inventory similar to Figure 6-3.1 for the items in one room of your home. You can choose the room where most of your personal items are kept or another room, such as the living room or kitchen. Use spreadsheet or database software to create the inventory, if it is available.
2. If possible, take pictures of or videotape items in the room to supplement the inventory.
3. If your family does not have a complete home inventory, encourage your parents or other adults with whom you live to create one.

Business Math Event

The FBLA Business Math Event and BPA Math Open Event allow students to demonstrate their ability to solve business math problems. Each contest consists of a test with various types of business math problems.

Evaluation

Students who take part in these events are judged on their ability to correctly solve the business math problems on the test. Read the following sample scenario and answer the related questions to practice solving business math problems.

Sample Scenario

Universe is a clothing store located in a college city. Most of the store's customers are college and high school students. Clothing sales for the store were $2.8 million last year. This year, sales have declined by 8 percent. One-eighth of annual sales are from blue jeans. The markup on merchandise purchased for sale is 250 percent. Universe marks down merchandise to 25 percent off the regular selling price after it has been in the store for 4 weeks. Merchandise is marked down to 50 percent off the regular selling price after 7 weeks and 75 percent off the regular selling price after 10 weeks. Salesclerks earn a commission of 12 percent of the selling price of items they sell.

Think Critically

1. What is the regular selling price of a shirt that the store buys for $20?
2. How much profit in dollars will the store make on a shirt it purchased for $20 when the shirt is marked down 50 percent on sale?
3. How much merchandise must an employee sell to earn $30,000 in commissions in 1 year?
4. What is the dollar amount of sales this year? What is the dollar amount of blue jeans sales?

www.fbla.org www.bpa.org