



personal finance

Eleventh Edition

Kapoor
Dlabay
Hughes



PERSONAL FINANCE

ELEVENTH EDITION

The McGraw-Hill/Irwin Series in Finance, Insurance, and Real Estate

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Consulting Editor

FINANCIAL MANAGEMENT

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Fifteenth Edition

Brealey, Myers, and Allen

Principles of Corporate Finance

Eleventh Edition

Brealey, Myers, and Allen

Principles of Corporate Finance, Concise

Second Edition

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Ninth Edition

Bodie, Kane, and Marcus

Investments

Tenth Edition

Hirt and Block

Fundamentals of Investment Management

Tenth Edition

Jordan and Miller

Fundamentals of Investments: Valuation and Management

Seventh Edition

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Running Money: Professional Portfolio Management

First Edition

Sundaram and Das

Derivatives: Principles and Practice

First Edition

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Rose and Hudgins

Bank Management and Financial Services

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Personal Financial Planning

First Edition

Harrington and Niehaus

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Fourth Edition

Kapoor, Dlabay, and Hughes

Personal Finance

Eleventh Edition

Walker and Walker

Personal Finance: Building Your Future

First Edition

PERSONAL FINANCE

ELEVENTH EDITION

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PERSONAL FINANCE, ELEVENTH EDITION

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To the memory of my parents, Ram and Susheela Kapoor; and to my wife, Theresa; and my children, Karen, Kathryn, and Dave

To the memory of my parents, Mary and Les Dlabay; and to my wife, Linda; and my children, Carissa and Kyle

To my mother, Barbara Y. Hughes; and my wife, Peggy

To my husband, David Hart; and my children, Alex and Madelyn

About the Authors

Jack R. Kapoor, EdD

College of DuPage

Jack Kapoor is a professor of business and economics in the Business and Technology Division of the College of DuPage, Glen Ellyn, Illinois, where he has taught business and economics since 1969. He received his BA and MS from San Francisco State College and his EdD from Northern Illinois University. He previously taught at Illinois Institute of Technology's Stuart School of Management, San Francisco State University's School of World Business, and other colleges. Professor Kapoor was awarded the Business and Technology Division's Outstanding Professor Award for 1999–2000. He served as an assistant national bank examiner for the U.S. Treasury Department and has been an international trade consultant to Bolting Manufacturing Co., Ltd., Mumbai, India.

Dr. Kapoor is known internationally as a coauthor of several textbooks, including *Business: A Practical Approach* (Rand McNally), *Business* (Houghton Mifflin), *Business and Personal Finance* (Glencoe), and *Focus on Personal Finance* (McGraw-Hill). He served as a content consultant for the popular national television series *The Business File: An Introduction to Business* and developed two full-length audio courses in business and personal finance. He has been quoted in many national newspapers and magazines, including *USA Today*, *U.S. News & World Report*, the *Chicago Sun-Times*, *Crain's Small Business*, the *Chicago Tribune*, and other publications.

Dr. Kapoor has traveled around the world and has studied business practices in capitalist, socialist, and communist countries.

Les R. Dlabay, EdD

Lake Forest College

Teaching about the “Forgotten Majority” (the more than 3 billion people living on \$2 or less a day) is a priority of Les Dlabay, professor of business at Lake Forest College, Lake Forest, Illinois. He believes our society can improve global business development through volunteer time, knowledge sharing, and financial donations. In addition to writing several textbooks, Dr. Dlabay teaches accounting

and various international business courses. His hobbies include a collection of cereal packages from over 100 countries and paper currency from 200 countries, which are used to teach about economic, cultural, and political aspects of international business environments.

His research involves informal and alternative financial services, microfinance, and value chain facilitation in base-of-the-pyramid (BoP) market settings. Dlabay has presented more than 300 workshops and seminars for teachers and community organizations. He serves on the boards of Bright Hope International (www.brighthope.org), which emphasizes microenterprise development through microfinance programs, and Andean Aid (www.andeanaid.org), which provides tutoring assistance to school-age children in Colombia and Venezuela. Professor Dlabay has a BS (Accounting) from the University of Illinois, Chicago; an MBA from DePaul University; and an EdD in Business and Economic Education from Northern Illinois University. He has twice received the Great Teacher award at Lake Forest College.

Robert J. Hughes, EdD

Dallas County Community Colleges

Financial literacy! Only two words, but Bob Hughes, professor of business at Dallas County Community Colleges, believes that these two words can literally change people's lives. Whether you want to be rich or just manage the money you have, the ability to analyze financial decisions and gather financial information are skills that can always be improved. In addition to writing several textbooks, Dr. Hughes has taught personal finance, introduction to business, business math, small business management, small business finance, and accounting since 1972. He also served as a content consultant for two popular national television series, *It's Strictly Business* and *Dollars & Sense: Personal Finance for the 21st Century*, and is the lead author for a business math project utilizing computer-assisted instruction funded by the ALEKS Corporation. He received his BBA from Southern Nazarene University and his MBA and EdD from the University of North Texas. His hobbies include writing, investing, collecting French antiques, art, and travel.

Melissa M. Hart, CPA

North Carolina State University

Melissa Hart is a permanent lecturer in the Poole College of Management at North Carolina State University. She was inducted into the Academy of Outstanding Teachers in 2012. She teaches courses in personal finance and corporate finance and has developed multiple ways to use technology to introduce real-life situations into the classroom and the distance education environment. Spreading the word about financial literacy has always been a

passion of hers. It doesn't stop at the classroom. Each year she shares her common sense approach of "No plan is a plan" with various student groups, clubs, high schools, and outside organizations. She is a member of the North Carolina Association of Certified Public Accountants (NCACPA) where she serves on the Accounting Education Committee. She received her BBA from the University of Maryland and an MBA from North Carolina State University. Prior to obtaining an MBA, she worked eight years in public accounting in auditing, tax compliance, and consulting. Her hobbies include keeping up with her family's many extracurricular activities as well as working on various crafts. She travels extensively with her family to enjoy the many cultures and beauty of the state, the country, and the world.

Preface



Personal Finance

KAPOOR
DLABAY
HUGHES
HART



11th Edition

Dear Personal Finance Professors and Personal Finance Students,

Just for a moment consider how the following questions affect you and your students.

Which direction is our economy headed?

Will the housing market regain its strength?

What type of investments should you choose for a long-term investment program?

How do you manage your money during an economic crisis or an economic recovery?

For most people, the answers to the above questions affect not only their financial security, but also their quality of life. In fact, for many individuals the financial crisis of 2007–2009 was a wake-up call that forced them to examine how they managed their personal finances. Until recently, for example, Americans had both the highest rate of homeownership and the highest concentration of wealth in housing ever recorded. And yet, easy access to credit and rapidly rising home values forced our personal savings rate to plunge to the lowest level since the 1930s. To make matters worse, many Americans lost their jobs and were forced to use their savings to pay everyday expenses. As the economy has begun to improve, many people now must rebuild their financial security.

As authors and teachers, we believe it is important to help people develop a plan to achieve financial security. While the 11th edition of *Personal Finance* does not guarantee that each student will be able to get the ideal job or become a millionaire, it does provide the information needed to take advantage of opportunities and to help manage personal finances. As in previous editions, we address the changing financial needs and challenges that students face on a daily basis. The 11th edition of *Personal Finance* provides a wealth of information about career planning; money management; taxes; consumer credit, including college loans; housing; legal protection; insurance; investments; retirement planning; and estate planning. By teaching students how to make informed choices, we believe you can encourage them to build a foundation of financial security.

For 11 editions, we have been keenly aware that our customers are students and professors. With each revision, we have asked professors for suggestions that will help them teach better and help students learn more efficiently. And with each edition, we have incorporated these suggestions and ideas to create what has become a best-selling personal finance textbook. We are also proud to say that we have included extensive student feedback in our text and instructional package. We do sincerely **thank you** for your suggestions, ideas, and support.

A text and instructional package should always be evaluated by the people who use it. We encourage you to e-mail us if you have comments, suggestions, or would like more information about the new edition. Finally, we invite you to examine the visual guide that follows to see how the new edition of *Personal Finance* and instructional package can help your students obtain financial security and success.

Welcome to the new 11th edition of *Personal Finance*.

Sincerely,

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PERSONAL FINANCE OFFERS YOU EVERYTHING YOU HAVE ALWAYS EXPECTED . . . AND MORE!

The primary purpose of this book is to help you apply the personal finance practices you learn from the book and from your instructor to your own life. The following *new* features of the tenth edition expand on this principle. You can use them to assess your current personal financial literacy, identify your personal finance goals, and develop and apply a personal finance strategy to help you achieve those goals. (*For a complete list of all of the features in Personal Finance, 11th ed., refer to the Guided Tour on pages xxi–xxvi.*)

NEW EDUCATION FINANCING APPENDIX

One of the biggest financial decisions that you will make in your life is whether or not to go to college, and how to finance that expense if you do choose to go. The new Appendix A covers applying for student loans and scholarships, key terms and forms, and the different types of financial aid available. Key resource websites are also highlighted.

NEW DASHBOARD FEATURE

Are you on track to meet your financial goals? It can be tough to tell sometimes. The new Finance Dashboard feature is designed to help students recognize where they're at on the continuum of financial health and to help students that aren't up to speed understand where to start and what they need to do to get to a stable and prosperous future.

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
Chapter 1	<i>New visual:</i> The financial system	Provides students with an overview of the financial intermediaries and markets that facilitate personal financial decisions.
	<i>Revised visual:</i> Financial goals and activities for various life situations	Provides expanded and reorganized coverage of foundation and life situation specific financial goals and activities.
	<i>New feature:</i> How to . . . Select a path to financial security	Contrasts easy and appropriate financial actions to guide students to long-term financial security and reduce emotional stress.
	<i>Revised content:</i> Time value of money	Explains future value and present value calculations using several methods: formula, time value of money tables, financial calculator, and spreadsheet software.
	<i>New Dashboard feature</i>	Provides an overview of emergency savings funds.
	<i>New case:</i> You Be the Financial Planner	Allows students an opportunity to assess various financial situations and recommend courses of action.
Chapter 2	<i>New content:</i> The “skills gap”	Informs students of the difference between skills needed by employers and the skills possessed by applicants.
	<i>Updated content:</i> Career trends	Provides an update on the careers expected to have the most demand in the future.
	<i>Revised content:</i> Entrepreneurial career options	Encourages students to become small business owners such as <i>social entrepreneurs</i> to mix traditional business practices with innovation to address concerns such as hunger, disease, poverty, and education.
	<i>New feature:</i> How to . . . Update Your Career Activities	Emphasizes both the career planning actions from the past that are still valid along with other actions to compete in a changing employment market.
	<i>New content:</i> Business cards in an age of social media	Offers insights about the importance of business cards in an age of various online networking tools.
	<i>New content:</i> Connecting experience and organizational needs	Assists students in better communicating their background in relation to the job description in their cover letter, résumé, or interview.
	<i>Revised content:</i> Developing a résumé	Provides enhanced and reorganized coverage of résumé content, types, preparation, and submission.
	<i>New visual:</i> Résumé makeover	Communicates actions that may be taken to update and restructure a résumé.
	<i>New content:</i> Your career brand	Provides suggestions for creating and communicating a professional image.
	<i>Revised visual:</i> Cover letter	Includes a bulleted link to highlight and communicate key experiences and competencies.
	<i>New content:</i> Preparing for a Skype interview	Suggests actions to take when preparing for and participating in an online interview.
	<i>New content:</i> How to . . . prepare for a case interview	Offers an overview of actions to take when required to use your analytical and decision-making abilities in a job interview.
	<i>New Dashboard feature</i>	Provides a template for developing career contacts.

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
Chapter 3	<p><i>New content:</i> Storing financial documents “in the cloud”</p> <p><i>Revised visual:</i> Where to keep your financial records</p> <p><i>New feature:</i> How to . . . Conduct a Money Management SWOT Analysis</p> <p><i>New examples:</i> Calculating net worth and a budget variance</p> <p><i>New Dashboard feature</i></p> <p><i>New case:</i> “Adjusting the Budget”</p>	<p>Provides guidelines for electronically storing and maintaining a system for personal financial documents.</p> <p>Suggests a format for a computerized system for personal financial documents.</p> <p>Allows students to identify and assess their money management strengths, weaknesses, opportunities, and threats.</p> <p>Presents specific numeric examples for determining net worth and a budget variance.</p> <p>Outlines how to keep a basic cash budget.</p> <p>Provides students an opportunity to make recommendations to revise a household budget.</p>
Chapter 4	<p><i>Updated content:</i> Recent tax law changes</p> <p><i>Expanded content:</i> Tax rates</p> <p><i>Expanded content:</i> Alternative minimum tax (AMT)</p> <p><i>Expanded content:</i> Filing status considerations</p> <p><i>Revised feature:</i> Filing taxes online</p> <p><i>Revised feature:</i> Tax scams</p> <p><i>Revised box feature:</i> Financial Planning Calculations</p> <p><i>New content:</i> 529 education savings plans</p> <p><i>New Dashboard feature</i></p> <p><i>Revised Financial Planning Case</i></p>	<p>Updates students on the key changes for planning a tax strategy and for filing their income tax return.</p> <p>Demonstrates how to calculate total tax due using a tax bracket schedule.</p> <p>Updates students on key changes for AMT exemption limits.</p> <p>Describes a situation where a <i>marriage penalty or bonus</i> could occur and how this amount would be calculated.</p> <p>Updates students on the most recent methods to file their taxes online.</p> <p>Provides a listing of the most recent tax scams.</p> <p>Provides revised calculations for short-term and long-term capital gains example.</p> <p>Describes how a 529 education savings plan can offer significant tax savings.</p> <p>Provides a graphic of how proper tax planning and organization can ensure that you pay your “fair share.”</p> <p>Includes revised numbers for calculating the Financial Planning case.</p>
Chapter 5	<p><i>New visual:</i> Financial institutions and banking services</p> <p><i>New visual:</i> Mobile banking</p> <p><i>New visual:</i> Expanding prepaid debit card services</p> <p><i>Expanded content:</i> The “Unbanked” and High-Cost Financial Services</p> <p><i>Updated content:</i> Types of CDs</p> <p><i>Updated content:</i> FDIC insurance</p> <p><i>New content:</i> Failing to reconcile your bank account</p> <p><i>New Dashboard feature</i></p> <p><i>New case:</i> Evaluating Banking Services</p>	<p>Presents an overview of deposit financial institutions, nondeposit institutions, nonbank financial service providers, and high-cost financial service providers.</p> <p>Details the payment, transfer, deposit, and other services available through mobile banking.</p> <p>Provides an overview of prepaid debit card “loading” methods, uses, and fees.</p> <p>Updates coverage of pawnshops, check-cashing outlets, payday loans, rent-to-own centers, and car title loans.</p> <p>Offers revised coverage of various types of certificates of deposit.</p> <p>Presents updated information on recent changes for federal deposit insurance.</p> <p>Warns of potential dangers as a result of not preparing a bank reconciliation.</p> <p>Provides an overview of healthy saving.</p> <p>Allows students to assess alternative financial services for use in various situations.</p>

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
Chapter 6	<i>New Content:</i> Changes in perception about credit.	Provides information why many people use credit to live beyond their means, and why past generations used it sparingly.
	<i>New content:</i> Advantages of credit	Describes how most major cards provide benefits, such as accidental death insurance, collision damage waiver, roadside services, gift cards, etc., at no extra cost.
	<i>New content:</i> Advantages of credit	Includes information that some credit cards extend the manufacturer’s warranty by up to one year when their credit card is used.
	<i>New content:</i> Disadvantage of credit	Points out that if you choose to make a minimum payment, it may take decades to pay off the credit card balance and hefty interest.
	<i>Updated Exhibit 6-2:</i> Volume of Consumer Credit	Shows that the volume of consumer credit has reached new highs in 2012.
	<i>Updated Exhibit 6-3:</i> Credit card holders and credit cards held	Provides updated statistics about credit card holders and credit cards held in 2012.
	<i>Updated Did You Know feature</i>	Provides updated statistics about 191 million debit card holders and how they use their cards.
	<i>New coverage:</i> Use of smart phones	Describe how some phones are now equipped to make purchases. Retailers such as Starbucks have apps that are scannable bar codes to quickly pay using a mobile phone.
	<i>Revised content:</i> What’s “phishing”?	Includes expanded information on “phishing” in the Financial Planning for Life’s Situations box.
	<i>Updated Exhibit 6-4:</i> Calculating debt-payments-to-income ratio	Gives updated information on how to calculate debt payments-to-income ratio with new figures.
	<i>New content:</i> VantageScore 3.0	Provides information on new VantageScore 3.0. Introduced in 2013, it features a score range of 300–850 and does not count debt collection accounts that have been paid off.
	<i>New Did You Know feature</i>	Informs how to obtain free credit report updates from Credit Sesame and free daily monitoring of Trans Union report from Credit Karma.
<i>Updated Did You Know feature</i>	Points out Consumer Sentinel Network identity theft complaints by victims’ age in 2012.	
<i>Updated Exhibit 6-12:</i> Consumer credit laws	Provides updated information about federal government agencies that enforce consumer credit laws.	
<i>New Dashboard feature</i>	Explains the importance of debt payments-to-income ratio in determining creditworthiness.	
Chapter 7	<i>New Content:</i> Predatory lending	Defines predatory lending and how these lenders exploit lower-income and minority borrowers.
	<i>Revised content:</i> Expensive loans	Provides revised and updated examples.
	<i>Updated Did You Know feature</i>	Gives updated information for using a credit card in a foreign country.
	<i>Revised content:</i> Cost of credit and expected inflation	Provides updated information about cost of credit and expected inflation.
	<i>Updated Exhibit 7-6:</i> Bankruptcy filings	Includes new statistics for U.S. consumer bankruptcy filings for 2010–2012.

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
Chapter 7 (Cont.)	<i>Revised content:</i> Chapter 7 bankruptcy	Provides revised Chapter 7 bankruptcy filing court fees.
	<i>New Dashboard feature</i>	Explains the importance of paying bills in a timely manner.
Chapter 8	<i>New visual:</i> Buying influences and wise spending strategies.	Presents an overview of factors that influence buying and actions that may be taken for wise shopping decisions.
	<i>New feature:</i> Net present value of buying a hybrid car	Provides a framework to assess various consumer purchases in terms of the time value of money.
	<i>New example:</i> Upside down	Presents a numeric examples for a situation in which the balance of an auto loan exceeds the value of the vehicle.
	<i>New visual:</i> Resolving consumer complaints	Offers detailed actions for obtaining assistance when facing a consumer problem situation.
	<i>New Dashboard feature</i>	Lays out a plan to minimize unplanned spending.
Chapter 9	<i>Expanded content:</i> Leases	Offers suggestions for negotiating the terms of a lease that may be considered unacceptable.
	<i>Expanded content:</i> Mortgage payment calculation	Presents a numeric example for determining a mortgage payment along with contrasting calculation methods using a formula, financial calculator, and spreadsheet software.
	<i>Expanded content:</i> Interest-only mortgages	Offers an overview and warning regarding interest-only mortgages.
	<i>Updated content:</i> Closing costs	Suggests revised amounts that might be encountered for home purchase settlement costs.
	<i>Updated coverage:</i> Short sales	Provides an overview of factors to consider when making a decision about being involved in a short sale.
	<i>New Dashboard feature</i>	Provides a plan to build mortgage equity.
Chapter 10	<i>New content:</i> “Disaster Blaster”	Describes the simulator created by the Institute for Business and Home Safety to test the wind-resistance of structural modifications for homes.
	<i>Updated exhibit:</i> Automobile insurance minimum limits	Lists the minimum limits by state for bodily injury and property damage liability coverages.
	<i>New example:</i> Deductible	Presents a specific numeric example for determining the amount paid for a claim for comprehensive and collision insurance.
	<i>New content:</i> Crash damage	Provides a comparison of the safety and damage caused by larger and smaller vehicles in a crash.
	<i>New Dashboard feature</i>	Outlines how to secure adequate personal property insurance coverage.
Chapter 11	<i>Revised Content:</i> Health care debate	Cautions that even though the U.S. Supreme Court upheld the Affordable Care Act in 2012, the debate still continues.
	<i>Revised coverage:</i> High medical costs	Provides revised and updated information on runaway health care costs.
	<i>Updated Exhibit 11-1:</i> National health expenditures	Highlights the U.S. national health expenditures from 1960 to 2018.
	<i>Updated coverage:</i> Health insurance and financial planning	Explains that although we spent over \$3.1 trillion on health care in 2013, the number of Americans without basic health insurance has been growing.
	<i>New boxed feature:</i> Financial Planning for Life’s Situations	Describes the important provisions of COBRA’s continuation coverage.
	<i>Updated coverage:</i> Types of health insurance coverage	Explains that a good health insurance plan should pay at least 80 percent for out-of-pocket expenses after a yearly deductible of \$1,000 per person or \$2,000 per family.

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
Chapter 11 (Cont.)	<i>Updated coverage:</i> Long term care insurance	Provides new statistics about the cost of long term care insurance.
	<i>Updated Did You Know feature</i>	Shows the 2012 average costs of Long-term care in nursing homes and other such facilities.
	<i>New coverage:</i> Private insurance companies	Describes that as of September 23, 2012, all health insurance companies and group health plans are required to provide a summary of health plan's benefits and coverage.
	<i>New Exhibit 11-4:</i> Summary of Benefits and Coverage	Provides a Uniform Summary of Benefits and Coverage under the new Affordable Healthcare Act.
	<i>New coverage:</i> PPOs	Explains that starting in 2014, a new type of non-profit, consumer-run health insurers will offer health insurance.
	<i>New coverage:</i> The Health Insurance Marketplaces	Describes that starting in 2014, the Health Insurance Marketplaces will make buying healthcare coverage easier and more affordable.
	<i>New Financial Planning for Life's Situation boxed feature</i>	Provides a checklist of seven steps that you can take to get ready now for the Health Insurance Marketplaces.
	<i>New content:</i> Medicare	Describes that according to the CMS, since 2010 Medicare Advantage premiums have decreased by 10 percent and enrollment has increased by 28 percent.
	<i>Expanded content:</i> Medicare	Explains that while Medicare enjoys broad support among seniors and the general public, it faces a number of policy challenges including its affordability.
	<i>New Did You Know feature</i>	Describes that Medicare enrollment has increased from 19 million in 1966 to over 50 million in 2013.
	<i>New Did You Know feature</i>	Provides information about downloading a computer file of your claims data and add your personal health information to share with your health care providers and family.
	<i>New content:</i> Medigap	Provides sources on how to get more information about Medigap policies.
	<i>New coverage:</i> Health insurance and the Patient Protection and Affordable Care Act (ACA)	Describes the major provisions of the ACA that take effect by January 2014. Is a government-run health care system that provides universal health care to all the most ethical?
<i>New coverage:</i> Pros and cons of the ACA	Explains the pros and cons of the Affordable Care Act.	
<i>New content:</i> The Food and Drug Administration	Provides information about the new websites maintained by the FDA and Medicare.	
<i>New Dashboard feature</i>	Explains the importance of disability insurance in your financial plan.	
Chapter 12	<i>Updated content:</i> Life insurance	Provides updated information on life insurance policies and their face value as of 2012.
	<i>Revised Exhibit 12-1</i>	Illustrates expectations of life and expected deaths based on sex and age in 2010.
	<i>New Exhibit 12-2:</i> Life expectancy and education	Presents a new graphic that compares life expectancy with education level attained.
	<i>New Did You Know?</i>	Provides information on the amount of hours and equivalent wage of a stay-at-home mom.

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
Chapter 12 (Cont.)	<i>Expanded content:</i> Online calculators and apps to calculate life insurance	Provides additional methods to calculate insurance needs using updated online calculators and apps.
	<i>Revised coverage:</i> Decreasing term insurance	Describes the use of decreasing term insurance as well as some common alternatives.
	<i>Revised Did You Know?</i>	Updates the average face amount of individual life insurance policies purchased.
	<i>Revised Exhibit 12-7</i>	Provides updated information for individual, group, and credit life insurance.
	<i>New Did You Know?</i>	Provides information about the most common insurance rider: waiver of premium.
	<i>New Financial Planning Calculation feature:</i>	Describes the effect of inflation on a life insurance policy using time value of money calculations.
	<i>New information:</i> Underwriting	Includes new information about the use of underwriting.
	<i>Revised Financial Planning Calculation feature:</i>	Updated calculations for determining the cost of insurance.
Chapter 13	<i>New content:</i> Payout options	Includes coverage of payout options for life insurance.
	<i>New Dashboard feature</i>	Provides a graphic of how much insurance is needed based upon various life stages.
	<i>New content:</i> Why you should pay your bills on time	Provides information about why an individual should pay recurring bills on time and what happens if bills aren't paid.
	<i>Updated coverage:</i> The need to manage credit card debt	Includes revised statistics about how many Americans use credit cards and how much they owe.
	<i>New content:</i> Basic information on economics	Defines economics and the business cycle and how the economy can affect an individual's personal finances and investment activities.
	<i>New Did You Know</i>	Points out trends for American consumer debt.
	<i>New content:</i> Priority of investment goals	Describes how many employers have eliminated or reduced their matching provisions in 401(k) or 403(b) retirement plans during the recent economic crisis.
	<i>Revised content:</i> The time value of money	Includes more streamlined coverage of how to calculate the time value of money.
	<i>New examples:</i> Real-world examples	Uses real-world companies including Apple, J.M. Smuckers, Borders Books, Shutterfly, and Biogen Idec to illustrate key topics in the chapter.
	<i>Updated statistics:</i> Value of long-term investments	Provides updated statistics about the performance of stocks and bonds for the period 1926 to 2013.
Chapter 14	<i>Updated Did You Know</i>	Gives updated information for different income levels for people in the United States.
	<i>New Dashboard feature</i>	Explains the importance of developing measurable investment goals and performing a financial checkup.
	<i>New content:</i> Why people invest in stocks	Explains the psychological reasons why people choose stocks for a long-term investment program.
Chapter 14	<i>New content:</i> How to make a decision to buy or sell stocks	Provides some specific steps to help individuals make a decision to buy or sell a stock.
	<i>Updated information:</i> Income from dividends	Explains the importance of the record date for a quarterly dividend distribution for Chevron.

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
	<i>Updated Exhibit 14-2</i> Sample stock transaction	Illustrates how investors can make money with a stock investment in The Walt Disney Corporation.
	<i>New Exhibit 14-5:</i> Stock information from the Internet	Describes the type of information provided by the Yahoo! Finance website for the Gap Corporation.
	<i>Updated Did You Know</i>	Provides new information about historical values for the Dow Jones Industrial Average for the period December 2007 through December 2012.
	<i>New Exhibit 14-7:</i> Value Line research information	Illustrates the type of detailed research information for Dollar Tree, Inc. available from the Value Line professional advisory service
	<i>New coverage:</i> Stock market bubbles	Defines a stock market bubble and describes how it can affect the value of an investment.
	<i>Updated coverage:</i> Numerical measures	Provides updated examples for all examples in the section Numerical Measures that Influence Investment Decisions.
	<i>New box feature:</i> Financial Planning Calculations	Illustrates how the time value of money can affect the value of a stock investment.
	<i>Updated boxed feature:</i> Financial Planning Calculations	Includes current statistics for the Boeing Company that are used to illustrate the price/earnings to growth (PEG) ratio calculation.
	<i>Updated Exhibit 14-8:</i> Typical commission charges	Shows current commission charges for some popular online brokerage firms.
	<i>New information:</i> Limit orders	Illustrates how a limit order can be used to specify a price to buy or sell stock in Macy's.
	<i>New Did You Know</i>	Gives an explanation of how Wall Street got its name.
	<i>Revised Exhibit 14-9:</i> Dollar-cost averaging	Includes seven years of investments instead of four years for the dollar-cost averaging example.
	<i>New example:</i> Margin transactions	Provides an example of how investors can increase their profits by using margin.
	<i>New material:</i> Selling short	Provides new material and an example on the selling short process that investors can use to increase profits.
	<i>New Dashboard feature</i>	Points out why investors need to save money before they begin investing.
	<i>New time value of money problems</i>	Adds new problems that illustrate how the time value of money can affect investment returns and cumulative dividend amounts.
	<i>New Financial Planning Case</i>	Allows students a chance to increase their ability to research a stock investment in Dollar Tree, Inc. and is based on the Value Line research information contained in Exhibit 14-7.
Chapter 15	<i>New Example:</i> Convertible bonds	Includes information about Ford Motor Company's convertible bond issue.
	<i>Updated Did You Know</i>	Provides updated information for the yields on high-quality corporate bonds.
	<i>New material:</i> The psychology of investing in bonds	Adds a new section on the psychology of investing in bonds and specific reasons why investors choose bonds.
	<i>Revised Example:</i> Interest calculation	Shows students how to calculate the interest for a \$1,000 AT&T bond that pays 5.50 percent annual interest.

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
Chapter 15 (Cont.)	<p><i>New boxed feature:</i> Financial Planning Calculations</p> <p><i>Updated Example:</i> Dollar appreciation for a bond</p> <p><i>Updated Exhibit 15-2:</i> Sample Corporate Bond Transaction</p> <p><i>Revised Content:</i> Government securities</p> <p><i>Updated Did You Know</i></p> <p><i>Revised Exhibit 15-4:</i> Tax-exempt yields</p> <p><i>Revised Exhibit 15-5:</i> Bond information</p> <p><i>Revised Exhibit 15-6:</i> Bond Ratings</p> <p><i>Revised Examples:</i> Yields</p> <p><i>Revised box feature:</i> Financial Planning Calculations</p> <p><i>New Dashboard feature</i></p> <p><i>Revised Financial Planning Case</i></p>	<p>Illustrates how reinvesting annual interest amounts can make a difference because of the time value of money.</p> <p>Shows how a bond's value can change because of changes in overall interest rates in the economy.</p> <p>Describes how bond investors can make money with an investment in a DuPont bond.</p> <p>Addresses the quality of securities issued by the U.S. government.</p> <p>Provides information about yields for 10-year treasury notes from 1990 to February 2013.</p> <p>Includes equivalent yields for all tax brackets including the recently added 39.6 percent bracket.</p> <p>Gives information from the Yahoo! Finance website about an American Express bond.</p> <p>Provides revised information about the bond ratings provided by Moody's and Standard and Poor's.</p> <p>Includes current dollar values for all the examples in the section Bond-Yield Calculations.</p> <p>Gives current financial information for AT&T that can be used to calculate the times interest earned ratio.</p> <p>Explains the reasons why people—even young investors—choose bonds for their investment program.</p> <p>Includes current prices for the possible investments provided in the case.</p>
Chapter 16	<p><i>New Example:</i> Janus Enterprise fund</p> <p><i>Updated Content:</i> Fund statistics</p> <p><i>Expanded Coverage:</i> Fund history</p> <p><i>Updated Did You Know</i></p> <p><i>New Exhibit 16-1:</i> Fund diversification</p> <p><i>New information:</i> Number of funds</p> <p><i>Updated Exhibit 16-2:</i> Fund fee table</p> <p><i>New Example:</i> A fund objective</p> <p><i>New box feature:</i> Time value of money</p> <p><i>New Did You Know</i></p> <p><i>Expanded coverage:</i> Fund managers</p> <p><i>New Did You Know</i></p>	<p>Illustrates how one person made money by investing in the Janus Enterprise fund.</p> <p>Provides new statistics about the people who invest in mutual funds.</p> <p>Adds new material about the history of mutual fund investing</p> <p>Includes current information about the age of investors who own mutual funds.</p> <p>Shows the type of stocks and securities included in the Invesco Growth and Income fund.</p> <p>Provides current numbers for exchange-traded, closed-end, and open-end funds.</p> <p>Illustrates the fee table for the Davis New York Venture fund.</p> <p>Provides the fund objective for the Vanguard Growth Equity fund.</p> <p>Ties the time value of money to fund investing.</p> <p>Illustrates the reasons why people invest in funds.</p> <p>Adds material about the role of a fund manager during both good and bad economic times.</p> <p>Provides information about the Morningstar "Star" ratings system.</p>

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
Chapter 16 (Cont.)	<p><i>Updated Exhibit 16-4:</i> Large funds</p> <p><i>Expanded coverage:</i> Professional advisory services</p> <p><i>New Exhibit 16-6:</i> Information from Money Magazine</p> <p><i>Updated Example:</i> Fidelity Stock Selector fund</p> <p><i>New Example:</i> Withdrawals</p> <p><i>New Dashboard feature</i></p> <p><i>New Financial Planning Case</i></p>	<p>Updates information about three large funds: The Vanguard Group, Fidelity Investments, and American Funds.</p> <p>Provides more information and an example of the type of research information about funds that is available on the Morningstar website.</p> <p>Shows a portion of the “Money 70 Best Mutual Funds and ETFs” article from <i>Money Magazine</i>.</p> <p>Provides current price information used to illustrate a capital gains distribution for the Fidelity Stock Selector fund.</p> <p>Adds an example of a withdrawal when an investor receives a portion of asset growth during an investment period.</p> <p>Points out that even with the professional management and diversification that funds offer, investors must still evaluate fund investments.</p> <p>Asks students to conduct research about a fund and then decide if they would invest money in the fund they chose.</p>
Chapter 17	<p><i>Updated Did You Know feature</i></p> <p><i>Updated Did You Know feature</i></p> <p><i>Revised, updated content:</i> Home as an investment</p> <p><i>New Exhibit 17-2:</i> U.S. home sales</p> <p><i>New Exhibit 17-3A:</i> House price declines</p> <p><i>New Exhibit 17-3B:</i> Increases in house prices</p> <p><i>Revised, updated content:</i> Vacation home</p> <p><i>New Financial Planning for Life’s Situations boxed feature</i></p> <p><i>New content:</i> REITs</p> <p><i>Updated Did You Know feature</i></p> <p><i>Revised and updated Financial Planning for Life’s Situations feature</i></p> <p><i>New coverage:</i> Disadvantages of real estate investments</p>	<p>Shows that home ownership in the United States soared to a historic high of 69.1 percent in 2005, but it dropped to 65.4 percent in 2012.</p> <p>Illustrates that home ownership is very low for people under 35, but it rises sharply as people enter their mid-30s.</p> <p>Explains that about \$7 trillion in household wealth was lost as average house prices decreased by nearly 33 percent from their peak in 2007.</p> <p>Shows that recent economic indicators suggest that the worse of the housing crisis is over.</p> <p>Displays the peak-to-trough home price declines for each state during the housing bust.</p> <p>Displays the increase in house prices since prices bottomed out in each state through June 2012.</p> <p>Provides updated information about the characteristics of vacation home investors.</p> <p>Cautions that investing in a foreclosure may be profitable, but make sure to protect your own property from being foreclosed.</p> <p>Explains that REITs invest in apartment buildings, hospital, hotels, industrial facilities, nursing homes, and other properties.</p> <p>Illustrates how REITs invest in all types of properties (in 2012).</p> <p>Provides new information about Uncle Sam and His Family (the government securities).</p> <p>Points out that beginning in 2013, a new 3.8 percent tax on some investment income is imposed to fund the Affordable Care Act.</p>

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
<p>Chapter 17 (Cont.)</p>	<p><i>Revised and updated coverage:</i> Precious metals</p> <p><i>Updated Exhibit 17-4:</i> Gold prices</p> <p><i>Revised and updated Did You Know feature</i></p> <p><i>New Financial Planning for Life’s Situations boxed feature</i></p> <p><i>New Dashboard feature</i></p>	<p>Provides the latest information on the recent rise and fall in the prices of gold, silver, platinum, palladium, and rhodium.</p> <p>Illustrates how the price of gold has fluctuated from 1976 to 2012.</p> <p>Shows the biggest producers of gold in the world (2011).</p> <p>Questions if gold is a solid investment, and if so, what are several ways to invest in it.</p> <p>Explains the importance of investment diversification by including a variety of assets in your portfolio.</p>
<p>Chapter 18</p>	<p><i>New content:</i> Why retirement planning?</p> <p><i>Revised content:</i> Starting early</p> <p><i>New content:</i> The power of compounding</p> <p><i>Revised content:</i> Financial Planning for Life’s Situations feature</p> <p><i>Updated Exhibit 18-4:</i> Older household expenditures</p> <p><i>Revised Did You Know feature</i></p> <p><i>Revised Did You Know feature</i></p> <p><i>Revised content:</i> The future of Social Security</p> <p><i>Updated Exhibit 18-8:</i> The future of Social Security</p> <p><i>Updated coverage:</i> Defined-contribution plan</p> <p><i>Updated coverage:</i> Regular and Roth IRAs</p> <p><i>New content:</i> Keogh plans</p> <p><i>New content:</i> Financial Planning for Life’s Situation boxed feature</p> <p><i>New Dashboard feature</i></p>	<p>Explains that as baby boomers near and enter their retirement years, they will encounter a unique set of challenges unlike those any previous generation has faced.</p> <p>Provides most current information about the importance of starting early.</p> <p>Shows the power of compounding at different annual rates of return over different time periods.</p> <p>Defines a qualified domestic relations order (QDRO) and cautions that there is no single “best” way to divide retirement benefits in a QDRO.</p> <p>Illustrates how an “average” older household spends its money (2011).</p> <p>Illustrates who receives Social Security benefits (2012).</p> <p>Provides updated information on monthly Social Security benefits in 2013.</p> <p>Caution that according to the 2012 Trustees Report, Social Security is not sustainable over the long term at current benefit and tax rates.</p> <p>Shows that the number of workers per beneficiary has plummeted since 1945.</p> <p>Describes new contribution limits for 2013.</p> <p>Provides new contribution limits for regular and Roth IRAs for 2013.</p> <p>Provides an expanded discussion of Keogh plans and SEP-IRAs.</p> <p>Adds a timeline for retirement in the retirement checklist.</p> <p>Explains the importance of exploring your options in retirement savings opportunities now that traditional pensions and other employer-funded investment plans have become increasingly rare.</p>

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
Chapter 19	<i>Revised content:</i> New lifestyles	Provides the latest available information about gift and estate tax exemptions.
	<i>New content:</i> Social media will	Explains the importance of preparing a social media will, if social media is part of your daily life.
	<i>New content:</i> Credit-shelter trust	Points out that a married couple will not pay any estate tax if their estate is less than \$10.5 million in 2013.
	<i>Revised content:</i> Federal and State Estate Taxes	Provides the latest available information about gift taxes (2013).
	<i>New content:</i> Estate Taxes	Points out that under the American Taxpayer Relief Act of 2012 (ATRA), the surviving spouse’s estate in excess of \$10.5 million (in 2013) faces estate tax of 40 percent.
	<i>Updated Exhibit 19-6:</i> Estate tax law changes	Shows the highest tax rates, gift exemption, and GST tax exemption amounts from 2001 to 2013.
	<i>New Dashboard feature</i>	Explains the importance of estate planning to ensure that you have a secure future for yourself and your loved ones.

ASSURANCE OF LEARNING

Many educational institutions today are focused on the notion of assurance of learning, an important element of some accreditation standards. *Personal Finance, 11th ed.*, is designed specifically to support your assurance of learning initiatives with a simple, yet powerful, solution.

Each test bank question for *Personal Finance, 11th ed.*, maps to a specific chapter learning outcome/objective listed in the text. You can use the test bank software to easily query for learning outcomes/objectives that directly relate to the learning objectives for your course. You can then use the reporting features of the software to aggregate student results in similar fashion, making the collection and presentation of assurance of learning data simple and easy.

GUIDED TOUR

Chapter Opener: The chapter opener contains new features that serve as the chapter road map at a glance!

What Will This Mean for Me?

A short summary of why this chapter is important. Also, what students can expect to learn from it and apply to their own personal financial plan.

Learning Objectives	What will this mean for me?
LO1-1 Analyze the process for making personal financial decisions.	Every person has some money. However, the amounts and individual needs and choices are diverse. You now have the opportunity to learn about varied financial paths for avoiding common money mistakes. Your knowledge and actions will move you toward financial security. Despite economic uncertainty, you will be able to use wise financial strategies in every stage of your life to achieve your personal goals.
LO1-2 Assess personal and economic factors that influence personal financial planning.	
LO1-3 Develop personal financial goals.	
LO1-4 Calculate time value of money situations associated with personal financial decisions.	
LO1-5 Identify strategies for achieving personal financial goals for different life situations.	

Learning Objectives

A summary of learning objectives is presented at the start of each chapter. These objectives are highlighted at the start of each major section in the chapter and appear again in the end-of-chapter summary. The learning objectives are also used to organize the end-of-chapter problems and activities, as well as materials in the *Instructor's Manual* and *Test Bank*. Problems in *CONNECT* can also be organized using the objectives.

my life

HOW DO I START?
One day, you may receive news that your aunt has given you a gift of \$10,000. Or you might find yourself with an extensive amount of credit card debt. Or maybe you desire to contribute money to a homeless shelter or a hunger-relief organization.

Each of these situations involves financial decision-making that requires, first, planning and then taking action. The process you use should be carefully considered so no (or only a few) surprises occur.

The main focus when making decisions is to avoid financial difficulties and legal troubles. How will you best plan for using your finances? For each of the following statements, select "yes," "no," or "uncertain" to indicate your personal response regarding these financial planning activities.

1. When making major financial decisions, I research them using a variety of information sources.	Yes	No	Uncertain
2. My family and household situation is likely to stay fairly stable over the next year or two.	Yes	No	Uncertain
3. My specific financial goals for the next year are in writing.	Yes	No	Uncertain
4. Time value of money calculations often guide my saving and spending decisions.	Yes	No	Uncertain
5. I am able to name specific types of risks that can affect my personal financial decisions.	Yes	No	Uncertain

As you study this chapter, you will encounter "My Life" boxes with additional information and resources related to these items.

My Life

The My Life concept begins with the chapter opener. It presents students with an engaging scenario that relates what they're about to learn to their own lives. The follow-up questions are designed to get students thinking about how involved they currently are in their personal finances and to motivate them to try new beneficial practices in their own personal finance life. The My Life Boxes throughout the chapters and the Learning Objectives in the chapter summary expand on this concept.

Boxed features are used in each chapter to build student interest and highlight important topics. Three different types of boxed features are used.

How To . . .

The How To . . . boxes fit in with the application-driven themes of *Personal Finance*. Each box highlights a personal finance issue and walks students through how to navigate the situation.

HOW TO...

File Your Taxes Online

In 2012, over 120 million taxpayers filed returns electronically. The IRS has made online filing easier and in many cases free. There are three main options for filing electronically.

OPTION 1-FREE FILE

In 2012, if your income is \$57,000 or less, you are eligible to use Free File which includes free tax preparation and free e-filing through a list of predetermined companies.

- Go to the "Free File" page at www.irs.gov and select "Pick a Free File Company." This will take you to a list of companies including descriptions and any limitations of their services. After you determine your eligibility for a particular company, select the link for the company's website.
- The online sites and tax software will guide you through the steps of the process. You will be prompted to enter your personal data, income amounts, deductions, and tax information.
- After you have ensured that all relevant information has been entered, you are ready to submit your federal tax form online. You will usually receive an e-mail confirmation of your submission, and your refund will be processed within two weeks.
- Be aware: Free e-file services may not include preparation of your state tax return.

OPTION 2-E-FILE

- The IRS offers a "Free File Fillable Forms" option. This option is available primarily for taxpayers whose income exceeds the income limitations for Free File. This may also be used by a taxpayer who attempted the Free File process and encountered additional fees or issues based on additional forms needed to complete their return. Quick, online access is available for the most commonly filed federal tax forms and schedules.
- It is strongly recommended that you print out relevant forms and perform necessary calculations prior to using this option. This will help to ensure accuracy and reduce the need to amend your return in the future.

OPTION 3-PAID PREPARER E-FILE (OR PURCHASED SOFTWARE)

- Most tax preparation software and paid preparers now offer e-filing as part of their service. If you purchase a tax preparation software tool, you will be able to connect directly through the software to electronically file your return. In addition, paid preparers that prepare more than 10 individual returns are now required by the IRS to electronically file returns.

Financial Planning for Life's Situations

WHAT'S "PHISHING"?

You open an e-mail and see messages like these: "We suspect an unauthorized transaction on your account. To ensure that your account is not compromised, please click the link below and confirm your identity." "During our regular verification of accounts, we could not verify your information. Please click here to update and verify your information." "Our records indicate that your account was overcharged. You must call us within 7 days to receive your refund." These senders are "phishing" for your information to commit fraud.

Regulatory agencies have published a brochure, *Internet Pirates Are Trying to Steal Your Information*, to assist you in identifying and preventing a new type of Internet fraud known as "phishing." With this type of scam, you receive fraudulent e-mail messages that appear to be from your financial institution. The messages often appear authentic and may include the institution's logo and marketing slogans.

These messages usually describe a situation that requires immediate attention and state that your accounts will be terminated unless you verify your personal information by clicking on a provided Web link. The Web link then takes you to a screen that asks for confidential information, including:

- Account numbers.
- Social Security numbers.
- Passwords.
- Place of birth.
- Other information used to identify you.

Those perpetrating the fraud then use this information to access your accounts or assume your identity.

The brochure advises consumers:

- If you're not sure the e-mail is legitimate, go to the company's site by typing in a Web address that you know is authentic.
- If you think the e-mail message might be fraudulent, do not click on any embedded link within the e-mail. The link may contain a virus.
- Do not be intimidated by e-mails that warn of dire consequences for not following the sender's instructions.
- If you do you fall victim to a phishing scam, act immediately to protect yourself by alerting your financial institution, placing fraud alerts on your credit files, and monitoring your account statements closely.
- Report suspicious e-mails or calls from third parties to the Federal Trade Commission, either through the Internet at www.consumer.gov/idtheft or by calling 1-877-IDTHEFT.

The brochure is on the Office of the Comptroller of the Currency's website, www.occ.gov/consumer/phishing.htm.

Source: Federal Trade Commission, www.consumer.ftc.gov/articles/0003-phishing, March 6, 2013.

Financial Planning for Life's Situations

This box offers information that can assist students when faced with special situations and unique financial planning decisions. Many emphasize the use of Internet sources.

Financial Planning Calculations

This feature presents more than 90 mathematical applications relevant to personal financial situations.

Financial Planning Calculations

ANNUAL PERCENTAGE YIELD

The Truth in Savings law requires that financial institutions report in advertisements, if a rate is quoted, and to savings plan customers the annual percentage yield (APY). The formula for APY is

$$APY = 100 \left[\left(1 + \frac{\text{Interest/Principal}}{365} \right)^{365} - 1 \right]$$

The *principal* is the amount of funds on deposit. *Interest* is the total dollar amount earned during the term on the principal. *Days in term* is the actual number of days over which interest is earned.

When the number of days in the term is 365 (that is, where the stated maturity is 365 days) or where the account does not have a stated maturity, the APY formula is simply

$$APY = 100 (\text{Interest/Principal})$$

APY provides a consistent comparison for savings plans with different interest rates, different compounding frequencies, and different time periods. APY may be easily viewed in terms of a \$100 deposit for a 365-day year. For example, an APY of 6.5 percent would mean \$6.50 interest for a year.

Margin notes provide connections to supplementary information. While the Did You Know? feature provides interesting statistics and tips in personal financial planning. The Practice Quiz feature provides an ongoing assessment tool.

Key Terms

Key terms appear in bold type and in the margin definition boxes. The terms and their page references are also listed at the end of each chapter.

My Life Boxes

My Life boxes appear next to material that relates back to the opening My Life scenario and the Learning Objectives. These boxes offer useful tips and possible solutions to help students better manage their finances.

20 Part 1 PLANNING YOUR PERSONAL FINANCES

For example, \$500 on deposit at 6 percent for six months would earn \$15 ($\$500 \times 0.06 \times 0.12$, or 1/2 year).

The increased value of money from interest earned involves two types of time value of money calculations, future value and present value. The amount that will be available at a later date is called the **future value**. In contrast, the current value of an amount desired in the future is the **present value**. Five methods are available for calculating time value of money:

1. **Formula Calculation.** With this conventional method, math notations are used for computing future value and present value.
2. **Time Value of Money Tables.** Traditionally, before calculators and computers, future value and present value tables were used (see Exhibit 1-8) to provide for easier computations.
3. **Financial Calculator.** A variety of calculators are programmed with financial functions. Both future value and present value calculations are performed using appropriate keystrokes.
4. **Spreadsheet Software.** Excel and other spreadsheet programs have built-in formulas for financial computations, including future value and present value.
5. **Websites and Apps.** Many time-value-of-money calculators are available online and through mobile devices. These programs may be used to calculate the future value of savings as well as loan payment amounts.

future value The amount to which current savings will increase based on a certain interest rate and a certain time period; also referred to as **compounding**.

my life 4
Time value of money calculations often guide my saving and spending decisions.
To assist you with using future value and present value computations for achieving personal financial goals, several websites are available: for example, www.dirkytown.net, www.moneychimp.com/calculator, and cgi.money.com/tools.

FUTURE VALUE OF A SINGLE AMOUNT Deposited money earns interest that will increase over time. **Future value** is the amount to which current savings will grow based on a certain interest rate and a certain time period. For example, \$100 deposited in a 6 percent account for one year will grow to \$106. This amount is computed as follows:
Future value = $\$100 + (\$100 \times 0.06 \times 1 \text{ year}) + \106
The same process could be continued for a second, third, and fourth year, however the computations would be time-consuming. The previously mentioned calculation methods make the process easier.
An example of the future value of a single amount might involve an investment of \$650 earning 8 percent for 10 years. This situation would be calculated as follows:

Formula	Time Value of Money Table	Financial Calculator	Spreadsheet Software
$FV = PV(1 + i)^n$	Using Exhibit 1-8A, multiply the amount deposited by the factor for the interest rate and time period.	$FV = 650(1 + 0.08)^{10}$ $FV = \$1,403.30$	$=FV(\text{rate, periods, amount per period, single amount})$ $=FV(0.08, 10, 650)$ $=\$1,403.30$
$FV = \$1,403.30$	$650 \times 2.159 = \$1,403.35$	(Different financial calculators will require different keystrokes.)	

(Note: Expanded explanations of these time value of money calculation methods are presented in the chapter appendix on page 34.)

Future value computations are often referred to as **compounding**, since interest is earned on previously earned interest. Compounding allows the future value of

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DID YOU KNOW?
In recent years, the Federal Reserve reported that over \$900 billion was being held in low- or no-interest checking accounts. Consumers are encouraged to consider high-yield checking accounts, available online or at a credit union, or move some of these funds into long-term investments.

lose your checkbook, closing the account and opening a new one is likely to be less costly than paying several stop-payment fees.

RECONCILING YOUR CHECKING ACCOUNT Each month you will receive a **bank statement** summarizing deposits, checks paid, interest earned, and fees such as service charges and printing of checks. The balance reported on the statement will usually differ from the balance in your checkbook. Reasons for a difference include checks that have not yet cleared, deposits not received by the bank, and interest earned.

To determine the correct balance, prepare a **bank reconciliation** to account for differences between the bank statement and your checkbook balance. See the Financial Planning Calculations box on page 179 for details of the bank reconciliation process.

A failure to reconcile your bank account each month can result in not knowing

- Your exact spending habits for wise money management.
- If the correct deposit amounts have been credited to your account.
- Any unauthorized ATM withdrawals.
- If you have been overcharged for fees.
- Errors that your bank may have made in your account.

OTHER PAYMENT METHODS

While personal checks are a very common payment form, other methods are available. A **certified check** is a personal check with guaranteed payment. The amount of the check is deducted from your balance when the financial institution certifies the check. A **cashier's check** is a check of a financial institution. You may purchase one by paying the amount of the check plus a fee. You may purchase a **money order** in a similar manner from financial institutions, post offices, and stores. Certified checks, cashier's checks, and money orders allow you to make a payment that the recipient knows is valid.

Traveler's checks allow you to make payments when you are away from home. This payment form requires you to sign each check twice. First, you sign the traveler's checks when you purchase them. Then, to identify you as the authorized person, you sign them again as you cash them. Electronic traveler's checks, in the form of a prepaid travel card, are also available. The card allows travelers visiting other nations to get local currency from an ATM.

PRACTICE QUIZ 5-5

- 1 What factors are commonly considered when selecting a checking account?
- 2 Are checking accounts that earn interest preferable to regular checking accounts? Why or why not?

PPP Sheet 26 Payment account comparison
PPP Sheet 27 Checking/payment account cost analysis
PPP Sheet 28 Checking account reconciliation

Did You Know?

Each chapter contains several *Did You Know?* features with fun facts, information, and financial planning assistance.

Practice Quiz

The *Practice Quiz* at the end of each major section provides questions to help students assess their knowledge of the main ideas covered in that section. As shown here, many of these quizzes include references to related Personal Financial Planning sheets, offered both in Excel and in hard copy at the back of the book.

A variety of end-of-chapter features are offered to support the concepts presented throughout each chapter.

Finance Dashboard and My Life Stages

There are increasing numbers of nontraditional students taking personal finance. The new Dashboard feature provides students of all ages with a high-level snapshot outlining how to evaluate progress in achieving mastery of the chapter concepts in real life. The My Life Stages box at the end of each chapter provides personal finance action items for students of all ages.

Financial Planning Problems

With more added to this edition, these problems allow students to apply their quantitative analysis of personal financial decisions.

Financial Planning Activities

The *Financial Planning Activities* provide methods of researching and applying financial planning topics.

Financial Planning Case

Students are given a hypothetical personal finance dilemma and data to work through to practice concepts they have learned from the chapter. A series of questions helps students to use analytic and critical thinking skills while reinforcing chapter topics.

Personal Financial Planner in Action

This feature provides long- and short-term financial planning activities per the concepts learned within the chapter, and links each to relevant Personal Financial Planner sheets (located at the end of the book) and websites for further personal financial planning.

PERSONAL FINANCIAL PLANNER IN ACTION

Selecting and Financing Housing

Housing represents a major budget expenditure. This area of financial planning requires careful analysis of needs along with a comparison of the costs and benefits of housing alternatives.

Your Short-Term Financial Planning Activities	Resources
1. Compare your current housing situation with your housing needs and financial situation.	PPP Sheet 40 http://homebuying.about.com http://realestate.msn.com www.mymoney.gov www.hud.gov
2. Conduct an analysis to compare renting and buying of housing.	PPP Sheet 41 www.homefair.com www.newbuyer.com http://home.yahoo.com

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CONTINUING CASE

Life Insurance

<i>Life Situation</i>	<i>Financial Data</i>
Young married couple	Monthly Gross Income \$4,600
Shelby, age 28	Living Expenses \$3,500
Mark, age 29	Assets \$182,000
	Liabilities \$118,000

The Lawrences recently had a baby named Blair and are concerned about their life insurance needs. Shelby has \$5,000 of coverage while Mark has life insurance coverage equal to approximately six times his annual salary. They need help in determining the appropriate life insurance amount for their family.

Questions

- What are the four general methods for estimating the amount of life insurance that the Lawrences need?
- Explain how Shelby and Mark might use the Personal Financial Planner sheet for figuring out their life insurance needs.
 - Determining Life Insurance Needs

Continuing Case

The continuing case gives students the opportunity to apply course concepts in a life situation. This feature encourages students to evaluate the changes that affect a family and then respond to the resulting shift in needs, resources, and priorities through the questions at the end of each case.

DAILY SPENDING DIARY

"My daily work expenses could easily be reduced if I'd be more careful with lunch and coffee spending."

Directions

Continue or start using the "Daily Spending Diary" sheets, or create your own format. Record every cent of your spending in the categories provided, or set up your own categories. Knowing your spending actions and achieving financial goals can improve by using this process.

Questions

- What types of job-related expenses might be commonly included as part of your Daily Spending Diary?
- What actions might be taken to reduce costs associated with seeking a job or when changing jobs?

The Daily Spending Diary sheets are located in Appendix D at the end of the book and on the student website at www.mhhe.com/kub.

Daily Spending Diary

Do you buy a latte or a soda every day before class? Do you and your friends meet for a movie once a week? How much do you spend on gas for your car each month? Do you try to donate to your favorite local charity every year?

These everyday spending activities might go largely unnoticed, yet they have a significant effect on the overall health of an individual's finances. The Daily Spending Diary sheets (in Appendix D and online) and end-of-chapter activities offer students a place to keep track of *every cent they spend* in any category. Careful monitoring and assessing of these daily spending habits can lead to better control and understanding of students' personal finances.

Personal Finance continues to provide instructors and students with features and materials to create a learning environment that can be adapted to any educational setting.

Personal Financial Planner Sheets

The PFP sheets that correlate with sections of the text are conveniently located at the end of the text. Each worksheet asks students to work through the application and record their own personal financial plan answers. These sheets apply concepts learned to students' personal situation and serve as a road map to their personal financial future. Students can fill them out, submit them for homework, and keep them filed in a safe spot for future reference!

Key websites are provided to help students research and devise their personal financial plan, and the “What’s Next for Your Personal Financial Plan?” section at the end of each sheet challenges students to use their responses to plan the next level, as well as foreshadow upcoming concepts. NEW to this edition, the authors recommend favorite apps to help students master the relevant contents.

Look for one or more PFP icons next to many Practice Quizzes. The icons direct students to the Personal Financial Planner sheet that corresponds with the preceding section.

Personal Financial Planner

Name: _____ Date: _____


22 Tax Planning Activities

Purpose: To consider actions that can prevent tax penalties and may result in tax savings. (pp. 142–147)
Instructions: Consider which of the following actions are appropriate to your tax situation. This sheet is also available in an Excel spreadsheet at www.mhhe.com/edh.
Suggested websites: www.irs.gov www.turbotax.intuit.com/tax-tools/

	Action to be taken (if applicable)	Completed
Filing Status/Withholding		
• Change filing status or exemptions because of changes in life situation.		
• Change amount of withholding because of changes in tax situation.		
• Plan to make estimated tax payments (due the 15th of April, June, September, and January).		
Tax Records/Documents		
• Organize home files for ease of maintaining and retrieving data.		
• Send current mailing address and correct Social Security number to IRS, place of employment, and other sources of income.		
Annual Tax Activities		
• Be certain all needed data and current tax forms are available well before deadline.		
• Research tax code changes and uncertain tax areas.		
Tax Savings Actions		
• Consider tax-exempt and tax-deferred investments.		
• If you expect to have the same or lower tax rate next year, accelerate deductions into the current year.		
• If you expect to have the same or lower tax rate next year, delay the receipt of income until next year.		
• If you expect to have a higher tax rate next year, delay deductions because they will have a greater benefit.		
• If you expect to have a higher tax rate next year, accelerate the receipt of income to have it taxed at the current lower rate.		
• Start or increase use of tax-deferred retirement plans.		
• Other.		

What's Next for Your Personal Financial Plan?

- Identify saving and investing decisions that would minimize future income taxes.
- Develop a plan for actions to take related to your current and future tax situation.



SUPPLEMENTS

Few textbooks provide such innovative and practical instructional resources for both students and teachers. The comprehensive teaching–learning package for *Personal Finance* includes the extensive tools housed on the book’s website.

Online Learning Center (OLC): www.mhhe.com/kdh

The Online Learning Center (OLC) contains access to Web-based study tools and instructor resources created for this text. OLCs can be delivered in multiple ways—through the textbook website (www.mhhe.com/kdh), through PageOut (see below), or within a course management system like Blackboard, WebCT, TopClass, and eCollege. They can also be easily accessed through McGraw-Hill’s CONNECT. Ask your campus representative for more details.

For Instructors

The *Instructor Edition* of the OLC holds all supplementary material, including the Instructor’s Manual, Test Bank, computerized testing software, PowerPoint, and related Web links:

- The *Instructor’s Manual* includes a “Course Planning Guide” with instructional strategies, course projects, and supplementary resource lists. The “Chapter Teaching Materials” section of the *Instructor’s Manual* provides a chapter overview, the chapter objectives with summaries, introductory activities, and detailed lecture outlines with teaching suggestions. This section also includes concluding activities, ready-to-duplicate quizzes, supplementary lecture materials and activities, and answers to concept checks, end-of-chapter problems, and cases.
- The *Test Bank*, revised by Montgomery Hill, *Northern Virginia Community College*, consists of almost 2,000 true–false, multiple-choice, and essay questions. Each test item is tagged with a corresponding learning objective, topic, level of difficulty, page number, and Blooms category. Use these tags to easily and effectively customize your test bank.
- *Computerized Testing Software*—McGraw-Hill’s EZ Test is a flexible and easy-to-use electronic testing program. The program allows instructors to create tests from book-specific items. It accommodates a wide range of question types, and instructors may add their own questions. Multiple versions of the test can be created, and any test can be exported for use with course management systems such as WebCT, BlackBoard, or PageOut. EZ Test Online gives you a place to easily administer your EZ Test–created exams and quizzes online. The program is available for Windows and Macintosh environments.
- Chapter *PowerPoint Presentations* revised by Michelle Grant, *Bossier Parish Community College*, offers more than 300 visual presentations that may be edited and manipulated to fit a particular course format.

ONLINE SUPPORT FOR STUDENTS AND INSTRUCTORS

The student edition of the OLC contains many helpful study tools.

For Students

Self-Study Quizzes

Quizzes consist of 10–15 self-grading multiple choice questions on important chapter topics. They reveal a score instantly as well as hints to help students solve questions they answered incorrectly. Each chapter contains a chapter quiz as well as pre- and posttest quizzes so that students can thoroughly gauge their understanding of the material.

Narrated Student PowerPoint, Revised by Michelle Grant, *Bossier Parish Community College*

Every student learns differently and the *Narrated PowerPoint* was created with that in mind! The interactive chapter presentations are part of the online premium content package and can be purchased. They guide students through understanding key topics and principles by presenting real-life examples based on chapter content.

And More!

Personal Finance Telecourse

If you teach personal finance as a telecourse, this text is a perfect fit! A telecourse program is available from Coastline Community College titled *Dollars \$ & Sense: Personal Finance for the 21st Century* that is based on the Kapoor, Dlabay, and Hughes text. The program includes 26 thirty-minute videotapes, which you purchase directly from Coast by contacting Lynn Dahnke, Marketing Director, Coast Learning Systems, 11460 Warner Ave., Fountain Valley, CA 92708, (800) 547-4748 or www.CoastLearning.org. The course also has a *Telecourse Study Guide* available that connects the videos to the text.

PACKAGE OPTIONS

You may also package your text with a variety of other learning tools that are available for your students:

MCGRAW-HILL *CONNECT*[™] *FINANCE*



Less Managing. More Teaching. Greater Learning. McGraw-Hill *Connect*[™] *Finance* is an online assignment and assessment solution that connects students with the tools and resources they'll need to achieve success. *Connect*[™] helps prepare students for their future by enabling faster learning, more efficient studying, and higher retention of knowledge.

McGraw-Hill *Connect*[™] *Finance* Features *Connect*[™] *Finance* offers a number of powerful tools and features to make managing assignments easier, so faculty can spend more time teaching. With *Connect*[™] *Finance*, students can engage with their coursework anytime and anywhere, making the learning process more accessible and efficient. *Connect*[™] *Finance* offers you the features described below.

Simple assignment management With *Connect*[™] *Finance*, creating assignments is easier than ever, so you can spend more time teaching and less time managing. The assignment management function enables you to

- Create and deliver assignments easily with selectable end-of-chapter problems and test bank items.
- Streamline lesson planning, student progress reporting, and assignment grading to make classroom management more efficient than ever.
- Go paperless with the eBook and online submission and grading of student assignments.

Smart grading When it comes to studying, time is precious. *Connect*[™] *Finance* helps students learn more efficiently by providing feedback and practice material when they need it, where they need it. When it comes to teaching, your time is also precious. The grading function enables you to

- Have assignments scored automatically, giving students immediate feedback on their work and side-by-side comparisons with correct answers.
- Access and review each response; manually change grades or leave comments for students to review.
- Reinforce classroom concepts with practice tests and instant quizzes.

Instructor library The *Connect*[™] *Finance* Instructor Library is your repository for additional resources to improve student engagement in and out of class. You can select and use any asset that enhances your lecture.

Student study center The *Connect*[™] *Finance* Student Study Center is the place for students to access additional resources. The Student Study Center

- Offers students quick access to lectures, practice materials, eBooks, and more.
- Provides instant practice material and study questions, easily accessible on the go.

Student progress tracking *Connect™ Finance* keeps instructors informed about how each student, section, and class is performing, allowing for more productive use of lecture and office hours. The progress-tracking function enables you to

- View scored work immediately and track individual or group performance with assignment and grade reports.
- Access an instant view of student or class performance relative to learning objectives.

Lecture capture through Tegrity Campus For an additional charge Lecture Capture offers new ways for students to focus on the in-class discussion, knowing they can revisit important topics later. This can be delivered through Connect or separately. See below for more details.

McGraw-Hill Connect™ Plus Finance McGraw-Hill reinvents the textbook learning experience for the modern student with *Connect™ Plus Finance*. A seamless integration of an eBook and *Connect™ Finance*, *Connect™ Plus Finance* provides all of the *Connect™ Finance* features plus the following:

- An integrated eBook, allowing for anytime, anywhere access to the textbook.
- Dynamic links between the problems or questions you assign to your students and the location in the eBook where that problem or question is covered.
- A powerful search function to pinpoint and connect key concepts in a snap.

In short, *Connect™ Finance* offers you and your students powerful tools and features that optimize your time and energies, enabling you to focus on course content, teaching, and student learning. *Connect™ Finance* also offers a wealth of content resources for both instructors and students. This state-of-the-art, thoroughly tested system supports you in preparing students for the world that awaits.

For more information about Connect™, go to www.mcgrawhillconnect.com, or contact your local McGraw-Hill sales representative.

Diagnostic and adaptive learning of concepts: LearnSmart Students want to make the best use of their study time. The LearnSmart adaptive self-study technology within *Connect Finance* provides students with a seamless combination of practice, assessment, and remediation for every concept in the textbook. LearnSmart's intelligent software adapts to every student response and automatically delivers concepts that advance the student's understanding while reducing time devoted to the concepts already mastered. The result for every student is the fastest path to mastery of the chapter concepts. LearnSmart

- Applies an intelligent concept engine to identify the relationships between concepts and to serve new concepts to each student only when he or she is ready.
- Adapts automatically to each student, so students spend less time on the topics they understand and more time on those they have yet to master.
- Provides continual reinforcement and remediation but gives only as much guidance as students need.
- Integrates diagnostics as part of the learning experience.
- Enables you to assess which concepts students have efficiently learned on their own, thus freeing class time for more applications and discussion.



SMARTBOOK™

SmartBook™ uses McGraw-Hill Education's market-leading adaptive technology to provide an ultra-efficient reading and learning experience for students. Students have access to a "smart" eBook, customized to highlight the most important concepts in the chapter and those that the individual student is yet to master. As the student reads, the reading material constantly adapts to ensure the student is focused on the content he or she needs most to close knowledge gaps.

Broken into separate modules that have students read, practice the material they just learned, and review material they have covered previously to improve knowledge retention, SmartBook is a next-generation study tool that is proven to improve student learning outcomes and understanding of the material.

Tegrity Campus: Lectures 24/7



Tegrity Campus is a service that makes class time available 24/7 by automatically capturing every lecture in a searchable format for students to review when they study and complete assignments. With a simple one-click start-and-stop process, you capture all computer screens and corresponding audio. Students can replay any part of any class with easy-to-use browser-based viewing on a PC or Mac.

Educators know that the more students can see, hear, and experience class resources, the better they learn. In fact, studies prove it. With Tegrity Campus, students quickly recall key moments by using Tegrity Campus's unique search feature. This search helps students efficiently find what they need, when they need it, across an entire semester of class recordings. Help turn all your students' study time into learning moments immediately supported by your lecture.

To learn more about Tegrity watch a two-minute flash demo at <http://tegritycampus.mhhe.com>.

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Personal Financial Planner

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chapter 1

Personal Finance Basics and the Time Value of Money



Learning Objectives

What will this mean for me?

- LO1-1** Analyze the process for making personal financial decisions.
- LO1-2** Assess personal and economic factors that influence personal financial planning.
- LO1-3** Develop personal financial goals.
- LO1-4** Calculate time value of money situations associated with personal financial decisions.
- LO1-5** Identify strategies for achieving personal financial goals for different life situations.

Every person has some money. However, the amounts and individual needs and choices are diverse. You now have the opportunity to learn about varied financial paths for avoiding common money mistakes. Your knowledge and actions will move you toward financial security. Despite economic uncertainty, you will be able to use wise financial strategies in every stage of your life to achieve your personal goals.



my life

HOW DO I START?

One day, you may receive news that your aunt has given you a gift of \$10,000. Or you might find yourself with an extensive amount of credit card debt. Or maybe you desire to contribute money to a homeless shelter or a hunger-relief organization.

Each of these situations involves financial decision-making that requires, first, planning and then taking action. The process you use should be carefully considered so no (or only a few) surprises occur.

The main focus when making decisions is to avoid financial difficulties and legal troubles. How will you best plan for using your finances? For each of the following statements, select "yes," "no," or "uncertain" to indicate your personal response regarding these financial planning activities.

- | | | | |
|---|-----|----|-----------|
| 1. When making major financial decisions, I research them using a variety of information sources. | Yes | No | Uncertain |
| 2. My family and household situation is likely to stay fairly stable over the next year or two. | Yes | No | Uncertain |
| 3. My specific financial goals for the next year are in writing. | Yes | No | Uncertain |
| 4. Time value of money calculations often guide my saving and spending decisions. | Yes | No | Uncertain |
| 5. I am able to name specific types of risks that can affect my personal financial decisions. | Yes | No | Uncertain |

As you study this chapter, you will encounter "My Life" boxes with additional information and resources related to these items.

The Financial Planning Process

LO1-1

Analyze the process for making personal financial decisions.

personal financial planning The process of managing your money to achieve personal economic satisfaction.

Being “rich” means different things to different people. Some define wealth as owning many expensive possessions and having a high income. People may associate being rich with not having to worry about finances or being able to pay bills. For others, being rich means they are able to donate to organizations that matter to them.

How people get rich also varies. Starting a successful business or pursuing a high-paying career are common paths to wealth. However, frugal living and wise investing can also result in long-term financial security. In recent years, many have discovered that the quality of their lives should be measured in terms of something other than money and material items. A renewed emphasis on family, friends, and serving others has surfaced.

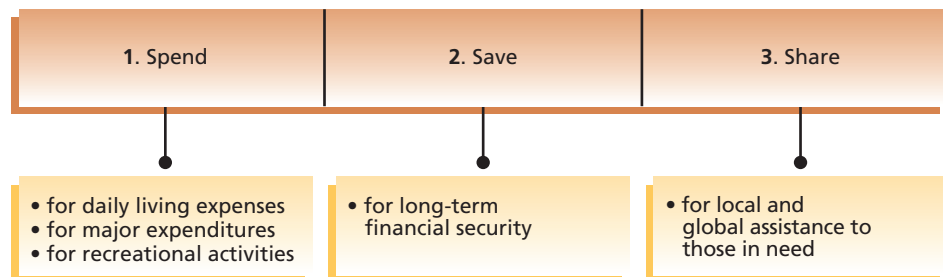
Most people want to handle their finances so that they get full satisfaction from each available dollar. To achieve this and other financial goals, people first need to identify and set priorities. Both financial and personal satisfaction are the result of an organized process that is commonly referred to as *personal money management* or *personal financial planning*.

Personal financial planning is the process of managing your money to achieve personal economic satisfaction. This planning process allows you to control your financial situation. Every person, family, or household has a unique financial position, and any financial activity therefore must also be carefully planned to meet specific needs and goals.

A comprehensive financial plan can enhance the quality of your life and increase your satisfaction by reducing uncertainty about your future needs and resources. The specific advantages of personal financial planning include

- Increased effectiveness in obtaining, using, and protecting your financial resources throughout your life.
- Increased control of your financial affairs by avoiding excessive debt, bankruptcy, and dependence on others for economic security.
- Improved personal relationships resulting from well-planned and effectively communicated financial decisions.
- A sense of freedom from financial worries obtained by looking to the future, anticipating expenses, and achieving your personal economic goals.

We all make hundreds of decisions each day. Most of these decisions are quite simple and have few consequences. Some are complex and have long-term effects on our personal and financial situations. Personal financial activities involve three main decision areas:



While everyone makes decisions, few people consider how to make better decisions. As Exhibit 1-1 shows, the financial planning process is a logical, six-step procedure that can be adapted to any life situation.

Exhibit 1-1

The financial planning process

**STEP 1: DETERMINE YOUR CURRENT FINANCIAL SITUATION**

First, determine your current financial situation regarding income, savings, living expenses, and debts. Preparing a list of current asset and debt balances and amounts spent for various items gives you a foundation for financial planning activities. The personal financial statements discussed in Chapter 3 will provide the information needed to match your goals with your current income and potential earning power.

EXAMPLE: Step 1

Within the next two months, Kent Mullins will complete his undergraduate studies with a major in global business development. He has worked part-time in various sales jobs. He has a small savings fund (\$1,700) and over \$8,500 in student loans. What additional information should Kent have available when planning his personal finances?

How about you? Depending on your current (or future) life situation, what actions might you take to determine your current financial situation?

STEP 2: DEVELOP YOUR FINANCIAL GOALS

Several times a year, you should analyze your financial values and goals. This activity involves identifying how you feel about money and why you feel that way. Are your feelings about money based on factual knowledge or on the influence of others?

Are your financial priorities based on social pressures, household needs, or desires for luxury items? How will economic conditions affect your goals and priorities? The purpose of this analysis is to differentiate your needs from your wants.

Specific financial goals are vital to financial planning. Others can suggest financial goals for you; however, *you* must decide which goals to pursue. Your financial goals can range from spending all of your current income to developing an extensive savings and investment program for your future financial security.

EXAMPLE: Step 2

Kent Mullins has several goals, including paying off his student loans, obtaining an advanced degree in global business management, and working in Latin America for a multinational company. What other goals might be appropriate for Kent?

How about you? Depending on your current (or future) life situation, describe some short-term or long-term goals that might be appropriate for you.



Financial choices require periodic evaluation.

STEP 3: IDENTIFY ALTERNATIVE COURSES OF ACTION

Developing alternatives is crucial when making decisions. Although many factors will influence the available alternatives, possible courses of action usually fall into these categories:

- *Continue the same course of action.* For example, you may determine that the amount you have saved each month is still appropriate.
- *Expand the current situation.* You may choose to save a larger amount each month.
- *Change the current situation.* You may decide to use a money market account instead of a regular savings account.
- *Take a new course of action.* You may decide to use your monthly savings budget to pay off credit card debts.

Not all of these categories will apply to every decision; however, they do represent possible courses of action. For example, if you want to stop working full time to go to school, you must generate several alternatives under the category “Take a new course of action.”

Creativity in decision making is vital for effective choices. Consideration of many alternatives will help you make more effective and satisfying decisions. For instance, most people believe they must own a car to get to work or school. However, they should consider other alternatives such as public transportation, carpooling, renting a car, shared ownership of a car, or a company car.

Remember, when you decide not to take action, you elect to “do nothing,” which can be a dangerous alternative.

DID YOU KNOW?

According to the National Endowment for Financial Education, 70 percent of major lottery winners end up with financial difficulties. These winners often squander the funds awarded them, while others overspend. Many end up declaring bankruptcy. Having more money does not mean you will make better financial choices.

EXAMPLE: Step 3

Kent Mullins has several options available for the near future. He could work full time and save for graduate school; he could go to graduate school full time by taking out an additional loan; or he could go to school part time and work part time. What additional alternatives might he consider?

How about you? Depending on your current (or future) life situation, list various alternatives for achieving the financial goals you identified in the previous step.

STEP 4: EVALUATE YOUR ALTERNATIVES

Next, you need to evaluate possible courses of action, taking into consideration your life situation, personal values, and current economic conditions. How will the ages of dependents affect your saving goals? How do you like to spend leisure time? How will changes in interest rates affect your financial situation?

CONSEQUENCES OF CHOICES Every decision closes off alternatives. For example, a decision to invest in stock may mean you cannot take a vacation. A decision to go to school full time may mean you cannot work full time. **Opportunity cost** is what you give up by making a choice. This cost, commonly referred to as the trade-off of a decision, cannot always be measured in dollars. It may refer to the money you forgo by attending school rather than working, but it may also refer to the time you spend shopping around to compare brands for a major purchase. In either case, the resources you give up (money or time) have a value that is lost.

opportunity cost What a person gives up by making a choice.

Decision making will be an ongoing part of your personal and financial situation. Thus, you will need to consider the lost opportunities that will result from your decisions. Since decisions vary based on each person's situation and values, opportunity costs will differ for each person.

EVALUATING RISK Uncertainty is a part of every decision. Selecting a college major and choosing a career field involve risk. What if you don't like working in this field or cannot obtain employment in it? Other decisions involve a very low degree of risk, such as putting money in an insured savings account or purchasing items that cost only a few dollars. Your chances of losing something of great value are low in these situations.

In many financial decisions, identifying and evaluating risk are difficult (see Exhibit 1-2). The best way to consider risk is to gather information based on your experience and the experiences of others, and to use financial planning information sources.

FINANCIAL PLANNING INFORMATION SOURCES

When you travel, you might use a GPS or a map. Traveling the path of financial planning requires a different kind of map. Relevant information is required at each stage of the decision-making process. This book provides the foundation you need to make appropriate personal financial planning decisions. Changing personal, social, and economic conditions will require that you continually supplement and update your knowledge. Exhibit 1-3 offers an overview of the informational resources available when making personal financial decisions.

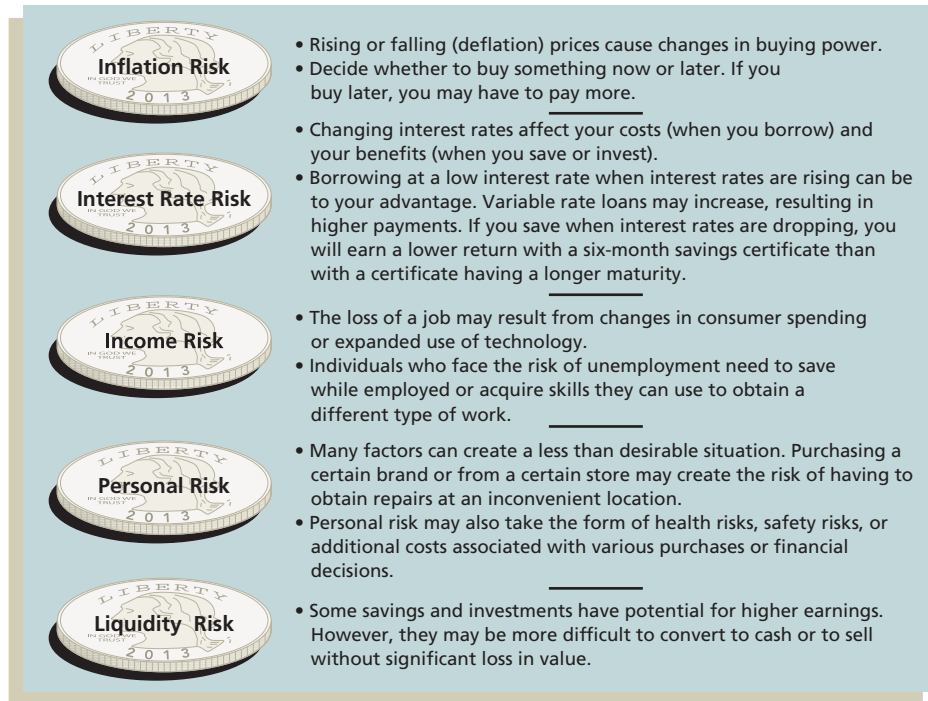
my life 1

When making major financial decisions, I research them using a variety of information sources.

Always consider information from several sources when making financial decisions. In addition to various websites, see Appendix B for other financial planning resources.

Exhibit 1-2

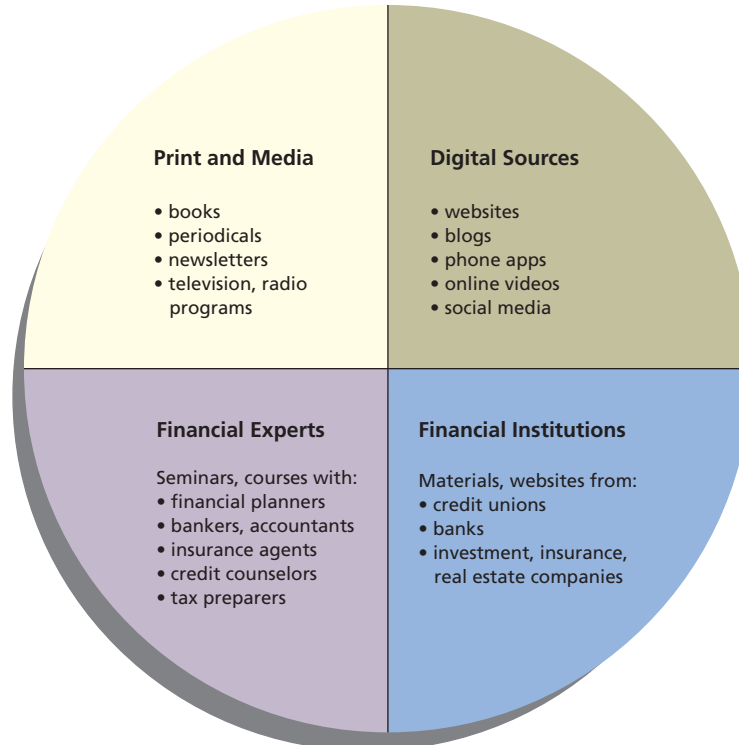
Types of risk



- **Inflation Risk**
 - Rising or falling (deflation) prices cause changes in buying power.
 - Decide whether to buy something now or later. If you buy later, you may have to pay more.
- **Interest Rate Risk**
 - Changing interest rates affect your costs (when you borrow) and your benefits (when you save or invest).
 - Borrowing at a low interest rate when interest rates are rising can be to your advantage. Variable rate loans may increase, resulting in higher payments. If you save when interest rates are dropping, you will earn a lower return with a six-month savings certificate than with a certificate having a longer maturity.
- **Income Risk**
 - The loss of a job may result from changes in consumer spending or expanded use of technology.
 - Individuals who face the risk of unemployment need to save while employed or acquire skills they can use to obtain a different type of work.
- **Personal Risk**
 - Many factors can create a less than desirable situation. Purchasing a certain brand or from a certain store may create the risk of having to obtain repairs at an inconvenient location.
 - Personal risk may also take the form of health risks, safety risks, or additional costs associated with various purchases or financial decisions.
- **Liquidity Risk**
 - Some savings and investments have potential for higher earnings. However, they may be more difficult to convert to cash or to sell without significant loss in value.

Exhibit 1-3

Financial planning information sources



EXAMPLE: Step 4

As Kent Mullins evaluates his alternative courses of action, he must consider his income needs for both the short term and the long term. He should also assess career opportunities with his current skills and his potential with advanced training. What risks and trade-offs should Kent consider?

How about you? Depending on your current (or future) life situation, what types of risks might you encounter in your various personal financial activities?

STEP 5: CREATE AND IMPLEMENT YOUR FINANCIAL ACTION PLAN

This step of the financial planning process involves developing an action plan that identifies ways to achieve your goals. For example, you can increase your savings by reducing your spending or by increasing your income through extra time on the job. If you are concerned about year-end tax payments, you may increase the amount withheld from each paycheck, file quarterly tax payments, shelter current income in a tax-deferred retirement program, or buy municipal securities. As you achieve your short-term or immediate goals, the goals next in priority will come into focus.

To implement your financial action plan, you may need assistance from others. For example, you may use the services of an insurance agent to purchase property insurance or the services of an investment broker to purchase stocks, bonds, or mutual funds.

EXAMPLE: Step 5

Kent Mullins has decided to work full time for a few years while he (1) pays off his student loans, (2) saves money for graduate school, and (3) takes a couple of courses in the evenings and on weekends. What are the benefits and drawbacks of this choice?

How about you? Depending on your current (or future) life situation, describe the benefits and drawbacks of a financial situation you have encountered during the past year.

STEP 6: REVIEW AND REVISE YOUR PLAN

Financial planning is a dynamic process that does not end when you take a particular action. You need to regularly assess your financial decisions. You should do a complete review of your finances at least once a year. Changing personal, social, and economic factors may require more frequent assessments.

When life events affect your financial needs, this financial planning process will provide a vehicle for adapting to those changes. Regularly reviewing this decision-making process will help you make priority adjustments that will bring your financial goals and activities in line with your current life situation.

DID YOU KNOW?

Most financial planning professionals have a code of ethics, but not all abide by these principles. To avoid financial difficulties and potential fraud, make sure your financial planner strictly applies industry policies regarding confidentiality, integrity, objectivity to prevent a conflict of interest, and a commitment to continuing education.