13TH EDITION

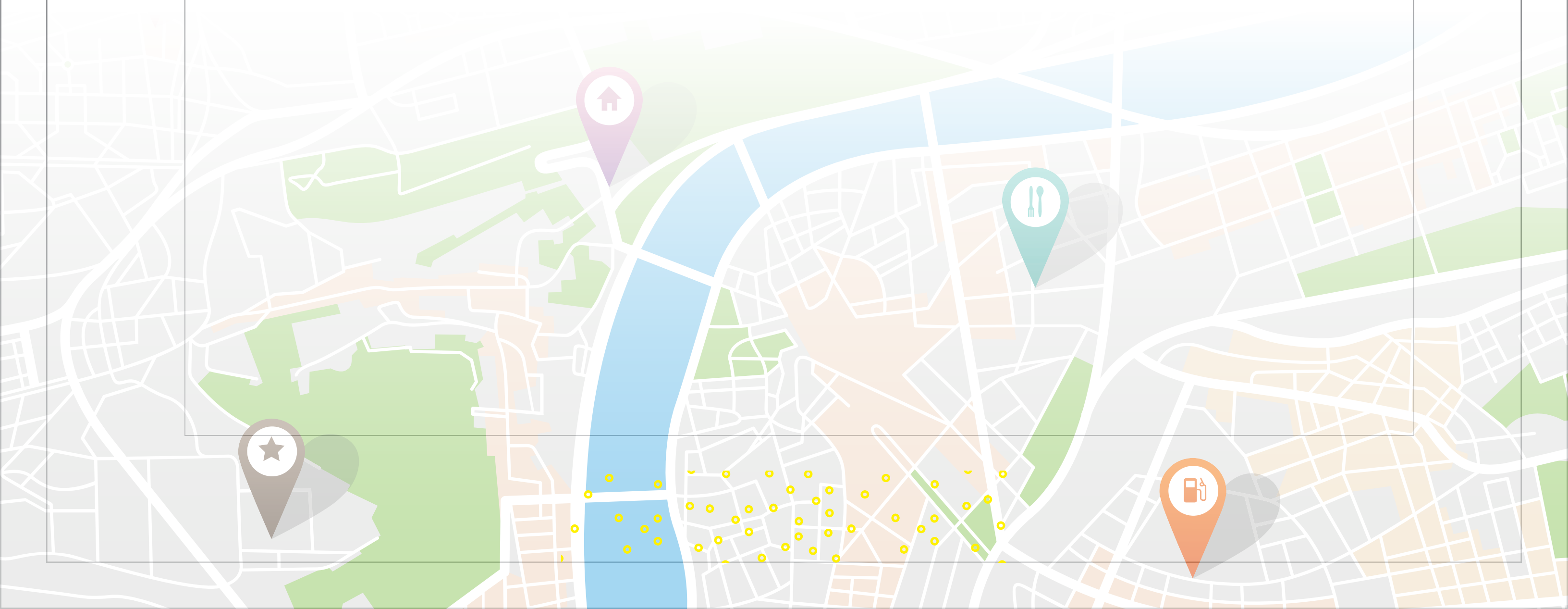
PERSONAL FINANCE

KAPOOR | DLABAY | HUGHES | HART

McGraw Hill Education

Personal Finance

THIRTEENTH EDITION



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THIRTEENTH EDITION

JACK R. KAPOOR
College of DuPage

LES R. DLABAY
Lake Forest College

ROBERT J. HUGHES
Dallas County Community Colleges

MELISSA M. HART
North Carolina State University

Mc Graw Hill Education

PERSONAL FINANCE, THIRTEENTH 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 my wife, Linda Dlabay; and my children, Carissa and Kyle, and their spouses, Doug Erickson and Anne Jaspers

To my wife, Robin; and to the memory of my mother, Barbara Y. Hughes

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

Brief Contents

About the authors

Jack R. Kapoor, EdD

College of DuPage

Jack Kapoor has been 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 University and his EdD in Business and Economic Education 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

"Learning for a life worth living" is the teaching emphasis of Les Dlabay, professor of business emeritus, who taught at Lake Forest College, Lake Forest, Illinois, for 35 years. In an effort to prepare students for diverse economic settings, he makes extensive use of field research projects related to food, water, health care, and education. He believes our society can improve global business development through volunteering, knowledge sharing, and financial donations. Dr. Dlabay has authored or has adaptations of more than 40 textbooks in the United States, Canada, India, and Singapore. He has taught more than 30 different courses during his career, and has presented over 300 workshops and seminars to academic, business, and community organizations. Professor Dlabay has a collection of cereal packages from more than 100 countries and banknotes from 200 countries, which are used to teach about economic, cultural, and political elements of international business environments.

His research involves informal and alternative financial services, cross-cultural exploration methods, and value chain facilitation in base-of-the-pyramid (BoP) market settings. Dr. Dlabay previously served on the board of Bright Hope International (www.brighthope.org), which emphasizes microenterprise development, and currently serves on the board of Andean Aid (www.andeanaid.org), which provides tutoring assistance and spiritual guidance 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 received The Great Teacher award at Lake Forest College three times.

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 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. She has been nominated for the Gertrude Cox Award for Innovative Excellence in Teaching and Learning with Technology as well as the Alumni Distinguished Undergraduate Professor Award. 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 online environment. Spreading the word about financial literacy has always been a passion of hers. Each year she shares her commonsense 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). 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 and traveling.

Preface

Dear Personal Finance Students and Professors,

Question: Why take a Personal Finance course?

Before you answer this question, imagine what your life will be like in 10, 20, or even 30 years. Decisions you make today can affect not only your life now, but have an impact on your future. If you make wise financial decisions, life can become a more joyous experience. On the other hand, if you make bad decisions, life may not turn out so well. As authors, we wrote ***Personal Finance*** with one purpose: To provide the information you need to make informed decisions that can literally change your life. Just for a moment consider the following questions:

- How will rising interest rates and inflation affect your ability to pay for college, buy an automobile, or purchase a home?
- How will the Tax Cuts and Jobs Act of 2017 affect your ability to obtain employment or start a business?
- How can you balance your current needs with saving and investing for the future?
- How can you obtain your career goals and personal goals to create the type of life you really want?
- How will the need for health insurance, employer-sponsored retirement plans, and Social Security affect your financial future?
- How will presidential policy, tariffs and trade wars, deregulation, environmental concerns, and social unrest affect the economy, consumer spending, and your financial future?

For most people, answers to these questions affect not only their quality of life, but also their financial security. While the 13th edition of ***Personal Finance*** does not guarantee that you will get the ideal job or become a millionaire, it does provide the information needed to take advantage of opportunities and to help manage your personal finances.

This new edition of ***Personal Finance*** is packed with updated information and examples that will not only help you get a better grade in this course, but also help you plan for the future and achieve financial security. For example, we have revised important topics like taxes, college loans, health care, and investments to provide the most current information available. Other important topics including credit, housing, legal protection, retirement planning, and estate planning have also been revised in this edition.

For 13 editions, we have listened carefully to both students and professors. With each revision, we have incorporated these suggestions and ideas to create what has become a best-selling personal finance textbook. For example, we've moved the appendices from the back of the book to the main text and revised both content and examples throughout the text. We've also included important content on Education Financing, Loans, and Scholarships in Chapter 7—Choosing a Source of Credit. *For all your suggestions, ideas, and support, we thank you.*

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,*** the McGraw-Hill Connect learning software, and our SmartBook technology can help you obtain financial security and success.

Welcome to the new 13th edition of ***Personal Finance***!

Sincerely,

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ACKNOWLEDGMENTS

The extensive feedback and thoughtful comments provided by instructors in the field have greatly contributed to the quality of the 13th edition of *Personal Finance.*

Many talented professionals at McGraw-Hill Higher Education have also contributed to the development of *Personal Finance,* 13th edition. We are especially grateful to Michele Janicek, Chuck Synovec, Jennifer Upton, Trina Maurer, Fran Simon, Jamie Koch, Jessica Cuevas, Abbey Jones, and Karen Jozefowicz.

In addition, Jack Kapoor expresses special appreciation to Theresa and Dave Kapoor, Kathryn Thumme, and Karen and Joshua Tucker for their typing, proofreading, and research assistance. Les Dlabay expresses his thanks to Joe Chmura, Kyle Dlabay, Linda Dlabay, Anne Jaspers, Jennifer Lazarus, Ben Rohde, and George Seyk for their help reviewing the manuscript. Finally, we thank our spouses and families for their patience, understanding, encouragement, and love throughout the years.

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 13th 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, *13th edition, refer to the Guided Tour on pages xxii–xxvii.*)

FINANCIAL LITERACY IN MY LIFE

This edition has moved with a laser-like focus toward the concept of financial literacy. In our many years of teaching and evaluating what knowledge and skills are most important to the lifelong success of our students, financial literacy—the ability to understand and interpret knowledge relating to the financial decisions we make—looms largest. We hope that students will remember all of the details we have put so much time and care into writing, and that you put into teaching. If nothing else, though, we feel we have been successful if students come out of this course with the skills required to interpret financial information and to make wise decisions about their own money, and the confidence that comes with knowing they are able to solve the problems they encounter.

Throughout the text, we spend more time talking about financial literacy. The new chapter opening vignettes ask questions about "Financial Literacy in My Life." The Financial Planning features are focused to emphasize "my life"—the life and decisions that you, the student, will make. Features on financial calculations and decision-making have been altered to focus on students achieving financial literacy.

Another new feature for this edition is the addition of updates related to the 2017 Tax Cuts and Jobs Act, which made drastic changes to much of our tax system. This is, of course, highlighted in the chapter about taxes (Chapter 4) but is touched on throughout the rest of the book, too—taxes impact budgeting, mortgages, estate planning, and many other topics. This expanded and updated coverage should help students to make sense of these new laws as they are implemented.

Additionally, you may notice that some contents covering important topics such as education funding, career development, and additional sources of information have been moved around in the book to integrate more tightly with the main contents. We know how important these topics are for students and wanted to find ways to make our discussion more accessible.

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 1	*Revised exhibit:* Financial planning information sources (*Exhibit 1-3*)	Provides an updated overview of personal financial planning information sources.
	New Smart Money Minute *feature*	Offers an overview of technology influences on banking and financial activities, such as artificial intelligence, robotics, the Internet of Things, blockchain, and wearable technology.
	New Smart Money Minute *feature*	Provides suggestions for becoming financially disciplined, and emphasizes the importance of the "why" of financial goals.
	Updated apps and websites	Presents additional online and mobile sources to consult for expanded information and assistance.
	New Smart Money Minute *feature*	Offers guidance on how to avoid mistakes when studying personal finance.
	New Smart Money Minute *feature*	Suggests sources for funding education costs along with a reference to the Chapter 7 Appendix.
	Added content: Financial Literacy for My Life	Discusses common financial planning mistakes as identified by financial advisors.
	Repositioned Daily Spending Diary *sheet*	Presents an explanation of the *Daily Spending Diary* sheet at the end of the chapter, rather than at the end of the book.
Chapter 2	*Revised exhibit:* Education and income (*Exhibit 2-1*)	Updates median weekly earnings for various levels of education, based on data from the Bureau of Labor Statistics.
	New Smart Money Minute *feature*	Suggests factors to emphasize for enhanced job search success.
	New Smart Money Minute *feature*	Reports the main sources of newly created jobs with innovative and young companies.
	Revised exhibit: Career information sources (*Exhibit 2-4*)	Presents an updated format, organization, and content for locating useful career planning information.
	Expanded content: Career Development office	Expands discussion of services offered by campus career offices.
	Updated content: Industry trends	Lists job opportunities with the greatest potential for career success in various industries.
	Revised Financial Literacy for My Life *feature*	Discusses career options related to social entrepreneurship, gig economy, shared economy, and circular economy, along with the availability of microloans for business funding.
	New Smart Money Minute *feature*	Emphasizes actions to avoid spelling and grammar errors in résumés and cover letters.
	New Smart Money Minute *feature*	Points out actions to take for a condensed cover letter.
	Revised Financial Literacy for My Life *feature*	Provides an overview of common employee benefits along with innovative benefits offered by various companies.
	New Smart Money Minute *feature*	Discusses the use of artificial intelligence (AI) for identifying and hiring employees.
	New example: Social media résumé	Suggests methods for the use of social media to communicate career competencies to hiring managers.
	New content: F-O-C-U-S for a résumé and cover letter	Communicates key elements of a résumé and cover letter to enhance job search success.

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 2 (Cont.)	*New content:* Preparing a cover letter	Highlights key items when preparing a cover letter.
	Revised exhibit: Interview questions you should expect (*Exhibit 2-D*)	Presents additional commonly encountered interview questions.
	New example: Checklist for interview success	Provides a list of factors to consider for enhanced interview success.
	Revised Smart Money Minute *feature*	Presents information on the use of simulations and job auditions as part of the interview process.
	Revised How To: Prepare for a Case Interview	Updates information to prepare for a case interview as part of the job application process.
Chapter 3	*Revised exhibit format:* Creating a personal balance sheet	Provides an updated format to enhance visual appeal and learning of balance sheet components.
	New Smart Money Minute *feature*	Suggests sources of grants and scholarships that go unused along with a reference to the Chapter 7 Appendix.
	Revised exhibit format: Creating a cash flow statement of income and outflows	Presents a revised format for improved understanding of cash inflows and outflows.
	New Smart Money Minute *feature*	Offers actions to take for keeping accurate financial records and to reduce financial stress.
	New Smart Money Minute *feature*	Suggests sources for additional income to enhance a person's financial situation.
	New Smart Money Minute *feature*	Presents financial rules of thumb for wise money management and for achieving saving and financial goals.
	New Smart Money Minute *feature*	Presents innovative apps and websites related to savings, borrowing, and other financial decisions.
	New Smart Money Minute *feature*	Reports on the financial attitudes and behaviors of young adults based on *Better Money Habits Millennial Report* conducted by Bank of America.
	Repositioned Appendix: Money Management Information Sources and Advisors	Presents updated money management and financial planning sources at the end of the chapter instead of at the end of the book.
	New Smart Money Minute *feature*	Points out the availability of robo-advisors to guide financial planning activities.
Chapter 4	*Updated content:* Tax Cuts and Jobs Act (TCJA)	Provides an updated, detailed incorporation of the new tax legislation.
	Updated content: Gift taxes	Covers new gift tax limits for 2018.
	Revised exhibit: Computing taxable income and tax liability (*Exhibit 4-1*)	Incorporates changes for the computation due to the TCJA.
	Revised content: Standard deductions	Updated annual limit for standard deduction for 2018.
	Revised content: Medical expense deduction	Incorporates changes for the computation due to the TCJA.
	Revised content: Itemized deductions	Incorporates changes for what is eligible due to the TCJA.
	Revised content: Tax rates	Demonstrates how to calculate total tax due using a tax bracket schedule, with most current tax rate information.
	Expanded content: Health care and taxes	Updates students on key changes related to the Affordable Care Act.

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 4 (Cont.)	*Revised content:* Tax credits	Covers revised tax credits for 2018.
	Revised content: Tax forms	Updated for basic tax form to be used starting with 2018. Eliminating 1040A and 1040EZ.
	Revised content: Filing taxes online	Updates students on the most recent process for filing taxes online.
	Revised content: Tax scams	Describes the latest and most popular tax scams.
	Revised exhibit: How to avoid common filing errors (*Exhibit 4-8*)	Provides an updated, detailed list of steps one might take to reduce the likelihood of a filing error.
	Revised Smart Money Minute *feature*	Updates statistics on the likelihood of a tax audit in recent years.
	Revised content: Capital gains	Incorporates changes for new tax rates due to the TCJA for capital gains.
	Revised content: Kiddie tax	Incorporates changes for new tax rates due to the TCJA for children's investment income.
Chapter 5	*New* Smart Money Minute *feature*	Explains an app program from Instant Financial that allows employees to access 50 percent of their pay each day they work.
	Updated data: Understanding interest rates	Provides data for various interest rates that affect spending, saving, borrowing, and investing decisions
	New Smart Money Minute *feature*	Offers suggestions to avoid or minimize unnecessary banking fees.
	New content: Other financial service providers	Provides an overview of nonbank organizations offering financial services, such as retailers, internet banks, and P2P (peer-to-peer) lending networks.
	Revised exhibit: Choosing a financial institution (*Exhibit* 5-5)	Presents a focused process for assessing and selecting a financial institution.
	New Smart Money Minute *feature*	Discusses savings plans available for financing college education along with a reference to the Chapter 7 Appendix.
	Revised content: Savings bonds	Updates current information related to buying and redeeming savings bonds.
	Expanded content: Financial Literacy for My Life *feature*	Adds discussion of informal remittance networks to other alternative financial services used around the world.
	Revised content: Deposit insurance	Updates information on credit union deposit insurance coverage.
	New Smart Money Minute *feature*	Provides information on the benefits and concerns associated with Bitcoin and other crypto-currencies.
	Revised How To: Avoid Identity Theft	Expands suggestions to prevent identity theft with an update of sources for assistance.
	New Smart Money Minute *feature*	Presents technology examples for emerging financial services, such as video tellers, facial recognition payments, and banking virtual assistants.
	New content: Money transfers	Provides an overview of methods to send funds across the country or around the world.

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 6	*Updated exhibit:* Volume of consumer credit (*Exhibit 6-1*)	Illustrates that the volume of consumer credit has been increasing steadily.
	New Smart Money Minute *feature*	Cautions what to watch for when activating a new credit card.
	New content: Use of smartphones	Describes the popularity and the use of smartphones worldwide.
	New content: Home equity loans	Explains how the Tax Cuts and Jobs Act of 2017 affects the deduction for home equity loans.
	Revised content: Debit and credit card fraud	Updated statistics and explanation for protecting yourself against credit card fraud.
	New content: Building and maintaining your credit rating	Describes a 2015 legal settlement that requires the Credit Reporting Agencies to reduce credit report errors.
	New content: What is in your credit files?	Summarizes the information contained in your credit report.
	New content: Time limits on adverse data	Explains that tax liens can be reported for 15 years on your credit report.
	New Financial Literacy for My Life *feature*	Describes what to do if you were affected by the Equifax data breach.
	New Smart Money Minute *feature*	Provides information on how to obtain your free credit reports from the three major credit reporting agencies.
	New Smart Money Minute *feature*	Explains that consumers are becoming more credit conscious and checking their credit scores more often.
	Revised content: FICO and VantageScore	Updates information about new FICO and VantageScore products.
	New and revised content: Financial Planning Problems	
Chapter 7	*New content:* Inexpensive loans	Refers readers to Chapter 7 Appendix: Education Financing, Loans, and Scholarships.
	Revised content: Medium-priced loans	Notes that 109 million members of the nation's 5,900 credit unions hold over $1.4 trillion in assets.
	New Smart Money Minute *feature*	Explains that debt collection is a $10.9 billion industry and employs nearly 120,000 workers.
	New content: Debt collection practices	Describes that in March 2018, the FTC and CFPB received 84,500 debt collection complaints.
	New Smart Money Minute *feature*	Explains what to do if you make a mistake of getting behind in paying your bills.
	New Smart Money Minute *feature*	Cautions readers about credit repair clinics.
	Updated exhibit: Consumer bankruptcy filings (*Exhibit 7-4*)	Provides up-to-date statistics on U.S. consumer bankruptcy filings from 1980–2017.
	Revised content: Chapter 7 bankruptcy	Updates fees on Chapter 7 bankruptcy in the United States for 2018.
Chapter 8	*New* Financial Literacy for My Life *feature*	Provides suggestions for obtaining the best buys for products and services during each month of the year.
	New Smart Money Minute *feature*	Encourages actions to avoid financial difficulties when people do not clearly distinguish needs from wants.

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 8 (Cont.)	*New* Smart Money Minute *feature*	Presents information on current retailing technology trends designed to enhance the shopping experience.
	New Smart Money Minute *feature*	Describes the features of car subscription services.
	Updated Financial Literacy for My Life *feature*	Includes updated coverage of romance scams, the "yes" scam, and other fraudulent activities.
	New content: Scholarship and financial aid scams	Warns students of fraudulent college financing programs along with a reference to the Chapter 7 Appendix.
	New Smart Money Minute *feature*	Warns consumers of the safety and financial dangers of buying fake and counterfeit products.
	New Smart Money Minute *feature*	Suggests a method for increasing amounts saved by putting the "You Saved" amount from a receipt in a savings account.
	Repositioned Appendix: Consumer Protection Agencies and Organizations	Presents contact information for federal, state, local agencies, and other organizations at the end of the chapter instead of at the end of the book.
Chapter 9	*Revised exhibit:* The home-buying process (*Exhibit 9-5*)	Presents clarified information for the steps in the home-buying process.
	Revised content: Assess types of housing	Enhances coverage of multiunit dwellings, duplexes, town houses, and planned unit developments (PUDs).
	New content: Housing construction	Expands discussion of factory-built houses, prefabricated homes, modular homes, mobile homes, and manufactured homes.
	New Smart Money Minute *feature*	Discusses the benefits and limitations of tiny houses (400 square feet or less).
	New Smart Money Minute *feature*	Suggests actions to plan for overlooked costs when buying a home.
	New Smart Money Minute *feature*	Recommends the best times of the year to buy and sell a house.
	New content: United States Department of Agriculture (USDA) loan program	Reports on a government home loan program to finance housing and community facilities in rural areas.
	New Smart Money Minute *feature*	Discusses current home buying attitudes and behaviors among young people based on a Harris poll, conducted on behalf of Trulia.
	Revised Financial Literacy for My Life *feature*	Presents actions to take when deciding whether to pay off a mortgage early.
	Revised exhibit: The main elements of buying a home (*Exhibit 9-12*)	Provides an updated, condensed overview of the major elements of home buying.
	New content: Lifestyle inflation	Cautions about overspending on housing and other items when receiving a salary increase.
	New content: Down payment wire fraud	Warns about the growing threat of identity fraud and monetary loss when processing personal and financial information for a home purchase.
	New Smart Money Minute *feature*	Reports upgrades with the largest payoffs when selling a home along with desirable paint shades for various rooms.

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 10	*New* Financial Literacy for My Life *feature*	Cautions readers that insurance companies may exclude coverage for certain losses.
	New Financial Literacy for My Life *feature*	Explains the importance of purchasing flood insurance.
	New Financial Literacy for My Life *feature*	Describes what steps to take if you are in an accident caused by another driver.
	Revised Smart Money Minute *feature*	Cautions that distracted driving can be dangerous, and offers tips to avoid it.
	New Financial Planning Problems	
Chapter 11	*New* Smart Money Minute *feature*	Describes how you can save time and money by receiving health care from a primary care physician.
	Revised content: High medical costs	Provides revised and updated information on runaway health care costs.
	Revised content: Rapid increase in medical expenditures	Updates data on medical expenditures.
	Revised exhibit: U.S. national health expenditures (*Exhibit 11-1*)	Provides projected health care costs to year 2026.
	New content: High costs of health care	Describes President Trump's executive order.
	New content: Reducing health care costs	Offers additional suggestions for staying healthy and well.
	New content: Group health insurance	Explains new Association Health Plans for small businesses, their employees, and proprietors.
	New Smart Money Minute *feature*	Discusses medical care benefit plans provided by employers to their employees in 2017.
	New Financial Literacy for My Life *feature*	Summarizes the specific qualifying events and qualified beneficiaries to elect continuation coverage under COBRA.
	New Smart Money Minute *feature*	Provides phone numbers and websites for COBRA, ACA, HIPAA, and ERISA.
	New Smart Money Minute *feature*	Provides the latest data on disability and long-term care services.
	Revised content: Long-term care insurance	Updates nursing home costs in the United States.
	New exhibit: Coverage limits of long-term care (*Exhibit 11-4*)	Summarizes the very limited long-term care coverage that Medicare, Medigap, and private health insurance provide.
	Revised Financial Literacy for My Life *feature*	Explains how HSAs work in 2019.
	New content: HSAs	Cautions that if you continue contributing to your HSA, you should not apply for Medicare or Social Security.
	New content: Medicare	Provides new contact information for Medicare websites.
	New content: Medicare and the Affordable Care Act	Explains that if you have Medicare Part A, you meet the requirement for having health coverage under the Affordable Care Act.
	New content: Medigap	Expands discussion about Medigap policies, and services they do and do not cover.
	New Smart Money Minute *feature*	Explains how Medicaid costs are rising rapidly.

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 11 (Cont.)	*New content:* The American Health Care Act of 2017	Describes the attempt to repeal and replace the Affordable Care Act.
	New content: Shared responsibility	Explains that starting in 2019, the Tax Cuts and Jobs Act repeals the Affordable Care Act mandate to have health insurance or pay a penalty.
	Expanded content: Health insurance marketplace	Explains that if you have Medicare, you don't need to worry about the marketplace.
	New Financial Literacy for My Life *feature*	Describes five questions to ask yourself when choosing a plan.
	New content: College students and the marketplace	Explains what college students need to know about the marketplace.
	New Financial Planning Problem	
Chapter 12	*Revised content:* Life insurance	Provides updated information on life insurance policies and their face value for most recent years.
	New content: The reality of life	Shows statistics regarding the need for life insurance to provide for family members.
	Revised exhibit: Life expectancy (*Exhibit 12-2*)	Provides updated information on life expectancy for most recent years.
	Revised examples: Multiple Method, DINK Method, Non-Working Spouse Method	Provides revised examples to demonstrate the use of the methods for students.
	Revised Smart Money Minute *feature*	Provides information on the amount of hours and equivalent wage of a stay-at-home mom.
	New content: Reentry term	Provides information about an additional type of term insurance policy.
	New content: Modified life	Provides information about an additional type of whole life insurance policy.
	Revised Smart Money Minute *feature*	Provides updated statistics about the average face amount of life insurance policies.
	Revised exhibit: Growth of individual, group, and credit life insurance (*Exhibit 12-7*)	Shows updated data for the growth of different classes of life insurance.
	New content: Joint life insurance	Includes additional variations of life insurance policies that are available.
	Revised content: The cost of insurance	Shows an updated example of the cost of life insurance, including the time value of money.
	New content: Installment payments	Includes additional variations of installment payments for life insurance benefits.
Chapter 13	*Expanded content:* Budgeting	Describes how software and mobile apps can improve budgeting skills.
	Updated statistics: Credit cards	Reports current statistics on credit cards, credit card debt, and student debt.
	New Smart Money Minute *feature*	Describes how one investor avoided making a costly mistake by researching an investment that turned out to be a pyramid scheme.
	New example: Risk-return trade-off	A new example describes a recent price decline for Johnson & Johnson's stock.

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 13 (Cont.)	*New example:* Return on investment	Illustrates how to calculate return on investment for a stock investment in the Lowes Home Improvement chain.
	New example: Effect of changing interest rates on bond prices	Illustrates how bond prices can change for a John Deere corporate bond when interest rates in the economy change.
	New example: Business failure risk	Describes what happened to investors when Toys R Us filed for bankruptcy and eventually closed all its stores.
	New content: Growth investments	Explains why Facebook, Amazon, and Netflix are examples of growth stocks.
	New content: Dow Jones Average	Describes the largest one-day point decline in the history of the Dow Jones Average.
	Revised Smart Money Minute *feature*	Includes new statistics for income for American families.
	Revised exhibit: Asset allocation (*Exhibit 13-2*)	Illustrates the concept of asset allocation for an investor who is 28 years old.
	New example: Interest calculations	Illustrates interest calculations for a Ford Motor Credit Company bond.
	New content: Mutual fund fees	Provides more information on typical fees associated with mutual fund investments.
	New content: Real estate returns	Updates the statistics for average real estate returns.
	Updated content: Investment taxation	Describes how the Tax Cuts and Jobs Act of 2017 affects how investment gains are taxed.
	New examples: Information available on the Internet	Provides information for an additional search engine (Bing) and a new investor link for Exxon Mobil.
	Revised exhibit: Useful sites for financial planning (*Exhibit 13-6*)	Provides additional information on individual websites.
	Updated Financial Planning Activities	Includes a link to *The Occupational Outlook Handbook*.
	New Financial Planning Case	Provides details about the financial situation of John and Nina Hartwick, a couple in their mid-30s who earn over $100,000 a year, but after monthly expenses never have enough money to establish an emergency fund or save.
Chapter 14	*Revised example:* McDonald's	Reports the increased value of an investment in McDonald's stock at the end of 10 years.
	New content: Taxation of investments	Provides new information about taxation of long-term and short-term investments.
	New example: Stocks can lose money	Describes how the Dow Jones Industrial Average suffered the largest one-day decline in history.
	New example: Starbucks's dividend payments	Includes information about how to determine the record date for a corporate stock.
	New exhibit: Stock investment in Apple (*Exhibit 14-2*)	Illustrates how an investor can earn a profit from an investment in Apple.
	Revised exhibit: Stock classifications (*Exhibit 14-4*)	Provides a revised definition for a penny stock.
	New exhibit: Stock price information on the internet (*Exhibit 14-5*)	Reports current information for The Gap, as reported on Yahoo! Finance.

Chapter	Selected Topics	Benefits for the Teaching–Learning Environment
Chapter 14 (Cont.)	*Revised* Smart Money Minute *feature*	Includes statistics for the Dow Jones Industrial Average for 2016 and 2017.
	New exhibit: Value Line report for Home Depot (*Exhibit 14-7*)	Provides detailed financial information from Value Line about Home Depot.
	New content: Projected earnings	Describes the importance of projected earnings for Visa.
	Revised Financial Literacy Calculations *feature*	Calculates and then describes the importance of a price/earnings to growth ratio for Visa.
	New examples: Current ratios	Uses current information for 3M Company and American Airlines to calculate dividend payout, dividend yield, total return, annualized holding period yield, and beta.
	Revised content: Buying and selling stocks	Describes the recent IPO for Snap along with an update for the value of its stock, one year later.
	Revised How To: Open an Account with a Brokerage Firm	Provides new information about the amount required to open an account, commissions charged for online trades, and other information about specific brokerage firms.
	New Smart Money Minute *feature*	Explains the types of services provided by a robo-advisor.
	Revised exhibit: Dollar cost averaging (*Exhibit 14-9*)	Includes current share prices for 2017 and 2018 for Johnson & Johnson.
	New example: Margin transaction	Provides a new example for a margin transaction for Pepsico.
Chapter 15	*Revised example:* Asset Allocation	Includes additional information about asset allocation in the example in the chapter introduction.
	New example: Convertible bonds	Provides new information about a convertible bond issued by Intercept Pharmaceuticals.
	Revised example: Current interest rates	Reduced interest rate from 8 percent to 6 percent to reflect current interest rates for corporate bonds.
	Revised Financial Literacy for My Life *feature*	Explains why one couple chose two bond funds to earn investment returns with minimal risk.
	New example: Interest income	Illustrates how to calculate interest for a bond issued by Microsoft.
	New example: Bond price fluctuations	Provides an example of how the price for a corporate bond issued by Apple can increase or decrease until maturity.
	New example: Bonds in bankruptcy	Illustrates what happened to Toys R Us bondholders.
	New exhibit: Bond transaction (*Exhibit 15-3*)	Describes a typical bond transaction for a corporate bond issued by Apple.
	Revised Financial Literacy Calculations *feature*	Includes a new tryout problem that illustrates the time value of reinvested interest for a bond issued by Visa.
	New content: Treasury bills	Provides more information about current rates for T-bills.
	New weblinks: Investor websites	Includes new links to bond websites for investors.
	New exhibit: FINRA bond coverage (*Exhibit 15-6*)	Adds new information available from the Financial Industry Regulatory Authority (FINRA) for a Tesla bond.
	Revised How To: Evaluate Corporate, Government, and Municipal Bonds	Includes new material about the bond screeners available on the Fidelity and Charles Schwab websites.

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 15 (Cont.)	*Revised exhibit:* Bond ratings (*Exhibit 15-7*)	Contains new information for the BBB– and BB+ bond ratings.
	New example: Boeing	Calculates current yield and yield to maturity calculations for Boeing.
	Revised Financial Literacy Calculations *feature*	Calculates the times interest earned ratio for Home Depot.
Chapter 16	*New* Chapter Opener *example*	Explains why one investor chose the T. Rowe Price Dividend Income fund for his investment portfolio.
	Revised content: Statistics for funds	Provides the latest available statistics for mutual funds.
	Revised content: Fund fees	Reports that the average load charge is now 3 to 5 percent.
	Revised content: Fund fees	Reports that the average management fee is now 0.5 to 2 percent.
	Revised exhibit: Fund fees (*Exhibit 16-2*)	Provides updated information from the fee table for the Davis New York Venture fund.
	Revised exhibit: Fund fees (*Exhibit 16-3*)	Summarizes the changes made throughout the chapter.
	Revised content: Type of funds	Includes revised amounts for large-cap funds (now $10 billion), mid-cap funds (now $2 to $10 billion), small-cap funds (now less than $2 billion).
	Revised Smart Money Minute *feature*	Describes why people invest in mutual funds.
	Revised How To: Open an Investment Account and Begin Investing in Funds	Adds more material on different types of investment accounts.
	New content: Economic factors	Provides new information about the relationship between the nations economy and a fund's performance and a fund's financial returns.
	Revised exhibit: Large fund families (*Exhibit 16-4*)	Describes the three large mutual fund companies: Vanguard, Fidelity, and American Funds.
	New exhibit: Fund research (*Exhibit 16-5*)	Illustrates detailed research information about the Fidelity Contrafund available from Morningstar.
	New exhibit: Kiplinger's Favorite Funds (*Exhibit 16-6*)	Shows a portion of the information available in the Kiplinger's 25 Favorite No Load Mutual Funds article.
	New example: Return on investment	Illustrates how an investor can earn a capital gain on an investment in the T. Rowe Price Communications and Technology fund.
	New content: Taxes and funds	Provides more information about how the 2017 Tax Cuts and Jobs Act affects fund investments.
	New and revised Financial Planning Problems	
Chapter 17	*New content:* How the Tax Cuts and Jobs Act affects home ownership	Explains how the new tax law reduces the tax benefit of owning a home.
	New exhibit: Annual home ownership rates for the United States by age groups (*Exhibit 17-2*)	Provides an insight into home ownership in the United States by age groups: 1982–2017.
	New Financial Literacy for My Life *feature*	Describes steps to take if you have been scammed and provides additional resources for help.

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 17 (Cont.)	*Revised content:* REITs	Provides the latest available data on REITs.
	Revised Financial Literacy for My Life *feature*	Includes when Ginnie Mae, Sonny Mae, and Nellie Mae were established.
	New content: The Tax Cuts and Jobs Act	Explains how the new tax law limits the mortgage interest deduction and capital gains exclusions.
	Revised exhibit: Gold prices (*Exhibit 17-3*)	Illustrates how the price of gold has fluctuated from 1976 to 2018.
	Revised Smart Money Minute *feature*	Shows the biggest producers of gold in the world as of 2016.
	Revised content: Prices of precious metals	Includes the latest prices of silver, platinum, palladium, and rhodium.
	New Smart Money Minute *feature*	Describes how color, cut, clarity, and carat determine the value of diamonds.
	New Smart Money Minute *feature*	Cautions that many sellers of collectibles and coins promise false "buy back" options.
	New Smart Money Minute *feature*	Emphasizes comparing quality, price, and service before buying jewelry, precious stones, or collectibles.
Chapter 18	*Revised content:* Centenarians	Explains that the number of centenarians in the United States is increasing.
	New exhibit: Older household expenditures (*Exhibit 18-4*)	Illustrates how an "average" older household spends its money.
	New content: Inflation rate	Includes the annual inflation rate in 2018.
	Revised content: Social Security	Explains that today 66 million people collect over $1 trillion in Social Security benefits.
	Revised Smart Money Minute *feature*	Shows what groups are collecting Social Security as of 2017.
	New Smart Money Minute *feature*	Explains the importance of delaying Social Security benefits at least until the full retirement age.
	New Smart Money Minute *feature*	Offers suggestions on when one should begin receiving retirement benefits from Social Security.
	New How To: Choose a Social Security Benefit Calculator	Explains how to choose a Social Security calculator.
	Revised exhibit: Number of workers per beneficiary (*Exhibit 18-8*)	Illustrates how the number of workers per beneficiary has plummeted over the decades.
	Revised content: 401(k) plans	Updates the contribution limits for 2018.
	Revised Smart Money Minute *feature*	Shows that there are nearly 24,000 private-sector defined benefit plans protected by PBGC.
	Revised content: IRAs	Updates the Roth IRA contribution limits for 2018.
	Revised content: SEP-IRAs	Updates the SEP-IRA contribution limits for 2018.
	New content: Dipping into your nest egg	Explains the tax consequences of early withdrawals from retirement accounts.
	New Financial Planning Problems	

Chapter	*Selected Topics*	Benefits for the Teaching–Learning Environment
Chapter 19	*Revised content:* New lifestyles	Points out that the new tax law allows $11,800,000 exemption for estate taxes.
	Revised content: Stated Dollar Amount Will	Explains that the new tax law allows you to pass on the stated amount of $11,800,000 in 2018.
	Revised content: Aging with dignity	Explains that “Five Wishes” is now valid in 42 states and in the District of Columbia.
	New content: Credit shelter trust	Provides updated and new information about the Tax Cuts and Jobs Act and the new exemption amounts for 2018.
	Revised content: Testamentary trust	Describes that testamentary trusts do not protect assets from the probate process.
	Revised content: Federal and state estate taxes	Provides the latest available information about gift and estate taxes under the Tax Cuts and Jobs Act of 2017.
	New Smart Money Minute *feature*	Emphasizes the importance of lifetime gifting to reduce estate taxes.
	Updated exhibit: Estate tax law changes (*Exhibit 19-6)*	Includes the new exemption amounts for 2017, 2018, and beyond (until 2025).
	Revised content: Self-test problems	Covers new tax law exemptions for gifting.
	Revised content: Financial Planning Problems	

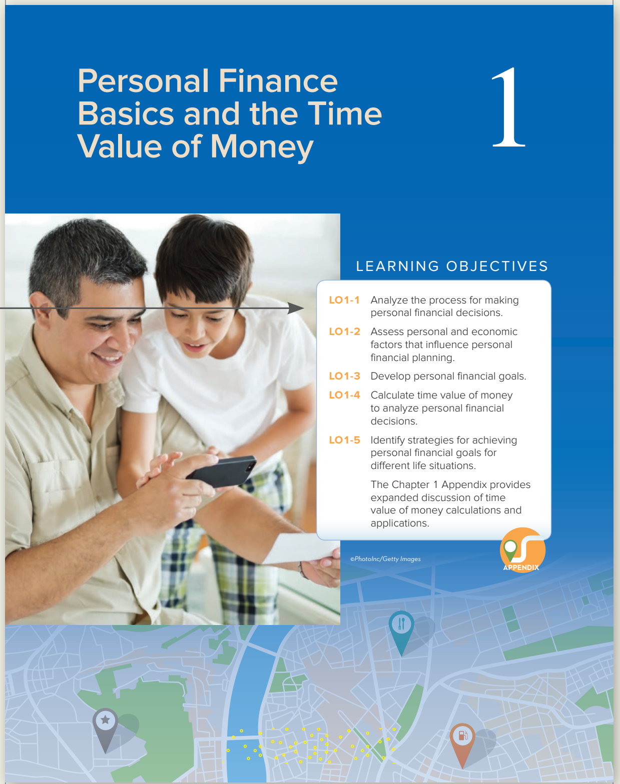
ASSURANCE OF LEARNING

Many educational institutions today are focused on the notion of assurance of learning, an important element of some accreditation standards. *Personal Finance,* 13th edition, is designed specifically to support your assurance of learning initiatives with a simple, yet powerful, solution.

Each test bank question for *Personal Finance,* 13th edition, 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.

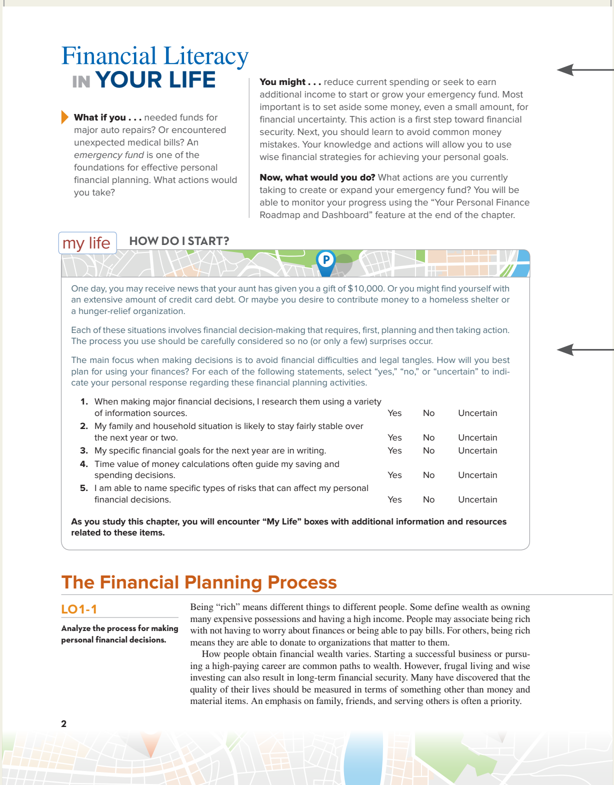
GUIDED TOUR

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



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.



Financial Literacy IN YOUR LIFE

What if you . . . needed funds for major auto repairs? Or encountered unexpected medical bills? An *emergency fund* is one of the foundations for effective personal financial planning. What actions would you take?

You might . . . reduce current spending or seek to earn additional income to start or grow your emergency fund. Most important is to set aside some money, even a small amount, for financial uncertainty. This action is a first step toward financial security. Next, you should learn to avoid common money mistakes. Your knowledge and actions will allow you to use wise financial strategies for achieving your personal goals.

Now, what would you do? What actions are you currently taking to create or expand your emergency fund? You will be able to monitor your progress using the "Your Personal Finance Roadmap and Dashboard" feature at the end of the chapter.

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 tangles. 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.

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 obtain financial wealth 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. Many have discovered that the quality of their lives should be measured in terms of something other than money and material items. An emphasis on family, friends, and serving others is often a priority.

2

Financial Literacy in Your Life

Covers why and how the issues presented in the chapter are important, and presents some alternatives that one might consider when facing related decisions. There is a strong emphasis here on action.

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 . . . Choose a Credit Counselor

Credit counseling organizations provide valuable assistance to financially distressed consumers. However, some firms may be misleading you about who they are, what they do, or how much they charge. Experts advise that you ask the following questions to find the best credit counselor.

- *What services do you offer?* Look for an organization that offers budget counseling and money management classes as well as a debt-management plan.
- *Do you offer free information?* Avoid organizations that charge for information or demand details about your problem first.
- *What are your fees?* Are there set-up and/or monthly fees? A typical set-up fee is $10. If you're paying a lot more, you may be the one who's being set up.
- *How will the debt-management plan work?* What debts can be included in the plan, and will you get regular reports on your accounts?
- *Can you get my creditors to lower or eliminate my interest and fees?* If the answer is yes, contact your creditors to verify this.
- *What if I can't afford to pay you?* If an organization won't help you because you can't afford to pay, go somewhere else for help.
- *Will you help me avoid future problems?* Getting a plan for avoiding future debt is as important as solving the immediate debt problem.
- *Will we have a contract?* All verbal promises should be in writing before you pay any money.
- *Are your counselors accredited or certified?* Legitimate credit counseling firms are affiliated with the National Foundation for Credit Counseling or the Association of Independent Consumer Credit Counseling Agencies.

Check with your local consumer protection agency and the Better Business Bureau to see if any complaints have been filed about the company.

Financial Literacy for My Life

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

Financial Literacy for My Life

IS IT TAXABLE INCOME? IS IT DEDUCTIBLE?

Certain financial benefits individuals receive are not subject to federal income tax. Indicate whether each of the following items would or would not be included in taxable income when you compute your federal income tax.

Is it taxable income?	Yes	No
1. Lottery/Jackpot winnings	_____	_____
2. Child support received	_____	_____
3. Worker's compensation benefits	_____	_____
4. Life insurance death benefits	_____	_____
5. Cash rebate for laptop	_____	_____
6. Unemployment income	_____	_____

Indicate whether each of the following items would or would not be deductible when you compute your federal income tax.

Is it deductible?	Yes	No
7. Life insurance premiums	_____	_____
8. Baggage fees for self-employed	_____	_____
9. Fees for traffic violations	_____	_____
10. Mileage for driving to volunteer work	_____	_____
11. An attorney's fee for preparing a will	_____	_____
12. Income tax preparation fee	_____	_____

Note: These taxable income items and deductions are based on the 2018 tax year and may change due to changes in the tax code.

Answers: 1, 6, 8, 10—yes; 2, 3, 4, 5, 7, 9, 11, 12—no.

Financial Literacy Calculations

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

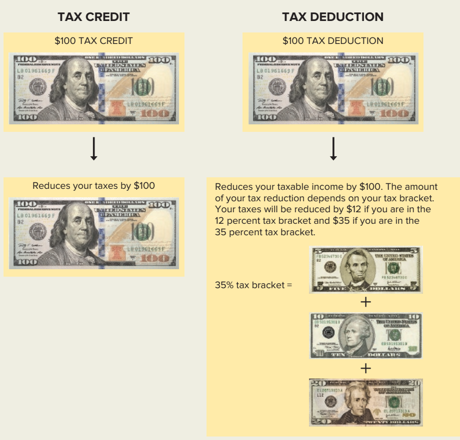
Financial Literacy Calculations

TAX CREDITS VERSUS TAX DEDUCTIONS

Many people confuse *tax credits* with *tax deductions.* Is one better than the other? A *tax credit,* such as eligible child care or dependent care expenses, results in a dollar-for-dollar reduction in the amount of taxes owed. A *tax deduction,* such as an itemized deduction in the form of medical expenses, mortgage interest, or charitable contributions, reduces the taxable income on which your taxes are based.

Shown at right is how a $100 tax credit compares with a $100 tax deduction:

As you might expect, tax credits are less readily available than tax deductions. To qualify for a $100 child care tax credit, you may have to spend $500 in child care expenses. In some situations, spending on deductible items may be more beneficial than qualifying for a tax credit. A knowledge of tax law and careful financial planning will help you use both tax credits and tax deductions to maximum advantage.



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Key Terms

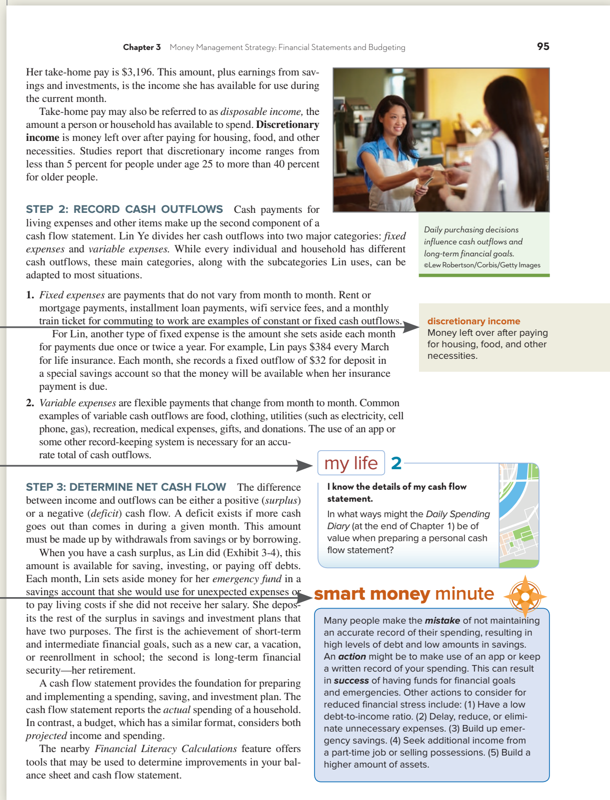
Key terms appear in bold type and in the margin definition boxes. The terms and their page references are also listed at the end of each chapter.

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.

Smart Money Minute

Each chapter contains several *Smart Money Minute* features with fun facts, information, and financial planning assistance. Many in this new edition focus on the ways that technology is changing personal finance.



Chapter 3 Money Management Strategy: Financial Statements and Budgeting **95**

Her take-home pay is $3,196. This amount, plus earnings from savings and investments, is the income she has available for use during the current month.

Take-home pay may also be referred to as *disposable income,* the amount a person or household has available to spend. **Discretionary income** is money left over after paying for housing, food, and other necessities. Studies report that discretionary income ranges from less than 5 percent for people under age 25 to more than 40 percent for older people.

Daily purchasing decisions influence cash outflows and long-term financial goals.
©Lew Robertson/Corbis/Getty Images

STEP 2: RECORD CASH OUTFLOWS Cash payments for living expenses and other items make up the second component of a cash flow statement. Lin Ye divides her cash outflows into two major categories: *fixed expenses* and *variable expenses.* While every individual and household has different cash outflows, these main categories, along with the subcategories Lin uses, can be adapted to most situations.

1. *Fixed expenses* are payments that do not vary from month to month. Rent or mortgage payments, installment loan payments, wifi service fees, and a monthly train ticket for commuting to work are examples of constant or fixed cash outflows.
   For Lin, another type of fixed expense is the amount she sets aside each month for payments due once or twice a year. For example, Lin pays $384 every March for life insurance. Each month, she records a fixed outflow of $32 for deposit in a special savings account so that the money will be available when her insurance payment is due.
2. *Variable expenses* are flexible payments that change from month to month. Common examples of variable cash outflows are food, clothing, utilities (such as electricity, cell phone, gas), recreation, medical expenses, gifts, and donations. The use of an app or some other record-keeping system is necessary for an accurate total of cash outflows.

discretionary income
Money left over after paying for housing, food, and other necessities.

STEP 3: DETERMINE NET CASH FLOW The difference between income and outflows can be either a positive (*surplus*) or a negative (*deficit*) cash flow. A deficit exists if more cash goes out than comes in during a given month. This amount must be made up by withdrawals from savings or by borrowing.

When you have a cash surplus, as Lin did (Exhibit 3-4), this amount is available for saving, investing, or paying off debts. Each month, Lin sets aside money for her *emergency fund* in a savings account that she would use for unexpected expenses or to pay living costs if she did not receive her salary. She deposits the rest of the surplus in savings and investment plans that have two purposes. The first is the achievement of short-term and intermediate financial goals, such as a new car, a vacation, or reenrollment in school; the second is long-term financial security—her retirement.

A cash flow statement provides the foundation for preparing and implementing a spending, saving, and investment plan. The cash flow statement reports the *actual* spending of a household. In contrast, a budget, which has a similar format, considers both *projected* income and spending.

The nearby *Financial Literacy Calculations* feature offers tools that may be used to determine improvements in your balance sheet and cash flow statement.

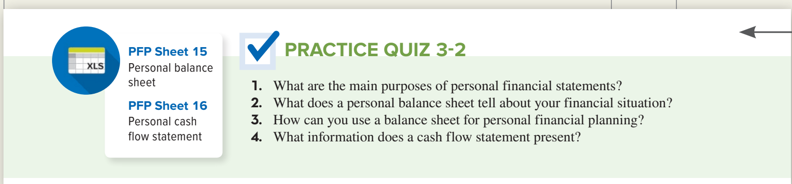
my life 2

I know the details of my cash flow statement.

In what ways might the *Daily Spending Diary* (at the end of Chapter 1) be of value when preparing a personal cash flow statement?

smart money minute

Many people make the ***mistake*** of not maintaining an accurate record of their spending, resulting in high levels of debt and low amounts in savings. An ***action*** might be to make use of an app or keep a written record of your spending. This can result in ***success*** of having funds for financial goals and emergencies. Other actions to consider for reduced financial stress include: (1) Have a low debt-to-income ratio. (2) Delay, reduce, or eliminate unnecessary expenses. (3) Build up emergency savings. (4) Seek additional income from a part-time job or selling possessions. (5) Build a higher amount of assets.



PFP Sheet 15
Personal balance sheet

PFP Sheet 16
Personal cash flow statement

PRACTICE QUIZ 3-2

1. What are the main purposes of personal financial statements?
2. What does a personal balance sheet tell about your financial situation?
3. How can you use a balance sheet for personal financial planning?
4. What information does a cash flow statement present?

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.

Your Personal Finance Roadmap and Dashboard:

Money Management

A monthly cash flow analysis will help you achieve various financial goals.

By comparing your cash inflows (income) and cash outflows (spending), you will determine if you have a *surplus* or *deficit*. A surplus allows you to save more or pay off debts. A deficit reduces your savings or increases the amount you owe.

Your Situation

Do you maintain a record of cash inflows and outflows? Does your cash flow situation reflect a deficit with unnecessary spending? How can you reduce spending to improve your cash flow situation? Other money management actions you might consider during various stages of your life include:

First Steps

- Maintain spending diary to monitor daily finances.
- Create a system for financial records and documents.
- Use a budget that includes savings.
- Create a personal balance sheet and income statement on an annual basis.
- Accumulate an appropriate emergency fund.
- Revise budget.

Next Steps

- Update personal financial statements.
- Begin investment program for funding children's education.
- Adapt budget to changing household needs.

Later Steps

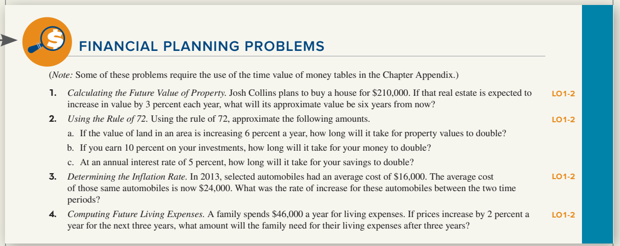
- Determine potential changes in daily spending needs during retirement.
- Consider increased savings and contributions to retirement plans.

Personal Finance Roadmap and Dashboard

There are increasing numbers of nontraditional students taking personal finance. The Dashboard feature provides students of all ages with a high-level snapshot outlining how to evaluate progress for key financial planning activities. The Roadmap at the end of each chapter provides personal finance action items for students of all ages.

Financial Planning Problems

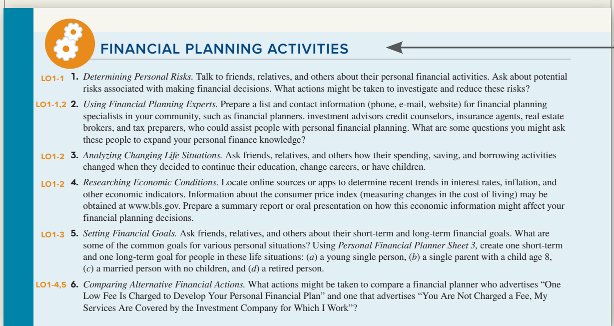
With more added to this edition, these problems allow students to apply their quantitative analysis of personal financial decisions.



FINANCIAL PLANNING PROBLEMS

(*Note:* Some of these problems require the use of the time value of money tables in the Chapter Appendix.)

1. *Calculating the Future Value of Property.* Josh Collins plans to buy a house for $210,000. If that real estate is expected to increase in value by 3 percent each year, what will its approximate value be six years from now? LO1-2
2. *Using the Rule of 72.* Using the rule of 72, approximate the following amounts. LO1-2
   a. If the value of land in an area is increasing 6 percent a year, how long will it take for property values to double?
   b. If you earn 10 percent on your investments, how long will it take for your money to double?
   c. At an annual interest rate of 5 percent, how long will it take for your savings to double?
3. *Determining the Inflation Rate.* In 2013, selected automobiles had an average cost of $16,000. The average cost of those same automobiles is now $24,000. What was the rate of increase for these automobiles between the two time periods? LO1-2
4. *Computing Future Living Expenses.* A family spends $46,000 a year for living expenses. If prices increase by 2 percent a year for the next three years, what amount will the family need for their living expenses after three years? LO1-2



FINANCIAL PLANNING ACTIVITIES

LO1-1 1. *Determining Personal Risks.* Talk to friends, relatives, and others about their personal financial activities. Ask about potential risks associated with making financial decisions. What actions might be taken to investigate and reduce these risks?

LO1-1,2 2. *Using Financial Planning Experts.* Prepare a list and contact information (phone, e-mail, website) for financial planning specialists in your community, such as financial planners. investment advisors credit counselors, insurance agents, real estate brokers, and tax preparers, who could assist people with personal financial planning. What are some questions you might ask these people to expand your personal finance knowledge?

LO1-2 3. *Analyzing Changing Life Situations.* Ask friends, relatives, and others how their spending, saving, and borrowing activities changed when they decided to continue their education, change careers, or have children.

LO1-2 4. *Researching Economic Conditions.* Locate online sources or apps to determine recent trends in interest rates, inflation, and other economic indicators. Information about the consumer price index (measuring changes in the cost of living) may be obtained at www.bls.gov. Prepare a summary report or oral presentation on how this economic information might affect your financial planning decisions.

LO1-3 5. *Setting Financial Goals.* Ask friends, relatives, and others about their short-term and long-term financial goals. What are some of the common goals for various personal situations? Using *Personal Financial Planner Sheet 3,* create one short-term and one long-term goal for people in these life situations: (*a*) a young single person, (*b*) a single parent with a child age 8, (*c*) a married person with no children, and (*d*) a retired person.

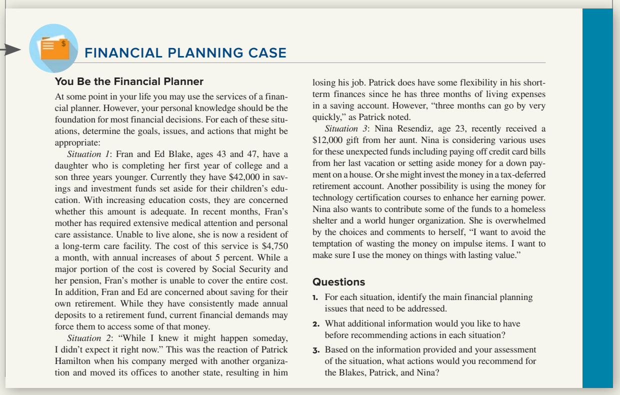
LO1-4,5 6. *Comparing Alternative Financial Actions.* What actions might be taken to compare a financial planner who advertises "One Low Fee Is Charged to Develop Your Personal Financial Plan" and one that advertises "You Are Not Charged a Fee, My Services Are Covered by the Investment Company for Which I Work"?

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 their mastery of chapter topics.



FINANCIAL PLANNING CASE

You Be the Financial Planner

At some point in your life you may use the services of a financial planner. However, your personal knowledge should be the foundation for most financial decisions. For each of these situations, determine the goals, issues, and actions that might be appropriate:

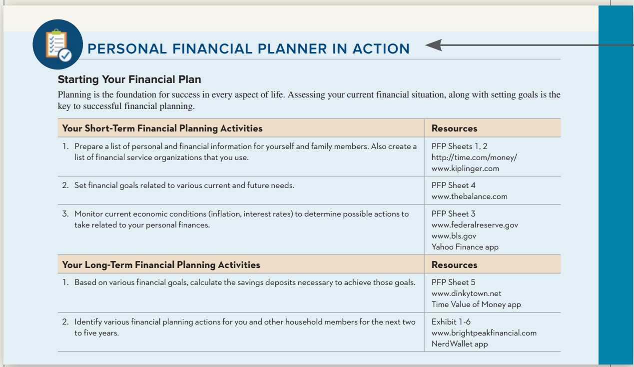
Situation 1: Fran and Ed Blake, ages 43 and 47, have a daughter who is completing her first year of college and a son three years younger. Currently they have $42,000 in savings and investment funds set aside for their children's education. With increasing education costs, they are concerned whether this amount is adequate. In recent months, Fran's mother has required extensive medical attention and personal care assistance. Unable to live alone, she is now a resident of a long-term care facility. The cost of this service is $4,750 a month, with annual increases of about 5 percent. While a major portion of the cost is covered by Social Security and her pension, Fran's mother is unable to cover the entire cost. In addition, Fran and Ed are concerned about saving for their own retirement. While they have consistently made annual deposits to a retirement fund, current financial demands may force them to access some of that money.

Situation 2: "While I knew it might happen someday, I didn't expect it right now." This was the reaction of Patrick Hamilton when his company merged with another organization and moved its offices to another state, resulting in him losing his job. Patrick does have some flexibility in his short-term finances since he has three months of living expenses in a saving account. However, "three months can go by very quickly," as Patrick noted.

Situation 3: Nina Resendiz, age 23, recently received a $12,000 gift from her aunt. Nina is considering various uses for these unexpected funds including paying off credit card bills from her last vacation or setting aside money for a down payment on a house. Or she might invest the money in a tax-deferred retirement account. Another possibility is using the money for technology certification courses to enhance her earning power. Nina also wants to contribute some of the funds to a homeless shelter and a world hunger organization. She is overwhelmed by the choices and comments to herself, "I want to avoid the temptation of wasting the money on impulse items. I want to make sure I use the money on things with lasting value."

Questions

1. For each situation, identify the main financial planning issues that need to be addressed.
2. What additional information would you like to have before recommending actions in each situation?
3. Based on the information provided and your assessment of the situation, what actions would you recommend for the Blakes, Patrick, and Nina?



PERSONAL FINANCIAL PLANNER IN ACTION

Starting Your Financial Plan

Planning is the foundation for success in every aspect of life. Assessing your current financial situation, along with setting goals is the key to successful financial planning.

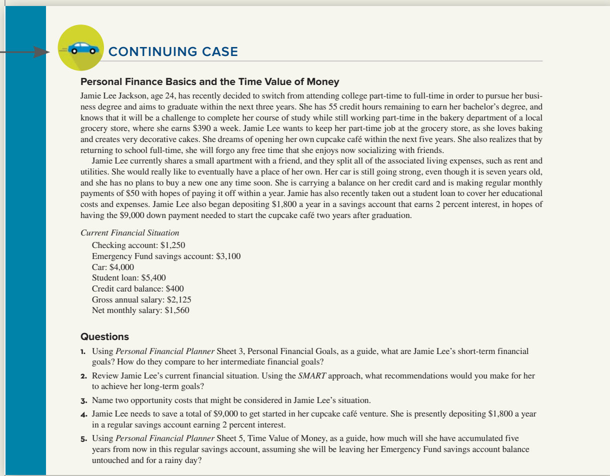
Your Short-Term Financial Planning Activities	Resources
1. Prepare a list of personal and financial information for yourself and family members. Also create a list of financial service organizations that you use.	PFP Sheets 1, 2 http://time.com/money/ www.kiplinger.com
2. Set financial goals related to various current and future needs.	PFP Sheet 4 www.thebalance.com
3. Monitor current economic conditions (inflation, interest rates) to determine possible actions to take related to your personal finances.	PFP Sheet 3 www.federalreserve.gov www.bls.gov Yahoo Finance app
Your Long-Term Financial Planning Activities	**Resources**
1. Based on various financial goals, calculate the savings deposits necessary to achieve those goals.	PFP Sheet 5 www.dinkytown.net Time Value of Money app
2. Identify various financial planning actions for you and other household members for the next two to five years.	Exhibit 1-6 www.brightpeakfinancial.com NerdWallet app

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) along with websites and apps for further guidance.

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 real life and then respond to the resulting shift in needs, resources, and priorities through the questions at the end of each case.



CONTINUING CASE

Personal Finance Basics and the Time Value of Money

Jamie Lee Jackson, age 24, has recently decided to switch from attending college part-time to full-time in order to pursue her business degree and aims to graduate within the next three years. She has 55 credit hours remaining to earn her bachelor's degree, and knows that it will be a challenge to complete her course of study while still working part-time in the bakery department of a local grocery store, where she earns $390 a week. Jamie Lee wants to keep her part-time job at the grocery store, as she loves baking and creates very decorative cakes. She dreams of opening her own cupcake café within the next five years. She also realizes that by returning to school full-time, she will forgo any free time that she enjoys now socializing with friends.

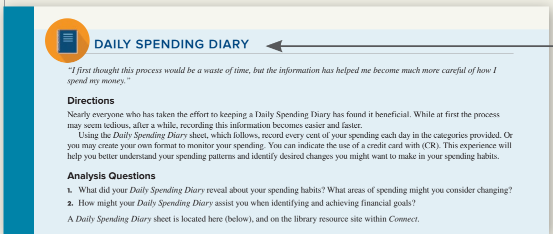
Jamie Lee currently shares a small apartment with a friend, and they split all of the associated living expenses, such as rent and utilities. She would really like to eventually have a place of her own. Her car is still going strong, even though it is seven years old, and she has no plans to buy a new one any time soon. She is carrying a balance on her credit card and is making regular monthly payments of $50 with hopes of paying it off within a year. Jamie has also recently taken out a student loan to cover her educational costs and expenses. Jamie Lee also began depositing $1,800 a year in a savings account that earns 2 percent interest, in hopes of having the $9,000 down payment needed to start the cupcake café two years after graduation.

Current Financial Situation

Checking account: $1,250
Emergency Fund savings account: $3,100
Car: $4,000
Student loan: $5,400
Credit card balance: $400
Gross annual salary: $2,125
Net monthly salary: $1,560

Questions

1. Using *Personal Financial Planner* Sheet 3, Personal Financial Goals, as a guide, what are Jamie Lee's short-term financial goals? How do they compare to her intermediate financial goals?
2. Review Jamie Lee's current financial situation. Using the *SMART* approach, what recommendations would you make for her to achieve her long-term goals?
3. Name two opportunity costs that might be considered in Jamie Lee's situation.
4. Jamie Lee needs to save a total of $9,000 to get started in her cupcake café venture. She is presently depositing $1,800 a year in a regular savings account earning 2 percent interest.
5. Using *Personal Financial Planner* Sheet 5, Time Value of Money, as a guide, how much will she have accumulated five years from now in this regular savings account, assuming she will be leaving her Emergency Fund savings account balance untouched and for a rainy day?



DAILY SPENDING DIARY

"I first thought this process would be a waste of time, but the information has helped me become much more careful of how I spend my money."

Directions

Nearly everyone who has taken the effort to keeping a Daily Spending Diary has found it beneficial. While at first the process may seem tedious, after a while, recording this information becomes easier and faster.

Using the *Daily Spending Diary* sheet, which follows, record every cent of your spending each day in the categories provided. Or you may create your own format to monitor your spending. You can indicate the use of a credit card with (CR). This experience will help you better understand your spending patterns and identify desired changes you might want to make in your spending habits.

Analysis Questions

1. What did your *Daily Spending Diary* reveal about your spending habits? What areas of spending might you consider changing?
2. How might your *Daily Spending Diary* assist you when identifying and achieving financial goals?

A *Daily Spending Diary* sheet is located here (below), and on the library resource site within *Connect*.

Daily Spending Diary

Do you buy a latte or a soft drink 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* sheet (following Chapter 1 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.

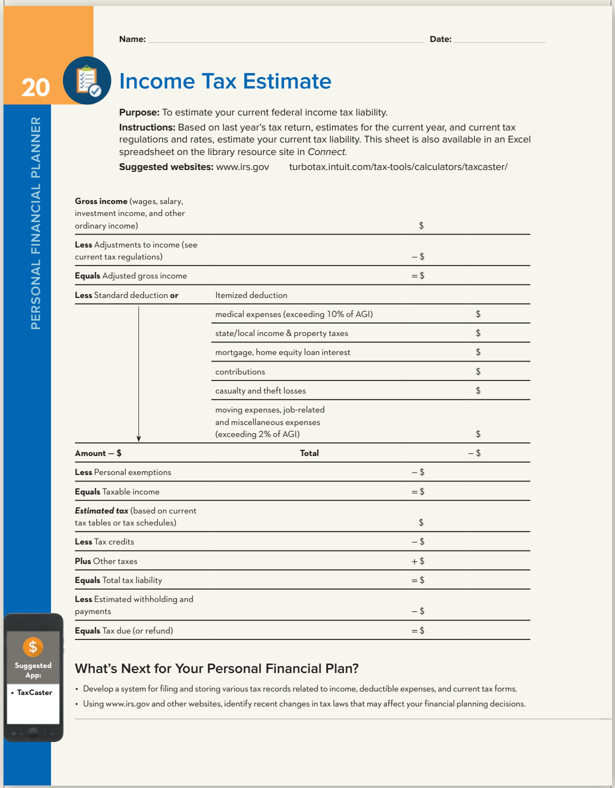
Personal Finance continues to provide instructors and students with features and materials to create a learning environment that can be adapted to any educational setting.

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 roadmap 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 future decisions. The authors also 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

20

Name: Date:

Income Tax Estimate

Purpose: To estimate your current federal income tax liability.

Instructions: Based on last year's tax return, estimates for the current year, and current tax regulations and rates, estimate your current tax liability. This sheet is also available in an Excel spreadsheet on the library resource site in *Connect*.

Suggested websites: www.irs.gov turbotax.intuit.com/tax-tools/calculators/taxcaster/

Gross income (wages, salary, investment income, and other ordinary income)		$	
Less Adjustments to income (see current tax regulations)		– $	
Equals Adjusted gross income		= $	
Less Standard deduction **or**	Itemized deduction		
	medical expenses (exceeding 10% of AGI)		$
	state/local income & property taxes		$
	mortgage, home equity loan interest		$
	contributions		$
	casualty and theft losses		$
	moving expenses, job-related and miscellaneous expenses (exceeding 2% of AGI)		$
Amount – $	**Total**		– $
Less Personal exemptions		– $	
Equals Taxable income		= $	
Estimated tax (based on current tax tables or tax schedules)		$	
Less Tax credits		– $	
Plus Other taxes		+ $	
Equals Total tax liability		= $	
Less Estimated withholding and payments		– $	
Equals Tax due (or refund)		= $	

Suggested App:
- TaxCaster

What's Next for Your Personal Financial Plan?

- Develop a system for filing and storing various tax records related to income, deductible expenses, and current tax forms.
- Using www.irs.gov and other websites, identify recent changes in tax laws that may affect your financial planning decisions.

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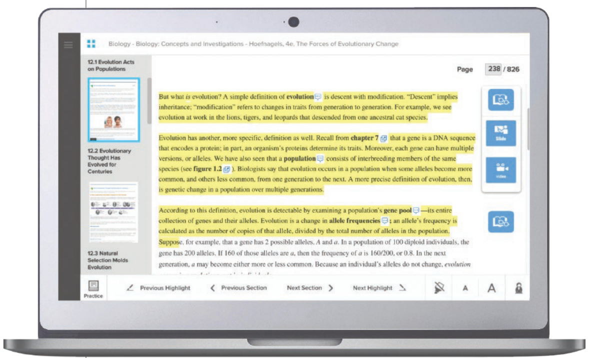

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>
> - Jordan Cunningham,
> Eastern Washington University

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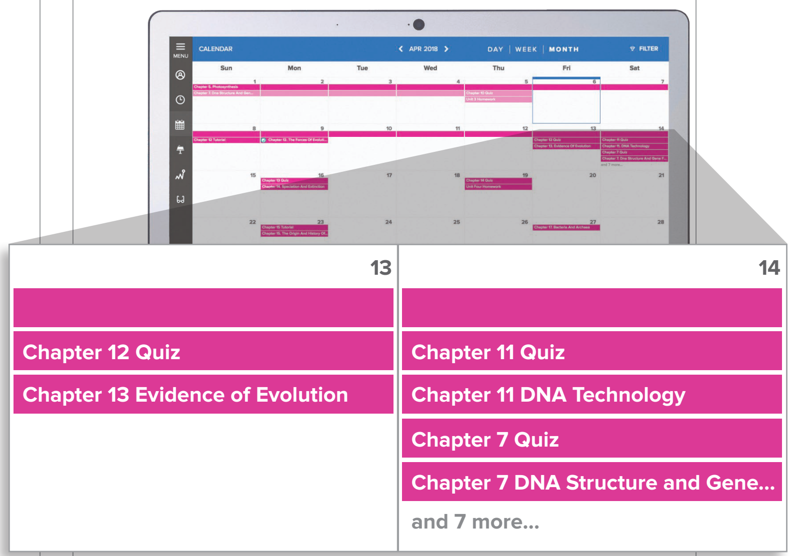

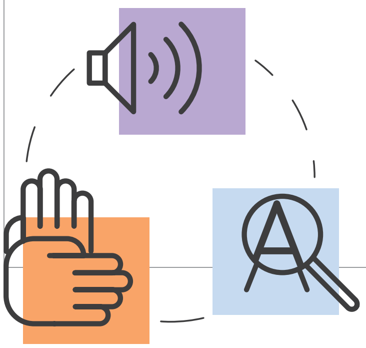

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Contents

Personal Finance Basics and the Time Value of Money

1

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LEARNING OBJECTIVES

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 to analyze personal financial decisions.

LO1-5 Identify strategies for achieving personal financial goals for different life situations.

The Chapter 1 Appendix provides expanded discussion of time value of money calculations and applications.

APPENDIX

Financial Literacy IN YOUR LIFE

What if you . . . needed funds for major auto repairs? Or encountered unexpected medical bills? An *emergency fund* is one of the foundations for effective personal financial planning. What actions would you take?

You might . . . reduce current spending or seek to earn additional income to start or grow your emergency fund. Most important is to set aside some money, even a small amount, for financial uncertainty. This action is a first step toward financial security. Next, you should learn to avoid common money mistakes. Your knowledge and actions will allow you to use wise financial strategies for achieving your personal goals.

Now, what would you do? What actions are you currently taking to create or expand your emergency fund? You will be able to monitor your progress using the "Your Personal Finance Roadmap and Dashboard" feature at the end of the chapter.

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 tangles. 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.

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 obtain financial wealth 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. Many have discovered that the quality of their lives should be measured in terms of something other than money and material items. An emphasis on family, friends, and serving others is often a priority.

Most people want to handle their finances to get full satisfaction from each available dollar. To achieve this and other financial goals, you 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. Since every person, family, or household has a unique financial position, every financial activity must be carefully planned to meet specific needs and goals.

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

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

- Increased effectiveness in obtaining, using, and protecting your financial resources throughout your life.
- Increased control of your financial activities by avoiding excessive debt, bankruptcy, and dependence on others for economic security.
- Improved personal relationships resulting from well-planned and effectively communicated financial decisions.
- Enhanced 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. Many of these choices are quite simple, with minimum consequences. However, some are complex and have long-term effects on our personal and financial situations. Personal financial activities involve three main decision areas:

1. Spending	**2.** Saving	**3.** Sharing
• for daily living expenses • for major expenditures • for recreational activities	• for emergencies • for long-term financial security	• for local and global programs to assist others in need

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.

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 your 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 - Determine Current Situation

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?

EXHIBIT 1-1

The financial planning process

STEP 2: DEVELOP 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 effective savings and investment program for your future financial security.

EXAMPLE: Step 2 - Develop Financial Goals

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.

STEP 3: IDENTIFY ALTERNATIVE COURSES OF ACTION

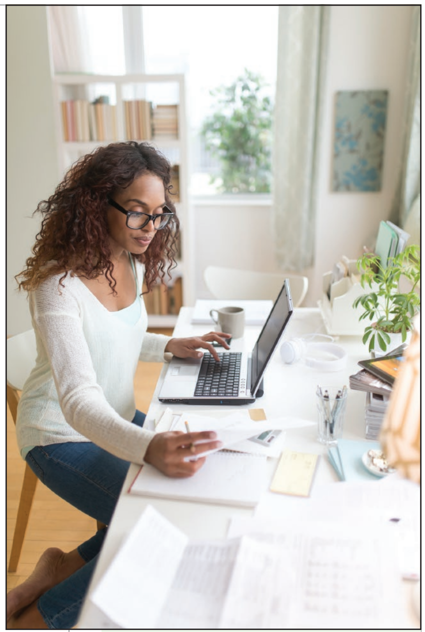
Developing alternatives is crucial when making decisions. Although many factors can influence your alternatives, common courses of action include:

- *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 alternatives 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."

Creative decision-making is vital for effective choices. By considering many alternatives, you will likely 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-car ownership, or use of a ride-sharing program.

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



Financial choices require periodic evaluation.
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EXAMPLE: Step 3 - Identify Alternatives

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 alternatives for achieving the financial goals you identified in the previous step.

STEP 4: EVALUATE YOUR ALTERNATIVES

Next, 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?

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

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 a *trade-off*, 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 comparison shopping for a major purchase. In either case, the resources you give up (money or time) have a value that is lost.

smart money minute

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

Decision-making will be an ongoing part of your life. 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 resources available when making personal financial decisions.

EXAMPLE: Step 4 - Evaluate Alternatives

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 personal financial activities?

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.

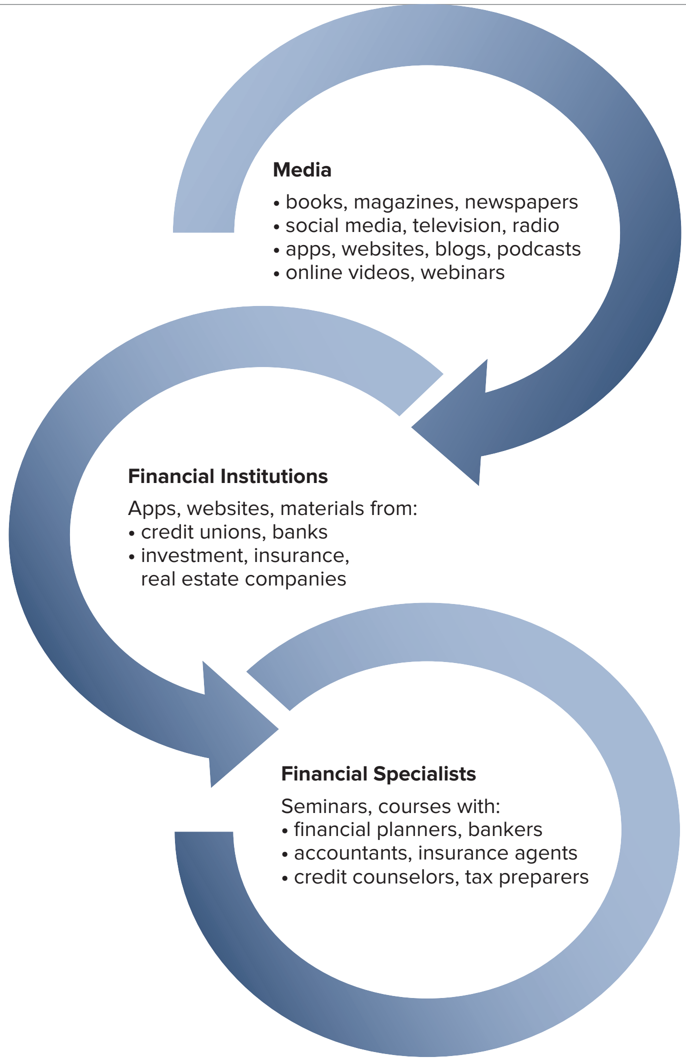
Income Risk
- The loss of a job may result from changes in consumer spending or expanded use of technology.
- Individuals who face the risk of unemployment need to save while employed or acquire skills they can use to obtain a different type of work.

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 the 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



For additional guidance when using financial planning information sources, see the Chapter 3 Appendix.

STEP 5: CREATE AND IMPLEMENT YOUR FINANCIAL ACTION PLAN

The next step of the financial planning process involves developing an action plan to identify methods to achieve your goals. For example, you can increase your savings by reducing spending or by increasing income through extra hours at work. 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 invest in tax-exempt securities. As you achieve your short-term and 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 an online investment account to purchase stocks, bonds, or mutual funds.

my life 1

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

Always consider several information sources when making financial decisions. In addition to apps and online sources, talk to friends, relatives, and financial planning specialists for banking, insurance, tax, and investment guidance.

EXAMPLE: Step 5 - Implement Financial Action Plan

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.

smart money minute

Personal FinTech Technology impacts every aspect of life, including financial decisions. *FinTech* involves apps, software, and computers for banking services and financial activities. Artificial intelligence, robotics, the Internet of Things, drones, 3-D printing, blockchain, wearable technology, and other innovations will influence how you earn, save, spend, and invest. Robo-advisors, for example, offer personalized, online advice based on your income, assets, debt, financial goals, and risk tolerance.

STEP 6: REVIEW AND REVISE YOUR PLAN

Financial planning is a dynamic process that does not end when you take 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.

EXAMPLE: Step 6 - Review and Revise the Plan

Over the next 6 to 12 months, Kent Mullins should reassess his financial, career, and personal situations. What employment opportunities or family circumstances might affect his need or desire to take a different course of action?

How about you? Depending on your current (or future) life situation, what factors in your life might affect your personal financial situation and decisions in the future?

PFP Sheet 1 Personal data

PFP Sheet 2 Financial institutions and advisors

PRACTICE QUIZ 1-1

1. What are the main elements of every decision we make?
2. What are some risks associated with financial decisions?
3. What are common sources of financial planning information?
4. Why should you reevaluate your actions after making a personal financial decision?

Influences on Personal Financial Planning

LO1-2

Assess personal and economic factors that influence personal financial planning.

Many factors influence daily financial decisions, ranging from age and household size to interest rates and inflation. Three main elements affect financial planning activities: life situation, personal values, and economic factors.

LIFE SITUATION AND PERSONAL VALUES

People in their 20s spend money differently than those in their 50s. Personal factors such as age, income, household size, and personal beliefs influence spending and saving patterns. Life situation or lifestyle is created by a combination of factors.

As society changes, different types of financial needs evolve. Today people tend to get married at a later age, and more households have two incomes. Many households are headed by single parents. More than 2 million women provide care for both dependent children and parents. People are also living longer; over 80 percent of Americans now living are expected to live past age 65.

The **adult life cycle**—the stages in the family and financial needs of an adult—is an important influence on your financial activities and decisions. Your life situation is also affected by marital status, household size, and employment, as well as events such as

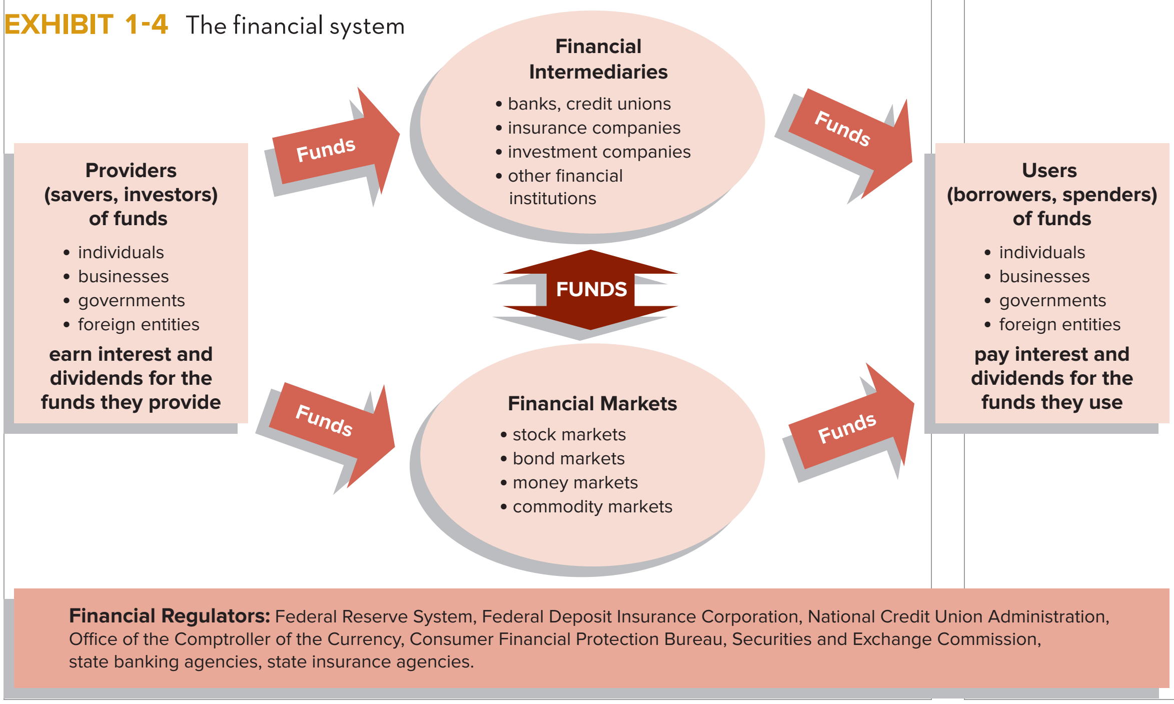
- Graduation (at different levels of education).
- Engagement and marriage.
- The birth or adoption of a child.
- A career change or a move to a new area.
- Dependent children leaving home.
- Changes in health.
- Divorce.
- Retirement.
- The death of a spouse, family member, or other dependent.

In addition to being defined by your family situation, you are defined by your **values**—the ideas and principles that you consider correct, desirable, and important. Values have a direct influence on such decisions as spending now versus saving for the future, or continuing school versus getting a job.

THE FINANCIAL SYSTEM AND ECONOMIC FACTORS

The financial system and daily economic activities influence personal financial decisions. As shown in Exhibit 1-4, money in an economy flows from providers of funds to users of funds through intermediaries and financial markets. The buying and selling of investments occur in these financial settings.

EXHIBIT 1-4 The financial system



my life 2

My family and household situation is likely to stay fairly stable over the next year or two.

Many personal, social, and economic factors can affect your life situation. Refer to Exhibit 1-6 for further information on financial goals and personal finance activities for various life situations.

adult life cycle The stages in the family situation and financial needs of an adult.

values Ideas and principles that a person considers correct, desirable, and important.

While some investments are physical items (houses, land, gold, rare coins), others represent borrowing or ownership. A *security* is a financial instrument that represents debt or equity. *Debt securities,* such as bonds, represent money borrowed by companies or governments. These debt securities are often bought as an investment. In contrast, *equity securities* (stock) represent ownership in a corporation. Shares of stock are also bought by investors. In addition to stocks and bonds, other examples of securities include mutual funds, certificates of deposit (CDs), and commodity futures.

economics The study of how wealth is created and distributed.

In most societies, the forces of supply and demand set prices for securities, goods, and services. **Economics** is the study of how wealth is created and distributed. The economic environment includes various institutions, such as businesses, labor, and government, that work together to satisfy needs and wants.

Various government agencies regulate financial activities (see Exhibit 1-4). The Federal Reserve System, the central bank of the United States, has significant economic responsibility. *The Fed,* as it is often called, maintains an adequate money supply. This is achieved by influencing borrowing, interest rates, and the buying or selling of government securities. The Fed attempts to make adequate funds available for consumer spending and business expansion while keeping interest rates and consumer prices at an appropriate level.

GLOBAL INFLUENCES The global economy also influences personal finance. An economy is affected by both the financial activities of foreign investors and competition from global companies. American businesses compete against foreign companies for the spending dollars of American consumers.

When the value of exports of U.S.-made goods is lower than the value of imported goods, more U.S. dollars leave the country than the dollar value of foreign currency coming into the United States. This reduces the funds available for domestic spending and investment. Also, if foreign companies decide not to invest their dollars in the United States, the domestic money supply is reduced. This reduced money supply can result in higher interest rates. A *trade deficit* also affects the value of a nation's money and the cost of items being purchased by consumers.

ECONOMIC CONDITIONS The economic conditions (see Exhibit 1-5) that most often influence personal financial decisions are consumer prices, consumer spending, and interest rates.

inflation A rise in the general level of prices.

1. Consumer Prices **Inflation** is a rise in the general level of prices. In times of inflation, the buying power of the dollar decreases. For example, if prices increased 5 percent during the last year, items that cost $100 one year ago would now cost $105. This means it now takes more money to buy the same amount of goods and services.

The main cause of inflation is an increase in demand without a comparable increase in supply. For example, if people have more money to spend because of pay increases or borrowing but the same amounts of goods and services are available, the increased demand can bid up prices for those goods and services.

Inflation is most harmful to people living on fixed incomes. Due to inflation, retired people and others whose incomes do not change are able to afford fewer goods and services.

Inflation can also adversely affect lenders of money. Unless an adequate interest rate is charged, amounts repaid by borrowers in times of inflation have less buying power than the money they borrowed. If you pay 4 percent interest on a loan and the inflation rate is 6 percent, the dollars you pay the lender have lost buying power. For this reason, interest rates rise in periods of high inflation.

The rate of inflation varies. During the late 1950s and early 1960s, the annual inflation rate was in the 1 to 3 percent range. During the late 1970s and early 1980s, the cost of living increased 10 to 12 percent annually. At a 12 percent annual inflation rate, prices double (and the value of the dollar is cut in half) in about six years. To find out how fast prices (or your savings) will double, use the *rule of 72:* Just divide 72 by the annual inflation (or interest) rate.

EXHIBIT 1-5 Changing economic conditions and financial decisions

Economic Factor	What It Measures	How It Influences Financial Planning
Consumer prices	The buying power of a dollar; inflation.	If consumer prices increase faster than income, you are not able to purchase the same amount of goods and services; higher consumer prices often cause higher interest rates.
Consumer spending	The demand for goods and services by individuals and households.	Increased consumer spending usually creates more jobs and higher wages; high levels of consumer spending and borrowing may push up consumer prices and interest rates.
Interest rates	The cost of money; the cost of credit when you borrow; the return on your money when you save or invest.	Higher interest rates make buying on credit more expensive; higher interest rates make saving and investing more attractive and may discourage borrowing.
Money supply	The dollars available for spending in our economy.	Interest rates tend to decline as more people save and invest; but higher saving (and lower spending) may also reduce job opportunities.
Unemployment	The number of people without employment who are willing and able to work.	Unemployed people should reduce their debt level and have an emergency fund; high unemployment reduces consumer spending and job opportunities.
Housing starts	The number of new homes being built.	Increased home building creates jobs, higher wages, more consumer spending, and overall economic expansion.
Gross domestic product (GDP)	The total value of goods and services produced within a country's borders, including items produced with foreign resources.	GDP is an indication of a nation's economic viability, resulting in jobs and opportunities for increased personal wealth.
Trade balance	The difference between a country's exports and its imports.	If a country has more exports than imports, the balance of trade deficit can result in price changes for foreign goods.
Dow Jones Average, S&P 500, other stock market indexes	The relative value of stocks represented by the index.	These indexes provide an indication of the general movement of stock prices.

EXAMPLE: Rule of 72

An annual inflation rate of 4 percent, for example, means prices will double in 18 years ($72 \div 4 = 18$). Regarding savings, if you earn 6 percent, your money will double in 12 years ($72 \div 6 = 12$).

More recently, the annual price increase for most goods and services as measured by the consumer price index has been less than 2 percent. The *consumer price index (CPI),* published by the Bureau of Labor Statistics, is a measure of the average change in the prices urban consumers pay for a fixed "basket" of goods and services. For current CPI information, go to www.bls.gov.

Inflation rates can be deceptive. Most people face *hidden* inflation since the cost of necessities (food, gas, health care), on which they spend most of their money, may rise

HOW TO . . . Set a Path to Financial Security

Do you feel stress when you think about money? Are your financial decisions influenced by emotions rather than valid information? Do you often have disagreements about money?

To address these and other financial concerns, two paths exist for your daily money decisions. The *easy* path involves little thinking, no planning, and minimal effort, usually resulting in wasted money and financial difficulties. In contrast, the *appropriate* path takes some time and effort, but results in lower stress and personal financial security.

It is EASY to…		*…but APPROPRIATE to…*
…spend without planning.	→	…save for emergencies and the future.
…overuse credit cards.	→	…maintain a low level of debt.
…avoid insurance coverage.	→	…have a risk management plan.
…select investments carelessly.	→	…research to avoid investment scams.
…make decisions on your own.	→	…communicate with others.

You can start to move yourself from *easy mistakes* to *appropriate actions* with these steps:

1. ***Do something.*** Start small, such as saving a small amount each month. Or, reduce your credit card use.
2. ***Avoid excuses.*** Do not tell yourself that "I don't have time" or "It's what everyone else is doing."
3. ***Rate your current situation.*** Indicate on this scale where you are currently in relation to the two available paths:

   Spender — Saver

   Financial difficulties — Financial security

4. ***Set your mission.*** Create a *personal finance mission statement* to communicate your personal values, financial goals, and future vision. This paragraph (or list or drawing or other format) will remind you and family members of your desired path for financial security. The wording describes where you want to be and how you will get there. Develop your financial mission statement by talking with those who can help guide your actions. Your personal finance mission statement may include phrases such as "My financial mission is to change my spending habits for . . . ," ". . . to better understand my insurance needs," or ". . . to donate (or volunteer) to local community service organizations."

Choosing to take the appropriate actions can result in reduced emotional stress, improved personal relationships, and increased financial security.

at a higher rate than the cost of nonessential items. This results in a *personal* inflation rate that is higher than the government's CPI.

Deflation, a decline in prices, can also have damaging economic effects. As prices drop, consumers expect they will go even lower. As a result, they cut their spending, which causes damaging economic conditions. While widespread deflation is unlikely, certain items may be affected, and their prices will drop.

2. Consumer Spending Total demand for goods and services in the economy influences employment opportunities and the potential for income. As consumer purchasing increases, the financial resources of current and prospective employees expand. This situation improves the financial condition of many households.

In contrast, reduced spending causes unemployment, since staff reduction commonly results from a company's reduced financial resources. The financial hardships of unemployment are a major concern of labor, business, and government. Retraining programs, income assistance, and job services can help people adjust.

3. Interest Rates In simple terms, interest rates represent the cost of money. Like everything else, money has a price. The forces of supply and demand influence interest rates. When consumer saving and investing increase the supply of money, interest rates tend to decrease. However, as consumer, business, government, and foreign borrowing increase the demand for money, interest rates tend to rise.

Interest rates affect financial planning. The earnings you receive as a saver or an investor reflect current interest rates as well as a *risk premium* based on such factors as the length of time your funds will be used by others, expected inflation, and the uncertainty about getting your money back. Risk is also a factor in the interest rate you pay as a borrower. People with poor credit ratings pay a higher interest rate than people with good credit ratings. Interest rates influence many financial decisions. Current interest rate data may be obtained at www.federalreserve.gov.

PRACTICE QUIZ 1-2

1. How do age, marital status, household size, employment situation, and other personal factors affect financial planning?
2. How might the uncertainty of inflation make personal financial planning difficult?
3. What factors influence the level of interest rates?

PFP Sheet 4
Current economic conditions

Developing Personal Financial Goals

LO1-3

Develop personal financial goals.

Because the United States is one of the richest countries in the world, it is difficult to understand why so many Americans have money problems. The answer is the result of poor planning and weak money management habits related to spending and the use of credit. Achieving personal financial satisfaction starts with clear financial goals.

TYPES OF FINANCIAL GOALS

Two factors commonly influence your financial aspirations for the future. The first is the time frame in which you would like to achieve your goals. The second is the financial need that drives your goals.

TIMING OF GOALS What would you like to do tomorrow? Believe it or not, that question involves goal setting, which may be viewed in three time frames.

1. *Short-term goals,* such as saving for a vacation or paying off small debts, will be achieved within the next year.
2. *Intermediate goals* have a time frame from one to five years.
3. *Long-term goals* involve financial plans that are more than five years off, such as retirement, money for children's college education, or the purchase of a vacation home.

A variety of personal and financial goals will motivate your actions.
©Mark Scott/Photographer's Choice RF/Getty Images

smart money minute

To become financially disciplined:

- select a word or short phrase to describe your goal.
- use a visual reminder—a photo, sticky note, or note card placed on your desk, computer, bathroom mirror, refrigerator, or car dashboard.
- keep a financial diary or journal.
- obtain support; work with a friend, roommate, spouse, or group to stay accountable.

Financial goals often lack the "why" to help you achieve meaningful results. If you are unable to answer "why," this may indicate a goal that is not appropriate for you. What is the "why" for one of your financial goals?

Long-term goals should be planned in coordination with short-term and intermediate ones. Setting and achieving short-term goals is the basis for achieving long-term goals. For example, saving for a down payment to buy a house is an intermediate goal that can be a foundation for a long-term goal: owning your own home.

Goal frequency is another ingredient in the financial planning process. Some goals, such as vacations or money for gifts, may be set annually. Other goals, such as a college education, a car, or a house, occur less frequently.

GOALS FOR DIFFERENT FINANCIAL NEEDS A goal of obtaining increased career training is different from a goal of saving money to pay a semiannual auto insurance premium. *Consumable-product goals* usually occur on a periodic basis and involve items that are used up relatively quickly, such as food, clothing, and entertainment. Such purchases, if made unwisely, can have a negative effect on your financial situation.

Durable-product goals usually involve infrequently purchased, expensive items such as appliances, cars, and sporting equipment; these consist of tangible items. In contrast, many people overlook *intangible-purchase goals*. These goals may relate to personal relationships, health, education, and leisure. Goal setting for these life circumstances is also necessary for your overall well-being.

GOAL-SETTING GUIDELINES

An old saying goes, "If you don't know where you're going, you might end up somewhere else and not even know it." Goal setting is central to financial decision-making. Your financial goals are the basis for planning, implementing, and measuring the progress of your spending, saving, and investing activities. Exhibit 1-6 offers typical goals and financial activities for various life situations.

Your financial goals should take a S-M-A-R-T approach, in that they are:

my life 3

My specific financial goals for the next year are written down.

Having specific financial goals in writing that you review on a regular basis is the foundation of successful personal financial planning. To start (or continue) creating and achieving your financial goals, use the *Financial Literacy for My Life: Developing Financial Goals* feature.

S—*specific*, so you know exactly what your goals are so you can create a plan designed to achieve those objectives.

M—*measurable* with a specific amount. For example, "Accumulate $5,000 in an investment fund within three years" is more measurable than "Put money into an investment fund."

A—*action-oriented*, providing the basis for the personal financial activities you will undertake. For example, "Reduce credit card debt" will usually mean actions to pay off amounts owed.

R—*realistic*, involving goals based on your income and life situation. For example, it is probably not realistic to expect to buy a new car each year if you are a full-time student.

T—*time-based*, indicating a time frame for achieving the goal, such as three years. This allows you to measure your progress toward your financial goals.

Having financial goals is just the start of your financial planning activities. Creating and implementing a process to move toward these goals must now occur.

EXHIBIT 1-6 Financial goals and activities for various life situations

Foundation Financial Goals and Activities			
• Obtain appropriate career training. • Create an effective financial record-keeping system. • Develop a regular savings and investment program.	• Accumulate an appropriate emergency fund. • Purchase appropriate types and amounts of insurance coverage. • Create and implement a flexible budget.		• Evaluate and select appropriate investments. • Establish and implement a plan for retirement goals. • Make a will and develop an estate plan.
Specialized Financial Goals and Activities for Various Life Situations			
Young, Single (18–35)	**Young Couple with Children under 18**	**Single Parent with Children under 18**	**Young Dual-Income Couple, No Children**
• Establish financial independence. • Obtain disability insurance to replace income during prolonged illness. • Consider home purchase for tax benefit.	• Carefully manage increased need for the use of credit. • Obtain an appropriate amount of life insurance for the care of dependents. • Use a will to name guardian for children.	• Obtain appropriate health, life, and disability insurance. • Contribute to savings and investment fund for college. • Name a guardian for children and make other estate plans.	• Coordinate insurance coverage and other benefits. • Create investment program for changes in life situation (larger house, children). • Consider tax-deferred contributions to retirement fund.
Unmarried Couple, No Children	**Older Couple (50+), No Dependent Children**	**Mixed-Generation Elderly Individuals and Children under 18**	**Older (50+), Single Person, No Dependent Children**
• Plan joint and individual bank and credit accounts. • Communicate budgeting attitude differences. • Discuss and share joint and individual financial goals. • Consider a home purchase with a property agreement.	• Review financial assets and estate plans. • Consider household budget changes several years prior to retirement. • Plan retirement housing, living expenses, recreational activities, and part-time work.	• Obtain long-term care, life, disability insurance coverage. • Use dependent care service. • Provide for handling finances of elderly if they become ill. • Consider splitting investment cost—elderly get income while alive, principal to survivors.	• Make arrangement for long-term health care coverage. • Review will and estate plan. • Plan retirement living facilities, living expenses, and activities. • Monitor investments to consider current financial needs and market conditions.

PRACTICE QUIZ 1-3

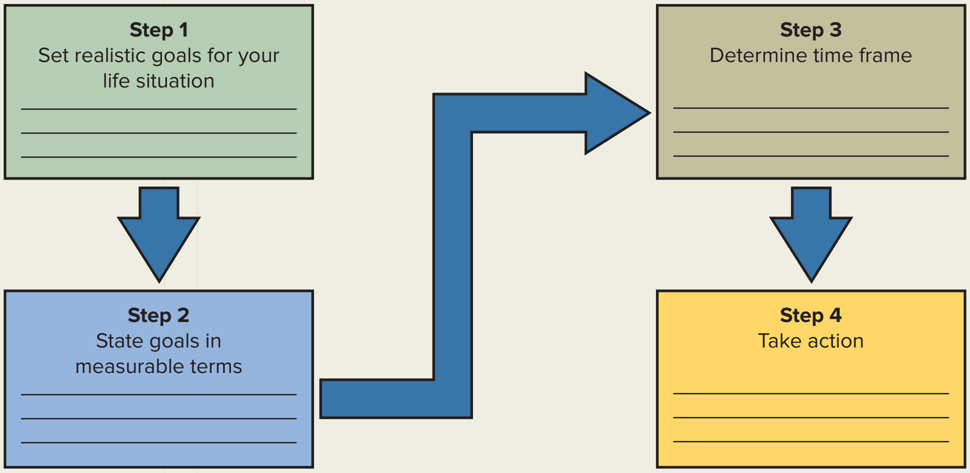
PFP Sheet 3 Personal financial goals

1. What are examples of long-term goals?
2. What are the five main characteristics of useful financial goals?

Financial Literacy for My Life

DEVELOPING FINANCIAL GOALS

Based on your current situation or expectations for the future, create one or more financial goals using these steps:



See ***Personal Financial Planner Sheet 3*** to plan and implement your financial goals.

Opportunity Costs and the Time Value of Money

LO1-4

Calculate time value of money to analyze personal financial decisions.

Have you noticed that you must give up something when you make choices? In every financial decision, you sacrifice something to obtain something else that you consider more desirable. For example, you might reduce current spending to invest funds for future purchases or long-term financial security. Or you might obtain use of an expensive item now by making credit payments from future earnings. These *opportunity costs* may be viewed in terms of both personal and financial resources (see Exhibit 1-7).

EXHIBIT 1-7

Opportunity costs and financial results should be assessed when making financial decisions.