

Budgets and Financial Records

TERMS TO KNOW

disposable
income

financial plan

budget

fixed expenses

variable expenses

assets

liabilities

net worth

contract

consideration

negotiable
instrument

co-signer

warranty

spreadsheet

database

Consider This . . .

Rania has a part-time job, attends school six hours a day, and participates in two after-school sports. She no longer receives a monthly allowance from her parents. She pays for all of her own clothes, gas, insurance, and entertainment. Last year, she was able to save over \$600.

“How do you do it?” asked her friend JoAnn. “I work more hours than you do, my parents pay for my clothes and most of my expenses, and I still don’t have any money left over for entertainment. I didn’t save a dime last year!”

“I have a budget,” said Rania. “Every time I get paid, I put aside money for savings. I know how much I spend on everything I buy. Keeping a good record of income and expenses helps me plan better, so I don’t run out of money. That doesn’t mean I buy anything I want, but it does mean that I know how much I can spend, so I can stretch my money to cover as many things as possible.”

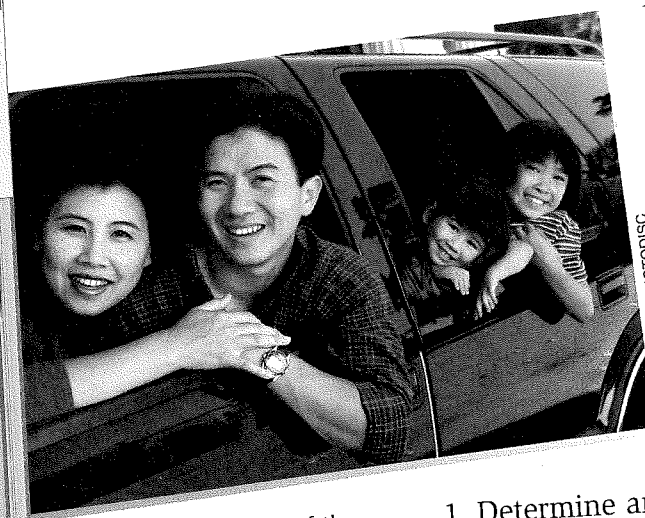
Lesson 8.1

Budgeting and Record Keeping

- Goals**
- Describe and prepare personal budgets.
 - Explain the purpose of record keeping.
 - Prepare a net worth statement and a personal property inventory.

■ IMPORTANCE OF FINANCIAL PLANNING

Do you have unlimited resources to buy all the things you want? Some people do, but if you are like most Americans, to achieve financial success you will have to plan and work for it. Budgeting and maintaining financial records are a significant part of financial planning. They provide the road map to financial security. Budgeting is the first step.



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Disposable income is the money you have left to spend or save after taxes have been paid. In order to use this income to your best advantage, you need a financial plan.

All the money you receive is spent, saved, or invested. You may spend it for things you need or want, save it for future needs, or invest it to earn more money. A **financial plan** is a set of goals for spending, saving, and investing the money you earn. Financial planning helps you:

1. Determine and evaluate options for your money.
2. Prioritize your options so your money goes as far as possible.
3. Avoid careless and wasteful spending.
4. Organize your *financial resources* (sources of income) so you can achieve your financial goals.
5. Avoid money worries by planning your saving, spending, and borrowing to live within your income.

What are some of the benefits of financial planning?

PREPARING A BUDGET

The first step toward achieving your financial goals is to prepare a budget. A **budget** is a spending and saving plan based on your expected income and expenses. In a budget, money coming in (earnings plus borrowing) must equal money going out (spending plus saving). The budget must balance. A budget helps you plan your spending and saving so that you won't have to borrow money to meet your daily needs.

Figure 8-1 shows a high school student's budget for one month. This student expects to receive a total of \$380 and plans to use the money for certain needs and wants and to save part of it as well. Notice that the total income equals the total of expenses plus savings. The budget balances.

Steps in Preparing a Budget

Follow these steps to prepare a budget:

1. Estimate your total expected income for a certain time period. Include all the money you expect to receive. You may wish to use a weekly, biweekly, or monthly budget—whichever best matches how often you expect to receive money.

SIMPLE BUDGET

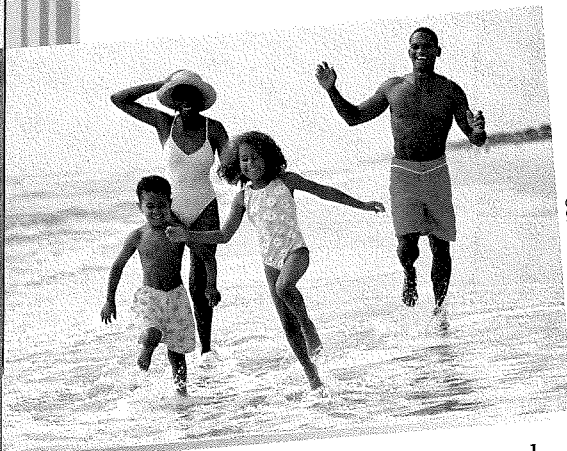
figure 8-1

BUDGET FOR SEPTEMBER	
Income	
Work (part-time)	\$320.00
Allowances for household chores	20.00
Lunch money	40.00
Total income	<u>\$380.00</u>
Expenses	
Daily lunches	\$ 80.00
Supplies	20.00
Snacks	40.00
Entertainment (movies and golfing)	140.00
Total expenses	<u>\$280.00</u>
Savings	
To Columbia County Credit Union	<u>\$100.00</u>
Total expenses plus savings	<u>\$380.00</u>

2. Decide how much of your income you want to save—to set aside for future needs. Most financial experts advise saving at least 10 percent of your disposable income each pay period. By saving at least this amount, you will have money to pay for future needs, both expected and unexpected.
3. Estimate your expenses, or money you will need for day-to-day purchases—for example, lunches, fees, personal care items, and clothing.
4. Balance your budget. If your expenses plus savings exceed your income, adjust your plan to make them match. Avoid spending more than you make. Use of credit limits future spending because you must pay off the loan with future income. To balance your budget, you may have to delay buying some items you want but don't need. Or, you may decide to save a little less this month. If you don't want to do either of these options, you'll have to find a way to bring in more money.

A Typical Monthly Budget

Figure 8-2 shows the monthly budget of Mike and Jennifer Harris. Mike and Jennifer have no children, and both are working. The Harrises estimated their expected income by adding together their two take-home incomes (paychecks), along with anticipated interest on savings and earnings on investments. They would like to save at least 10 percent every month, setting aside money for emergency savings, short-term savings, and long-term investments as shown.



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Would vacation costs be considered fixed or variable expenses? Explain your answer.

Fixed expenses are costs you are obligated to pay at specific times, regardless of other events. You cannot change them without making a major revision in your lifestyle. For example, you must pay your rent or mortgage, utility bills, car loan, and insurance premiums when they are due, no matter what else is going on in your life. Most financial experts recommend that a family have fixed expenses of no more than 50 to 60 percent of take-home pay. However, this standard is difficult to achieve for young people just starting life on their own. But with time, pay raises, and careful budgeting, a family can achieve that goal.

Variable expenses are costs that vary in amount and type, depending on events and the choices you make. For example, your grocery bill can be larger or smaller, depending on what you choose to buy. Other examples of variable expenses are costs for eating out, going to movies, and buying clothes.

**MONTHLY AND YEARLY BUDGET
FOR A MARRIED COUPLE**

figure 8-2

BUDGET — Mike and Jennifer Harris

	Monthly	Yearly
Income		
Salary (Mike) after taxes	\$ 1,600	\$19,200
Salary (Jennifer) after taxes	1,800	21,600
Interest on savings	50	600
Earnings on investments	50	600
Total income	<u>\$ 3,500</u>	<u>\$42,000</u>
Expenses		
Fixed expenses:		
Rent	\$ 1,000	\$12,000
Utilities	150	1,800
Car payment	300	3,600
Insurance:		
Car	100	1,200
Life and Health	75	900
Total fixed expenses	<u>\$ 1,625</u>	<u>\$19,500</u>
Variable expenses:		
Telephone	\$ 45	\$ 540
Gasoline	150	1,800
Car repairs and maintenance	60	720
Cable television	40	480
Groceries	400	4,800
Clothing	200	2,400
Personal care:		
Dry cleaning, household	50	600
Drugs, cosmetics	50	600
Insurance deductibles and co-pays	50	600
Recreation and entertainment	100	1,200
Gifts, donations, miscellaneous	300	3,600
Total variable expenses	<u>\$ 1,445</u>	<u>\$17,340</u>
Total fixed and variable expenses	<u>\$ 3,070</u>	<u>\$36,840</u>
Cash surplus (total income minus total expenses)	<u>\$ 430</u>	<u>\$ 5,160</u>
Allocation of cash surplus:		
Emergency savings fund	\$ 100	\$ 1,200
Short-term savings	100	1,200
Long-term investments	230	2,760
Total savings and investments	<u>\$ 430</u>	<u>\$ 5,160</u>
Total expenses plus savings	<u>\$ 3,500</u>	<u>\$42,000</u>

Net Nuggets

American Consumer Credit Counseling believes that education is the key ingredient to credit counseling and managing debt. Within their online Education Source, the Learning Center includes information on financial planning, money management (including budgeting), consumer issues, and student financial resources. Check out their Web site at www.consumercredit.com.

PERSONAL RECORDS

Good personal record keeping makes budgeting and long-range planning easier. Your records also form the basis for completing income tax returns, credit applications, and other financial forms. You should keep four types of personal records: income and expense records, a net worth statement, a personal property inventory, and tax records. Many people keep financial records on their computer, usually password-protected. As with any important files you keep electronically, always keep a current backup of your financial records.

Records of Income and Expenses

Your W-2 forms show the money earned and deductions taken from your paycheck during the year. The W-2 forms also state the amount of taxes and social security tax withheld. You may need the W-2 forms later when you want to collect benefits. Other records of income include statements from banks showing interest earned on savings and statements from investment companies listing dividends earned from stock or other investments. Expense items include receipts listing charitable contributions, medical bills, or work-related expenses. When you prepare your budgets and tax returns, these receipts and statements serve as documentation (proof) of income and expenses. Store these documents in a safe place for future reference.



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What are the different kinds of financial records you should keep?

Net Worth Statement

A *net worth statement*, such as that shown in Figure 8-3, is a list of items of value that a person owns, called **assets**; amounts of money owed to others, called **liabilities** or debts; and the difference between the two, known as **net worth**. If your assets are greater than your lia-

NET WORTH STATEMENT

Nygen Phomm

January 1, 20--

ASSETS		LIABILITIES	
Checking account	\$ 500	Loan on car	\$1,800
Savings account	800	Loan from mother	100
Car value	3,000	Total liabilities	\$1,900
Personal property: (inventory attached)	5,000		
Total assets	<u>\$9,300</u>		
		NET WORTH	
		Assets minus liabilities	<u>\$7,400</u>
		Total	<u>\$9,300</u>

bilities, you are said to be *solvent*, or in a favorable financial position. But if your liabilities are greater than your assets (you owe more than you own), you are said to be *insolvent*, or in a poor financial position.

You will need your net worth information (lists of assets and liabilities) when you apply for a loan or credit. The bank or other financial institution will want you to be solvent and a good risk—a person who will likely pay back the loan. It also helps you keep track of how you spend your money and what you have to show for it at the end of the year.

Personal Property Inventory

A *personal property inventory*, such as the one shown in Figure 8-4, is a list of all valuable items you own, along with their purchase prices and approximate current values. Personal property includes anything of value inside your home—clothing, furniture, appliances, and so forth. A personal property inventory is useful in the event of fire, theft, or property damage. The inventory will help you list lost items and their value when you make an insurance claim.

As a further safeguard, photograph items of value, attach the photographs to the inventory, and keep this information in a safe deposit box or other secure place to use as evidence in the event the property is damaged, lost, or stolen. A personal property inventory also helps you see what you have to show for the money you have spent. Reviewing it will help you assess your spending patterns. As you buy new items and dispose of others, revise the inventory.



PERSONAL PROPERTY INVENTORY			
Nygen Phomn			
January 2, 20--			
Item	Year Purchased	Purchase Price	Approximate Current Value
Sphinx XTL DVD Player with big-screen TV	2003	\$3,200	\$1,300
Bedroom furniture (bed, dresser, lamp, clock)	2001	2,000	1,200
Clothing, jewelry	----	3,000	500
MBD motor bike	2000	1,800	1,000
CD collection, digital camera, scanner, CD burner	2001	<u>2,000</u>	<u>1,000</u>
		<u>\$12,000</u>	<u>\$5,000</u>

Tax Records

All taxpayers should keep copies of their tax records for at least three years after they file their tax return. Tax records include the return form, W-2 forms, and other receipts verifying income and expenses listed on each return. Keep your tax records in a safe place in case of an audit. The IRS has the legal right to audit your tax returns and supporting records for three years from the date of filing (longer if fraud or intentional wrongdoing on your part can be proved).

✓ Check Your Understanding

1. What is the first step in budgeting?
2. How are fixed expenses different from variable expenses?
3. Why would you prepare a net worth statement?

11. An unconditional written promise to pay a specified sum of money upon demand of the holder.
12. A computer program that organizes data in columns and rows and can perform calculations using the data.
13. A computer program that organizes data for easy search and retrieval.
14. Money you have left to spend or save after taxes have been paid.
15. The difference between assets and liabilities.

REVIEW FACTS AND IDEAS

1. Why should you prepare a budget?
2. What are the four steps in preparing a budget?
3. What choices do you have if your initial budget doesn't balance?
4. If you had to reduce your spending to balance your budget, which would you try to reduce first: fixed or variable expenses? Why?
5. What four types of personal records should you prepare and keep in a safe place?
6. Besides for obtaining credit, what is another good reason for preparing a personal property inventory?
7. How is an implied contract different from an express contract?
8. Give three examples of contracts that must be in writing in order to be enforceable.
9. In order to be legally enforceable, contracts must contain what four elements?
10. List five consumer responsibilities when entering into a contract.
11. What is the most commonly used form of negotiable instrument?
12. Explain the concept of a filing system for personal records and list several file labels you would choose.

Solve Problems ⊕ Explore Issues

1. Based on the following information, prepare a monthly and yearly budget for Antwan and Keyondra Harbour. Use Figure 8-2 as a model.

Average Income

Net paychecks total \$1,800 monthly
Interest on savings = \$50 monthly

Average Monthly Expenses

Rent payment	\$400
Utilities	120
Gasoline	100
Insurance	150
Groceries	200
Clothing	100
Car payment	210
Car maintenance	50
Telephone	40
Entertainment and Recreation	200

Cash Surplus

Savings	To be Determined
Investment fund	60
Miscellaneous	120

2. Based on the following information, prepare a monthly and yearly budget for Elena Espinoza. Follow the style shown in Figure 8-2.

Average Income

Net monthly pay is \$1,400

Average Monthly Expenses

Rent	\$410
Insurance	60
Utilities	50
Gasoline	60
Clothing	60
Entertainment	100
Savings	120
Telephone	15
Car payment	150
Car repairs	20
Groceries	150
Personal care	50
Miscellaneous	155

3. Revise Elena's budget when she agrees to share her apartment with a friend. Some expenses can be shared equally. Assume the telephone expense increases to \$30, utilities to \$60, and insurance to \$70. These expenses along with rent are shared equally. What will you have her do with the added funds?
4. Based on the following information, prepare a net worth statement for Sako Masuta. Follow Figure 8-3. Sako owns a car worth about \$3,000 but owes \$1,500 on it to the bank. He has \$500 in savings and \$100 in checking. His personal property totals \$3,000, and he also owes \$90 to his credit union.
5. Sako has 5 payments left to pay off the remaining \$1,500 of his car loan. He is paying 8 percent interest. Locate a loan planner tool and determine his monthly payments.
6. Based on the following information, prepare a personal property inventory for Sako Masuta. Follow Figure 8-4.

Sako has these furnishings in his apartment:

- JWA CD stereo system, Model 252, SN 975923, bought last year for \$600, presently worth \$500
- Sofa, presently worth about \$800
- Bright alarm clock, SN 630AM and Blare radio, Model 2602, SN 413T, bought four years ago, total worth about \$100.

Sako also has the following personal items:

- Miscellaneous clothing and jewelry, presently worth about \$800
- Quantex wristwatch, presently worth about \$100
- Coin collection, valued last year at \$600.

Sako has photographs of these items. (List a hypothetical purchase price for all items except the CD system in preparing your property inventory.)

For related activities and links, point your browser to www.mypf.swlearning.com

