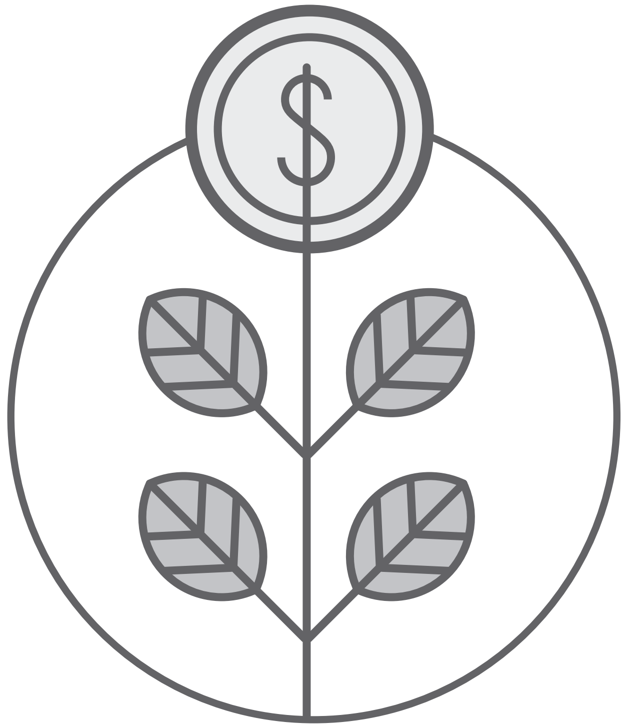
UNIT 3 | Making a Financial/Investment Plan

TEACHING STANDARDS/KEY TERMS



- 401(k) plan
- 403(b) plan
- Annuity
- Assets
- Asset allocation
- Compound interest
- Central Registration Depository (CRD)/BrokerCheck
- Decision making
- Defined benefit/defined contribution plans
- Diversification
- Expenses
- Financial adviser
- Financial plan
- Goal
- Incentive
- Income
- Investment plan
- IRAs
- Liability
- Matching contribution
- Net worth statement
- Roth IRA

Unit Objectives:

INDIVIDUALS WILL:

- Learn the benefits of financial planning.
- Consider factors that go into financial planning and investment decisions.
- Design a personal financial/investment plan.
- Consider how to select a stockbroker or investment adviser.

Unit Teaching Aids:

LESSON 1:
- Myth Vs. Reality: Financial/Investment Planning (Handout/Overhead)
- Financial Planning Phase 1 – Financial Goals

LESSON 2:
- Financial Planning Process (Handout/Overhead)
- Financial Planning Phase 2 – Net Worth Statement
- Personal Net Worth Statement (Worksheet)
- Financial Planning Phase 3 – Income and Expense Statement
- If Expenses Exceed Income (Handout/Overhead)
- If Income Exceeds Expenses (Handout/Overhead)
- Income and Expense Statement (Worksheet)
- Financial Case Study (Handout/Worksheet)
- Employer-Sponsored Retirement Plans (Worksheets)

UNIT TEST:
- *(Test and Answer Key)*

For Instructors

Why Teach This Unit?

Americans now face more financial decisions at an earlier age than previous generations. Young people today will face decisions while still in their twenties about employer-based retirement savings plans. Some young people make the mistake of not participating in such plans. As a result, they lose out on the matching funds offered by employers, the advantages of saving on taxes, and the time value of money. Some who do take advantage of savings plans at work may not be aware of the importance of asset allocation, a strategy for selecting various investment vehicles to spread risk among stocks, bonds and cash reserves, such as money market funds and certificates of deposit. The decisions young people make about employer-based retirement plans early in their careers can have a tremendous impact on their future financial security and retirement. Older investors may simply fail to deal with saving for retirement or find the entire topic too confusing. This is a classic case of “failing to plan is planning to fail.”

Individuals who plan their finances are likely to have more positive choices to make in later life. Financial planning is all about taking charge of one’s circumstances. For most people, it takes more than luck to get what they want out of life — they have to know what they want and then commit to a plan to meet their goals. People sometimes miss out on becoming financially independent in early and later life because they fail to plan. They may not know what action to take or they may simply procrastinate … without knowing the long-term costs of such delays.

LESSON 1: Introduction to Financial Planning/Investing Concepts

Individuals can successfully manage their money if they have the know-how and the will to set aside some of today's income for the things they will want and need in the future. A financial/investment plan is a personal blueprint that helps a person:

- Live within their means (income).
- Identify financial priorities.
- Allocate funds to meet expenses.
- Meet financial emergencies.
- Reduce uncertainty and conflict about financial affairs.
- Achieve a sense of financial independence and control.
- Save and invest to reach financial goals.

A financial plan is a tool to get what one wants out of life. Encourage your class to think of a financial plan as a road map. A road map helps plan a trip to an unfamiliar destination. It is a necessary tool travelers need to arrive successfully at the right destination. Many people are unfamiliar with how to arrive at financial security … with the road map of a financial/investment plan they can figure out how to get to their destination.

A financial plan works best if it is simple, uses realistic income and expense estimates, is reviewed annually (or even more frequently), and adjusted to reflect changing conditions and goals. A common mistake people make is to prepare a financial plan and then fail to follow it or adjust it when necessary.

Throughout the entire financial planning process, individuals will make decisions about how to distribute their income to meet their most important expenses. These decisions will be influenced by many factors, including personal values, goals, wants, and needs.

Individuals will need to ask themselves the following questions to begin the process of framing a financial plan:

- What are my short-term, medium-term, and long-term goals?
- What is my total income after taxes and deductions?
- What are my current living expenses?
- What changes in living expenses do I expect?
- How much can I realistically save and invest each month for future goals such as college expenses or a down payment on a house or car?
- How can I protect against inflation?
- How can I develop a plan for retirement?

LESSON 2: Framing a Plan to Meet Individual Financial/Investment Goals

There are four key phases in the financial planning process:

1 **Identify financial goals.**

2 **Determine net worth.**

3 **Estimate and balance income and expenses.**

4 **Implement and modify the financial plan:**

A. Review personal debt situation.

B. Allocate savings and investments to reach goals.

C. Modify as needed.

PHASE 1: Financial Goals

The first phase in designing a financial/investment plan is to identify individual **goals.** Saving and investing is easier with specific goals in mind. Goals can be divided among different categories, including short-term, medium-term, and long-term **needs** and **wants**:

- **Needs** are short-, medium-, or long-term goals that must be met. Examples are paying off a credit card, paying for a college education, and saving for retirement.
- **Wants** are short-, medium-, or long-term goals that are not absolutely necessary. Examples are saving to buy a new TV or for a special vacation, and even saving for a down payment on a house.

It is extremely important to set a manageable number of goals that are attainable rather than an overwhelming number of goals that are also unrealistic. The first step in Phase 1 is to make a list of all goals and then prioritize them according to importance and the time it will take to reach them:

- **Short-term goals** are those to be reached within a year. Examples of short-term financial goals may include building an emergency fund, saving to buy a new smartphone or TV, paying off a credit card, or establishing a holiday gift fund.
- **Medium-term goals** may be in the one- to five-year range, such as saving and investing for a first home, college expenses, and starting a family.
- **Long-term goals** are those that may not be reached for five-10 or more years. Examples of typical long-term goals are financing a new business and investing for a comfortable retirement.

After identifying personal goals, the next steps are to determine the cost of these goals.

- Set a date for completing each goal.
- Estimate how much will have to be saved and/or invested each month to reach each goal.

PHASE 2: Net Worth Statement

Individuals now know what they want to achieve with a financial/investment plan, so it is time to determine where each of them actually stands. To do this, individuals will prepare a net worth statement (and be prepared to modify it annually). A net worth statement — or personal balance sheet — is a comparison of what each of us owns (assets) and owes (liabilities) at a specific time. It is like a snapshot of an individual's or household's financial condition at a certain point in time. Follow these steps to determine personal net worth:

- List the market or resale value of all assets.
- List all liabilities or money owed to others.
- Determine total assets and total liabilities.
- Subtract total liabilities from total assets.
- Determine if there is a positive or negative net worth.

Many young adults will have a low or negative net worth as they incur debt for schooling and other large expenses. The most recent U.S. Census data (from 2011) found that 18 percent of households have a zero or negative net worth, while 26 percent of households have a net worth of a quarter million dollars or more. Like income, wealth tends to rise with educational level and is higher for homeowners and married couples.

PHASE 3: Income and Expense Statement

An income and expense statement, sometimes called a cash flow statement, lists and categorizes the money an individual receives and spends. It is a financial planning tool that helps individuals determine the following aspects of their financial picture:

- The amount of money to be set aside for future goals.
- The extent of personal debt.
- The amount of interest being paid.
- How to pay off debt faster while still saving and investing for future goals.

The income and expense statement is usually prepared on a bi-weekly or monthly basis. The statement comprises an income component and an expense component. Income is payment received as a result of investments, interest, or work.

Have your class take the following step to create the income component of this statement: Record all money that they expect to receive during the coming year. Begin with regular income, such as wages, interest, and dividends, and then add any other money that may come in. List the amounts and total them to determine how much money will be received.

An expense is an outflow of money. Because saving money is simply withholding it from current spending, it is considered an expense. The following step will create the expense component of this statement: Use old records, receipts, bills, and canceled checks to estimate future expenses. It is helpful to keep records for two or three months to see where money is being spent. Periodic expenses such as car insurance can be broken down into monthly amounts in the budget. List the expenses and determine how much money was spent during the previous 1 – 3 months.

After the students have completed the income and expense statement, ask them to consider areas that can be cut back and areas that should be increased. There are several options to consider if the income or the expenses exceed each other. For example, if the income is greater than the expenses, increasing savings and investments may be an option. However, if the expenses are greater than income, it is wise to postpone some purchases, cut expenses, or identify additional sources of income.

Consider the following if expenses exceed income:

- What expenses can be reduced?
- Which expenditures can be postponed?
- How can income be increased?

Consider the following if your income exceeds expenses:

- Increase savings or investing for goals. (This should be your top priority.)
- Satisfy more immediate wants.
- Increase giving to worthy causes.

The challenge here is to balance income and expenses to live comfortably now while saving for future goals. In the long run, people who live within their income are more likely to enjoy the freedom that comes with being financially independent.

PHASE 4: Implement and Modify the Plan

The final phase in developing a personal financial/investment plan is to implement and modify the plan. This includes several steps:

1. **Review Personal Debt Situation:** Credit allows individuals to have and enjoy things now and pay for them later. It is convenient and can be a cushion in emergencies. But credit costs money (this is especially true for young people who have no track record of repayment of debt) and can encourage overspending. People who do not pay their debts in a timely manner will soon have an unfavorable credit report, which can influence their ability to obtain new credit for years to come.

   How much debt is affordable and realistic? One rule of thumb is that no more than 20 percent of a household's take-home pay should be committed to consumer installment and credit card debt. Paying cash is almost always less expensive than using credit. When credit is used, it is best to borrow as little as possible, seek the lowest finance charge, and pay off the loan as soon as possible.

2. **Allocate Savings and Investments to Reach Goals:** The best way to take care of financial needs is to "pay yourself first." That is, establish a set amount to save and invest first each payday rather than immediately spending it on wants or needs. The habit of saving regularly for future goals is a powerful financial tool, even if the amount saved each payday is small. People living at low income levels may find it difficult to save money because most of their current income is needed for living expenses; however, even a few dollars a month can grow and contribute to improved financial security. The best motivation is to define the goals that are important to you and then to commit to the savings needed to reach them.

3. **Implement the Plan:** There is more information about different saving and investment alternatives available in Unit 2 of this teaching guide. Individuals should understand that there is nothing embarrassing about using a financial professional to help select specific investment products. There also are numerous resources at their fingertips to help them make decisions. They should be conscious, however, of the need to check out their financial professional just as diligently as they would research picking a stock or a mutual fund. (See Lesson 3.) The key things they will need to consider when it comes to setting up an investing plan are:

- **Risk tolerance** | Younger people have more time to invest, so they can take more risks and look at more aggressive investment alternatives. (See Units 1 and 2.) The greater the risk one is willing (and financially able) to assume to make money, the more money can be made. Key factors that determine your risk factor are age, income, and investing experience. Risk is the chance one takes that an investment will lose money or will earn less from one investment than another. If someone can't reasonably expect to do better than that for the risk being taken, there's no sense in taking the risk.
- **Time horizon** | The number of years one has to invest — and how long one has to achieve one's key short-, medium-, and long-term goals — will be one of the major ways to choose investment products. For example, if an individual will need money in five years, he or she wouldn't want to invest in a bond that tied up funds for 20 years (unless one is willing to pay a hefty premium). Similarly, individuals could consider an aggressive growth mutual fund if they have 20 or 30 years to reach their key goal. Investment products are like tools — when the "right tool" for the job is used, investors get the best result.
- **Diversification** | Investors shouldn't put all of their eggs in just one or even two baskets. Buying an investment product — such as a mutual fund — that involves multiple investments reduces one's overall level of risk and increases long-term potential for making a profit — this is ***diversification*** of investments. Investors seek the dual goals of growth and safety by distributing their investments among the three major asset classes: stocks, bonds, and cash or cash equivalents. The average annual market return of stocks, bonds, and cash differ substantially. Investing in all three categories helps shelter against major losses. This is true because stocks, bonds, and cash investments not only produce returns in different ways; they also tend to provide their strongest returns at different times. In most time periods, if one asset class is performing poorly, the other two are doing better.
- **Asset allocation** | Every person needs a financial plan that is suited to his or her specific needs. The right mix of stocks, bonds, and cash (see Unit 2 for descriptions) is the ideal asset allocation scheme. How this customized approach is put together can have major implications for return on investments. Individuals should recognize that asset allocation is a two-step process: First, they assign a percentage of their entire portfolio to each asset class — stocks, bonds, and cash. Second, they select a variety of investments within each of the three classes to make up that percentage. Their personal situation will determine what percentage of their portfolio is assigned (or "allocated") to each class. The best approach for each of them might be aggressive, moderate, or conservative. Aggressive investors seek growth by investing heavily in stock and stock mutual funds. Moderate investors might put 40-60 percent of their portfolios in stock or stock funds and the balance in bonds and bond funds. Conservative investors seek to hold on to what they have and, as a result, put the emphasis on cash investments and certain bonds.
- **Review and Modify the Plan As Needed** | A financial/investment plan is an ongoing process. It is a tool to help individuals reach their financial goals. Reviewing and modifying the plan is essential to the effectiveness of the overall plan. An important goal of a financial plan is to protect against financial risk.

About Employer-Sponsored Retirement Plans and IRAs

Saving money at work is one of the best ways to build up your retirement nest egg. If you are self-employed or want to save even more to "feather your nest egg," you need to understand the alternatives available to you:

Employer-sponsored retirement plans are saving and investment plans that allow employees to place funds in a tax-sheltered account for the purpose of funding all or part of their retirement. One example of an employer-sponsored retirement plan is a **401(k) plan**, a **tax-deferred** retirement plan that allows an employer to "match" employee deposits into the account up to a certain amount. Tax-deferred retirement savings plans for employees of government agencies or nonprofit organizations are known as 403(b) plans or 457 plans.

Matching contributions, or combining an employee's contribution with that provided by employers, is a very powerful incentive, or motivator, for encouraging participation in employer-sponsored retirement savings plans. It is essentially free money. In these plans, employees choose how to distribute their investments among the many different investment products offered.

Employer-sponsored retirement plans are generally grouped into two major categories: **defined benefit (DB)** and **defined contribution (DC)**. In a defined-benefit plan (often referred to as a "pension"), the employer promises to pay a defined amount to retirees who meet certain eligibility criteria. The employer pays a lifetime monthly benefit to retirees who fulfill specific age and service requirements. Benefits are usually linked to the number of years of service and salary level.

However, due to rising costs of defined benefit plans, fewer and fewer employers offer defined-benefit plans today.

An alternative to a defined-benefit plan is a defined contribution plan, which spells out what an employer puts in rather than a specific benefit you will receive in retirement. The employee receives the proceeds in either a lump sum or an **annuity** paid at various intervals. Since the benefit is not defined, the retirement outcomes depend on how well the employee does investing the money and how consistently they contribute over their working lives. In 1978, the Internal Revenue Code was modified to create 401(k) plans, authorizing the use of a new type of defined contribution plan that allows employees to make pre-tax contributions to a retirement plan.

Employee 401(k) contributions are automatically deducted from their paycheck each pay period. This money is taken out before the paycheck is taxed. Contributions are invested at each employee's direction into one or more of the mutual-fund-like options defined in the 401(k) plan. Employers often match employee contributions, but are not required to do so.

An advantage of these types of retirement plans is that employees can choose investment products that match their personal investment goals. One drawback is that many employees do not have a basic understanding of investments, and as a result, invest in products that do not match their investment goals or their risk comfort level. With proper education, employees will become comfortable with their investment choices and feel confident about their retirement preparations. Because most people will likely be required to fund a substantial part of their retirement, it is necessary to begin learning about investing early in life.

Even if workers don't have a 401(k) at work, they can set up their own **Individual Retirement Account (IRA)**. Under an IRA, they can put aside up to $5,000 of earnings yearly. The real beauty of the IRA is that earnings accumulate on a tax-deferred basis increasing the already powerful effect of compound interest. A yearly $5,000 non-deductible IRA contribution earning at a rate of 10 percent per year compounded annually over a 20-year period will grow to about $315,000. If the earnings were taxed annually in the 25 percent bracket, the account would grow to only about $232,700. Powerful stuff for those who want to invest in themselves!

The IRA alternative can be very attractive to young people and their parents and grandparents. An IRA can be used to pay for certain college and home-buying expenses. Qualified expenses include tuition, fees, books, supplies, and required equipment. For individuals attending college at least half time, room and board also qualifies. If individuals withdraw up to a total of $10,000 to buy or build a first home, they will escape the penalty. However, they will owe income tax on the withdrawal in both cases.

On the other hand, the **Roth IRA** has no deduction for contributions, but instead provides a benefit that isn't available for any other form of retirement savings: if you meet certain requirements, all earnings are free of taxes when you or your beneficiary withdraws them.

The opportunities for investing in IRAs are almost unlimited. Individuals can find sponsored IRAs in many institutions — banks, savings and loans, credit unions, mutual funds, insurance companies — offering almost every imaginable investment. If investors prefer to put together their own portfolio rather than rely on mutual fund managers, they can do it through what is called a "self-directed IRA."

These accounts, usually set up through brokers, let investors choose what they want to invest in, such as stocks and bonds of individual companies. They decide what and when to buy and sell. But if they wheel and deal too much, commissions can eat up a good portion of a nest egg. The fees attached to this type of account demand close attention, especially in the early years of an IRA, when it holds a relatively modest amount.

A **Roth 401(k)** combines some characteristics of Roth IRAs and 401(k)s. Pay-ins do not reduce taxable income because they are made with after-tax dollars. Withdrawals from them are tax-free, including earnings on the account, if an investor takes withdrawals after participating in the plan for more than five years and after they reach age 59 ½. The Roth 401(k) pay-in cap (the maximum amount you can put in) will be higher than for a Roth IRA. The standard 401(k) limits will apply per IRS Pension Plan Limitations plus additional catch-up provisions for participants older than age 50.

LESSON 3: Selecting Financial Professionals

If an individual decides to branch out beyond a retirement plan into the wider world of investing, he or she may end up needing the help of a **stockbroker** or **investment adviser** (sometimes called a "financial planner"). It is important to recognize that most financial professionals are salespeople who make most of their money on commission — which means they get part of what they sell you, just like a real estate agent or car salesman. Some investment advisers are paid on a fee basis or a percentage of the assets they manage, rather than for selling individual products.

Brokers make recommendations about specific investments like stocks, bonds, or mutual funds. While taking into account a client's overall financial goals, brokers generally do not give a detailed financial plan. Brokers are paid commissions when their clients buy or sell securities through them.

Investment advisers help to develop a financial/investing plan. Some investment advisers also work on a commission basis and sell the products that go into a financial plan. Others are "fee-only planners" who get paid a fee to develop a plan, but do not implement it. As with brokers, investment advisers who get a commission for selling products may have an incentive to steer individuals to certain investments that are more lucrative for them.

Remember: **There is no such thing as a free lunch**. Financial professionals get paid for the work they do — just like any other professional. Some of their fees are easier to see than others. But in all cases, investors should always ask the method and amount an adviser is being paid. If the fee is quoted as a percentage, it is critical to understand how that translates into actual dollars. Investors should press financial professionals to explain why a recommended investment strategy or product is right for them. A good rule of thumb for all consumers is to invest only in those products and strategies that they fully understand.

Federal or state securities laws require brokers, advisers, and their firms to be licensed, or registered, and to make important information public. But it's up to the individual to find that information and use it to protect his or her investment dollars. The good news is this information is easy to get – one phone call to your state securities office or Web search may save people from sending their money to a con artist, a bad broker, or disreputable firm. This is important because investors who do business with an unlicensed securities broker or a firm that later goes out of business are unprotected and there may be no way for them to recover their money.

Checking Out Stockbrokers

The Central Registration Depository (or CRD) is an online database that contains information about most brokers, their representatives, and the firms for whom they work. For instance, anyone can find out if brokers are properly licensed in his or her state and if they have had run-ins with regulators or have received serious complaints from investors. Information is also available regarding brokers' educational backgrounds and their employment history.

Investors can get information from the CRD or from either the office of their state securities regulator or FINRA. State securities regulators may provide more information from the CRD than FINRA, especially regarding investor complaints, so it's a good idea to check with them first. Contact information for state securities regulators is on the North American Securities Administrators Association (NASAA) Web site at **http://www.nasaa.org**. To use FINRA's **BrokerCheck** service, go online to **http://www.finra.org**, or call 1-800-289-9999.

Checking Out Investment Advisers

Any individual who gives investment advice for compensation, as well as the firm with whom they are employed, is required to be registered with either the U.S. Securities and Exchange Commission (SEC) or the state securities regulator(s) in those states in which they conduct business. Investment advisers who manage $25 million or more in client assets generally must register with the SEC. Those who manage less than $25 million usually register with the state securities regulator.

To find out if advisers are properly registered, read their registration forms. This document, which is referred to as Form ADV, has two parts: Part 1 has information about the adviser's business and if they have had problems with regulators or clients; Part 2 outlines the adviser's services, fees, and strategies. Always ask for and carefully read both parts of the ADV before hiring an investment adviser. Investment advisers' most recent Form ADV can be found online on the SEC website at **http://www.adviserinfo.sec.gov**. You also can get a copy from your investment adviser.

The database currently contains only those Forms ADV filed by investment adviser firms that register electronically using the Investment Adviser Registration Depository, but will eventually expand to encompass all registered investment advisers as well as their firms. Copies of Form ADV for individual advisers and firms are available from state securities regulators or the SEC, depending on the size of the adviser. To contact the state securities regulator, go online to **http://www.nasaa.org**. If the SEC registers the investment adviser, the Form ADV is available for a modest fee plus postage from the SEC.

Financial/Investment Planning: Myth vs. Reality

MYTH	REALITY
I don't earn enough money to need a financial plan.	A financial plan is a tool that helps people to live within their income. It also allows them to make better use of their money.
Investing is just for people with a lot of money.	Investing is for all income levels. People don't have to be rich to begin investing; however, they must have an understanding of basic investment products and their risks and rewards. Investing provides the opportunity for anyone to build wealth.
Young people don't need to think about saving for retirement.	Today's young people can expect to live 20 or more years in retirement. Those who begin early to contribute to a retirement savings plan are more likely to have money for a comfortable retirement because of time and compound interest. Saving small amounts of money over a long time makes use of the magic of compounding. Employer-based savings programs are tax-deferred, and the employer may contribute to your account as well. That's free money.
I'm too old to save for retirement.	It's never too late to start saving for retirement. The only thing worse than starting to plan when you are older … is not planning at all. Any prudent steps taken to ensure your security in retirement are good things.

Social Security is a business-funded program to provide financial aid to people who are retired.	Social Security is an employer and employee-funded government program that provides a base-level retirement income. It is not intended to be the sole source of retirement income. Individuals are responsible for filling the gap between income they will need in retirement and the money provided by Social Security. The additional funds can come from employer-based retirement savings plans, personal savings, and Individual Retirement Accounts (IRAs).

Lesson Outline: Financial Planning Phase 1

Financial Goals

OBJECTIVE	**Learners will:** ■ Create a set of personal financial goals, ranked in order of importance.
MATERIALS	■ 3"x 5" index cards for listing and ordering financial goals.
PROCEDURES	**Instructor will:** ■ Lead a discussion using the following statements: • "It takes more than luck to get what you want out of life." • "You have to know what you want, then create a plan to reach your goals." • Explain the process of creating a financial plan. • Use 3"x 5" cards for students to list financial goals. **Learners will:** ■ List three to five of their most important goals and estimate the cost of each (one goal per 3"x 5" card). Rank goals in order of importance. Individuals may modify or eliminate unattainable goals.
ASSESSMENT	■ 3"x 5" goal cards, ranked.
ESTIMATED TIME	■ 45 – 50 minutes of class time.
BEYOND THE CLASSROOM	■ Learners will describe the specific steps they will take to accomplish one or more of the goals indicated in this lesson.

FINANCIAL PLANNING PROCESS

- Identify financial goals
- Determine net worth
- Estimate and balance income and expenses
- Implement and modify the plan
    - Review personal debt situation
    - Allocate savings and investments to reach goals
    - Review the plan annually or as circumstances change
    - Modify the plan as needed

Lesson Outline: Financial Planning Phase 2

Net Worth Statement

OBJECTIVE	**Learners will:** ■ Create a personal net worth statement.
MATERIALS	■ "Net Worth Statement" worksheet.
PROCEDURES	**Instructor will:** ■ Lead a discussion about the key elements of a net worth statement: assets and liabilities. ■ Discuss valuation of assets (resale value, not the purchase price). **Learners will:** ■ Take the "Net Worth Statement" worksheet home and look at all their possessions. ■ Estimate the resale value to determine assets. ■ Determine liabilities. Do they owe any friends or family members money or have credit cards? Are they paying back a loan such as an auto loan?
ASSESSMENT	■ "Net Worth Statement" worksheet.
ESTIMATED TIME	■ 30 minutes of im-class time discussion plus outside homework.
BEYOND THE CLASSROOM	■ Help friends or family members crate a Net Worth Statement of their own.

Name ______________________________ Date ______________

Personal Net Worth Statement

Assets — What You Own	
Cash on hand	$
Checking account	$
Savings (CDs, U.S. Savings Bonds, etc.)	$
Cash value of life insurance	$
Personal property	$
Money owed to you	$
Investments (market value of stocks, bonds, mutual funds, etc.)	$
Other:	$
Total Assets:	$

Liabilities — What You Owe	
Personal loans (parents, siblings, friends)	$
Credit card balances	$
Installment loans (auto, furniture, bank loan, etc.)	$
Mortgage balance	$
Educational loan balances	$
Other:	$
Total Liabilities	$

Net Worth	**= Total Assets**	**— Total Liabilities**
$__________	**= $**__________	**— $**__________

Lesson Outline: Financial Planning Phase 3

Income and Expense Statement

OBJECTIVE	**Learners will:** ■ Create a personal income and expense statement.
MATERIALS	■ “Income and Expense Statement” worksheet. ■ “If Expenses Exceed Income” overhead. ■ “If Income Exceeds Expenses” overhead.
PROCEDURES	**Instructor will:** ■ Lead a discussion using the following statements: • “The best way to get ahead financially in life is...” • “There’s no need to keep track of what you spend, just be careful and everything will work out fine.” ■ Discuss key elements of an income and expense statement. ■ Distribute the “Income and Expense Statement” worksheet and have the learners estimate how much they spend and how much they earn each month. ■ Collect the worksheets and hold them for one month. During this month, individuals will track all their expenses. ■ At the end of the month, pass out a second income and expense statement and have individuals complete it with their actual figures. Return their first income and expense statement and have them compare the amounts on both statements. How accurate were their estimates? ■ Discuss alternatives if expenses exceed income or income exceeds expenses. ■ Ask: Did the month’s income exceed the expenses or vice versa? How? What items were underestimated or overestimated?

Lesson Outline: Financial Planning Phase 3

Income and Expense Statement

PROCEDURES	**Learners will:** ■ Complete the "Income and Expense Statement" worksheet in class and turn it in. ■ Record each time they spend money and receive any type of income for the next month. ■ Fill out a second "Income and Expense Statement" worksheet at the end of the month with the actual amount spent to compare with the first statement. ■ Describe the differences between their first and second income and expense statements. ■ Discuss the importance of living within their income to achieve financial independence.
ASSESSMENT	■ Two "Income and Expense Statement" worksheets
ESTIMATED TIME	■ 45 – 60 minutes in class and outside homework.
BEYOND THE CLASSROOM	■ Interview people from several generations (World War II, Baby Boomer era, Gen X, etc.) about different methods they have used to track their income and expenses and organize their finances. Ask how they budget their money and what they have done to reduce expenses and make ends meet.

IF EXPENSES EXCEED INCOME...

- Determine where overspending occurs
- Cut back on expenses
- Postpone some expenditures
- Increase income

IF INCOME EXCEEDS EXPENSES...

- Increase savings and investments for future goals
- Satisfy more immediate wants
- Increase giving to worthy causes

Name ______________________________ Date ______________

Income and Expense Statement

Income Source		Expense	
Wage from primary job	$	**LIVING**	
Wage from 2nd job	$	Rent/Mortgage	$
Gifts	$	Housing bills	$
Interest on savings	$	Food	$
Interest on earning	$	Clothing	$
Other	$	Laundry/Cleaning	$
		Other	$
		TRANSPORTATION	
		Car payment	$
		Public transportation	$
		Gas	$
		Maintenance	$
		Insurance (auto, etc.)	$
		Other	$
		OTHER	
		Entertainment	$
		Medical	$
		Emergency fund	$
		Savings	$
		Personal care	$
		Gifts	$
		DEBT	
		Credit/Loan payments	$
		Other	$
Total	$	Total	$

Discretionary income is what is left after all bills and regular monthly expenses are paid. What is your discretionary income?

Net Worth **= Total Assets** **— Total Liabilities**

$______________ = $ ______________ — $ ______________

Name ______________________________ Date ______________

Financial Case Study: Maria Lopez

Net Worth Statement

Maria is 22 years old. She works as a ______________

______________in (City) ______________

____

Maria's Assets | Maria owns a used car valued at $6,000. She has $200 cash in her apartment and $900 in a bank checking account. She owns jewelry valued at $400, a TV valued at $800, and a computer valued at $1,200.

Personal items such as clothes, books, luggage, a bicycle, furniture, and dishes are valued at $1,100. Maria did not purchase the optional term life insurance policy available through her employer because she has no dependents.

Maria owns a stock mutual fund with a current value of $1,500.

Maria's Liabilities | Maria owes $4,000 on her car and $6,000 on a student loan. Her credit card balance due is $850. The credit card purchases were for furniture for the apartment and clothes for work.

Car	**$6,000**
Cash	**$200**
Bank	**$900**
Jewelry	**$400**
CD System	**$300**
Computer	**$1,200**
Personal	**$1,100**
Mutual Fund	**$1,500**
Total Assets	**$** ________
Car	**$4,000**
Student Loan	**$6,000**
Credit Card	**$850**
Total Liabilities	**$** ________
NET WORTH	**$** ________

Maria's Financial Goals | Maria would like to pay off her student loan, reduce her credit card debt, and increase her savings. She wants to buy a washer and dryer and continue to upgrade her wardrobe for work. A summer trip with friends would also be nice.

Maria wants to begin contributing to her employer-based retirement savings plan at work. It is called a 401(k) plan, and her employer matches her contribution. This is a salary reduction plan, so Maria would not pay income tax on the contributions and earnings are tax-deferred.

Calculate Maria's Net Worth: Total Assets — Total Liabilities ________________________

Maria's Income

Maria's annual salary is ___________. After taxes, her take-home pay is approximately ___________, which is automatically deposited into her bank checking account. In addition, Maria receives an annual cash gift of $1,000 from her grandparents. Maria reinvests her earnings in her mutual fund account. She expects no other income this year.

Maria's Expenses

Housing | Maria pays monthly rent of ____________ and her electrical bill is _______________. Monthly telephone and Internet costs are ____________________ and the gas bill is _____________.

Food and Clothing | Maria's food at home averages __________________ per month. Her food away from home averages ___________________. She spends about __________________ a month on clothing and on laundry and cleaning.

Salary	$
Take-home pay	$
Gifts	$
Rent	$
Electrical	$
Cell phone	$
Internet	$
Gas	$
Food Home	$
Food Away	$
Clothing	$
Laundry/Clean	$
Gasoline	$
Car Maintenance	$
Parking	$
License	$
Car Loan	$
Student Loan	$
Credit Balance	$

Car | Maria is beginning to think that her car is an expensive convenience because public transportation is good and she lives near a shopping center. Gasoline averages ___________ per month. Maintenance costs average ___________. Parking fees are ___________per month and license costs are ___________ per year.

Loans | Maria's monthly car payment is ___________ and her student loan payment is ___________. She pays $50 a month on her credit card balance.

Insurance | Maria's auto insurance costs ___________ per year. She does not own life or renter's insurance. Her medical, dental, and disability insurance are paid by her employer.

Recreation | Maria spends ___________ on health club dues and ___________ on movies. She enjoys reading, hiking, and swimming.

Other | Maria spends about ___________ a month on haircuts and personal care. She contributes ___________ a month to a charitable organization and spends about ___________ a year on gifts for family and friends.

Savings and Investments | Maria knows that saving regularly is important so she sets saving as a regular monthly expense.

Her emergency fund is the $900 in her checking account. She would like to increase it to an amount equal to three months' living expenses. She authorized the bank to automatically deposit $50 each month from her checking account into her mutual fund account. She also plans to contribute to the 401(k) plan at work.

Auto Insurance	**$**
Health Club	**$**
Movies	**$**
Personal	**$**
Gifts	**$**
Savings	**$**
Emergency	**$**
Mutual Fund	**$**
401(k)	**$**

Lesson Outline:
Employer-Sponsored Retirement Plans

OBJECTIVE	**Learners will:** ■ Analyze an investor's plan for dividing savings among stocks, bonds, and cash reserves in an employer-sponsored retirement saving/investing plan.
MATERIALS	■ "Employer-Sponsored Retirement Plans" worksheets.
PROCEDURES	**Instructor will:** ■ Review the relative risks and returns that might be expected from stocks, bonds, and cash reserves using "Pyramid of Investment Risks" from Unit 1. ■ Ask individuals to explain the difference between a stock and a bond. Give examples of cash reserves. Historically, which categories of investments have yielded the greatest long-term return — stocks, bonds, or cash reserves? ■ Define and discuss time value of money, diversification, and asset allocation. ■ Have individuals complete the "Employer-Sponsored Retirement Plan" worksheet. ■ Debrief the activity by having individuals discuss why they chose the option (aggressive growth, growth, moderate growth, or conservative growth). **Learners will:** ■ Participate in the class discussion. ■ Complete the "Employer-Sponsored Retirement Plan" worksheet.

Lesson Outline:
Employer-Sponsored Retirement Plans

ASSESSMENT	■ From the completed worksheets and class discussion, determine whether the individuals grasped the concepts of saving, investing, risk, time value of money, and diversification as applied to asset allocation decisions.
ESTIMATED TIME	■ 45 – 60 minutes of class time.
BEYOND THE CLASSROOM	■ Learners will interview someone who has retired about retirement preparation. Among other questions they may ask, "What would you do differently about saving for retirement if you were young again?" ■ Learners will interview local high school graduates about their experiences regarding saving part of their income through employer-sponsored saving/investing plans.

Name ______________________________ Date ____________

Employer-Sponsored Retirement Plans

Jim and Tina are engaged to be married. Prior to their marriage, they discussed their knowledge and feelings about money. One financial issue they are currently exploring is their employee-sponsored retirement programs. They studied information from their employee benefits offices and also checked the Internet for information on 401(k) plans and asset allocation options. Finally, they spoke with parents and friends who had experience with employer-based savings programs. Below are some of the questions they asked.

QUESTION: Should we join the employer-sponsored program?

Contributing to 401(k) plans can help employees prepare for a financially secure future, especially since some employers often match employee contributions. It's never too soon to start a regular investing plan to take advantage of the tax-deferral and compounding that 401(k) plans offer.

QUESTION: How should we divide our contributions among stocks, bonds, and cash reserves?

There are no easy answers here. Decisions on how to divide Jim and Tina's retirement contributions are dependent on their risk tolerance, the number of years until retirement, and the options provided in their employer-sponsored plans. Here are some ideas Jim and Tina can use:

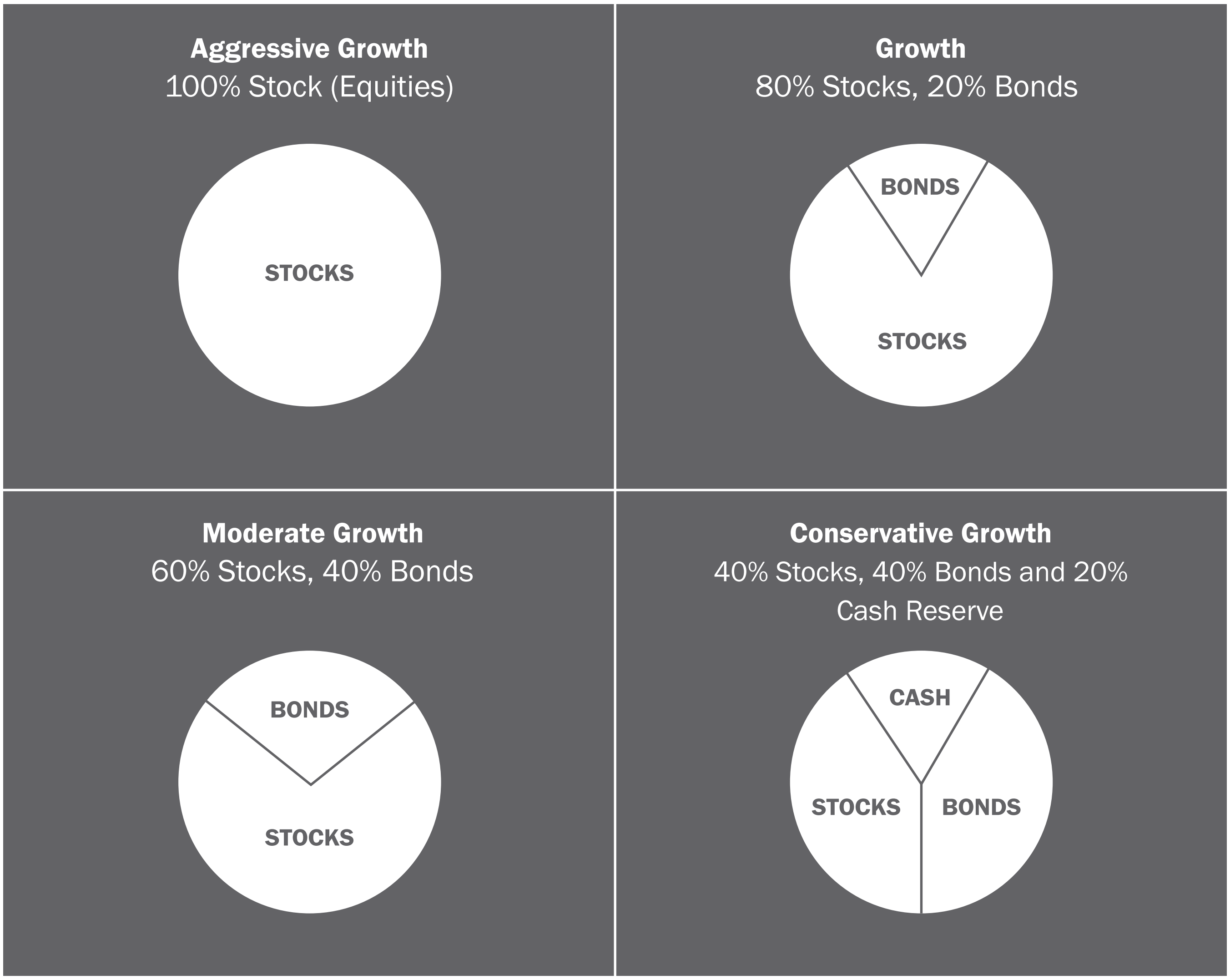
- Diversify to reduce risk.
- Time is on their side so they can assume greater risk.
- Other investment advisors say that young people who have 30 to 40 years before retirement can afford to be much more aggressive with stocks because they have more time to ride out the market and make up for losses. Historically, stocks have outperformed bonds significantly, but there are no guarantees of future performance.
- Individuals must determine their preferences and understand the trade-offs of both options.

QUESTION: Can we use the money in our employer-based savings plans for emergencies before we retire?

Yes, Jim and Tina can borrow from their retirement savings plan, but they will not borrow unless absolutely necessary. Borrowing will reduce earnings because the principal has decreased and may trigger income taxes and penalties. As an alternative, Jim and Tina decide to seek other loan options.

Decision Time — Initial Asset Allocation

Jim and Tina have narrowed their allocation choices to four options.



Which plan would you recommend for Jim and Tina? Give reasons for your answer.

Jim and Tina know that their 401(k) plans give them the option to alter their allocations if their goals change or if they find the allocation too conservative or too risky. What might be the reason(s) to do this?

Name ____ Date ______________

Unit 3 Test

MULTIPLE CHOICE

1. A ______________________ is a road map to help you plan your future.
2. Saving $20 a week to buy a new TV is an example of a _________________________ financial goal.
3. ________________________ refers to the mix of stocks, bonds and other investment vehicles individuals develop as part of their financial/investment plan.
4. "Don't put all your eggs in one basket" is an example of ________________________ in your financial / investment plan.
5. The securities agency regulates ________________________ in your state.
6. Background information on individual financial professionals is available from the ______________________.

Diversification	Financial/Investment plan	Investment advisers
Asset allocation	Short term	Central Registration Depository

TRUE OR FALSE

1. T F Financial/investment plans, once developed, should not be modified.

2. T F Since young people have more time to invest, they can afford to take more risks in their investments.

3. T F Having a combination of varied investments in your portfolio reduces your overall risk to loss.

4. T F An employer match is a strong disincentive for employees to contribute to 401 (k) plans.

5. T F Investing in mutual funds is a good way to achieve diversification.

6. T F The ADV form will help you check the experience and services of investment advisers you may be considering hiring.

Unit 3 Answer Key

MULTIPLE CHOICE

1. **Financial/Investment plan**
2. **Short range**
3. **Asset allocation**
4. **Diversification**
5. **Investment advisers**
6. **Central Registration Depository**

TRUE OR FALSE

1. **False**
2. **True**
3. **True**
4. **False**
5. **True**
6. **True**