THEME 5

Get a Plan: Get a Grip on Life

OVERVIEW

Student Letter

Do you know people who handle money carelessly? Lots of seemingly smart people are clueless on where they stand financially. There is Beverly, a professional woman, who calls the bank every two or three months to find out what the balance is in her checking account. She has never reconciled her checking account, so she never knows what her balance is. What Beverly still hasn't learned is that people at her bank don't know what Bev's real balance is either, because they don't know what checks Beverly has written in the last day or two. Only Beverly knows that. And then there is Ben. Ben actually believes that he can write checks as long as he has blank ones to be used. Ben has been heard to say, "Why would the bank give me blank checks if I'm not supposed to use them?"

You can avoid financial life in the Bev and Ben lane. You can get on the fast track to wealth by becoming good at managing your money. It starts with knowing some basic information and using some common sense and then taking action. We recommend three steps.

First, get a grip on your spending. How can you do that? Use the old-fashioned way. Set up a budget. Make a list of your income and expenses. Then subtract your expenses from your income. If you have any surplus cash, plan how you will use it. Do this each month. Maybe you will learn that now is the time to get started with a mutual fund or stock account.

Second, get to know the various services offered by financial institutions in your community. Checking accounts are perhaps the most common financial service people use, but there are many others including ATMs, direct deposits, savings accounts, credit cards, installment loans, student loans, retirement accounts, and stock accounts. While there are many types of financial institutions, the four most important ones are commercial banks, savings and loans, credit unions, and brokerage firms. Open an account now at one or more financial institutions. Start with checking and savings, but don't wait long to start other, more rewarding savings programs. Becoming wealthy is within your grasp. Starting to save when you are young is absolutely the best time.

Finally, you need to learn how to protect yourself against risk. All choices involve risk. But some risks are greater than others. Buying insurance is a common way to reduce risk. There are many kinds of insurance to consider including auto, health, renter's, homeowner's, life, and disability. The type and amount of insurance you will need will change as you get older and as the value of your assets increases.

The best thing regarding these three tips and others covered in these lessons is that none of this is overly difficult. It might take some work, but you can learn this stuff. Your efforts now can have a big payoff later.

Questions

1. What is a budget?

2. What are examples of financial institutions?

3. What is the point of buying insurance?

4. What are common forms of insurance?

5. When is the best time to get started on saving your first million bucks?

FAQs

ABOUT GET A PLAN: GET A GRIP ON LIFE

1. What is net worth?

Net worth is a measure of what you are worth financially. Net worth is the current value of your assets minus your liabilities.

2. What does it mean to "pay yourself first"?

Treat savings like it is a fixed expense—the same as paying your rent or car payment. Set your saving goal and arrange your income and spending so that you can reach it.

3. What are some common services offered by financial institutions such as banks, savings and loans, credit unions, and brokerage firms?

There are many financial services with which to become familiar. These include checking accounts, savings accounts, certificates of deposit, direct deposit, deposit insurance, credit cards, installment loans, home mortgages, home equity loans, student loans, small business loans, retirement accounts, and accounts for the purchase of stocks, bonds, and mutual funds.

4. Can you write checks as long as you have blank checks?

No. Here is how it works. You deposit money in your checking account to cover checks that you write. The checks that you write are subtracted from your checking account. If you write checks for more than the amount of funds in the account, negative consequences await. Your bank and most creditors charge high fees for overdrafts, which is when the requested payments from the account are more than what is in the account. When you write a check for money you don't have in the account, you risk ruining your credit rating. If you repeatedly write checks for more than what is in your account, you will be taken to court and could be put in jail.

5. How does insurance work?

The idea is to spread out the risk over several payers. A pool of people contribute money to buy insurance with the expectation that only a few will actually experience a loss that will need to be covered.

6. When is the best time to get started on your first million bucks?

Now!

EXERCISE 20.1

Budgets Are Beautiful Call-In Show

Radio Host Budget Bob

Hello, financial health fans! Welcome to the nation's newest financial advice show, Budgets Are Beautiful. This is the radio call-in show that lets you, the radio listener, get the latest advice on how to manage your family finances. Today our topic is how to improve your skills at managing your family's finances. Our guest today is a successful family financial planner, Dr. Penny Saver. Dr. Saver has helped hundreds of families and has a Ph.D., M.A., and an S.U.V. Hello, Dr. Saver. Welcome to the show.

Dr. Saver

Hello Bob, and hello to all those people who are tuned in today. I am ready to take your questions.

Budget Bob

Here is our first caller: Connie from Connecticut. You're on the air, Connie.

Connie

*Hi ,Dr. Saver. I am having a disagreement with my husband regarding the meaning of some financial vocabulary. He had heard someone on another call-in show talking about how to spend **disposable income.** My husband laughed and said that **all** our income is disposable. He said that we dispose of all our income by the end of every month. Sometimes we dispose of our income **before** the end of the month. I think he was joking, but could you tell me: What do financial planners mean when they talk about disposable income?*

Dr. Saver

Actually, your husband was not too far off. Disposable income is the money that you have to spend or save as you wish after you pay your taxes, Social Security, and the other deductions that have been taken out of your gross pay. While disposable income can be used in many ways, most families have important financial obligations. Rent, car payments, and food bills add up quickly, so tough choices need to be made.

Budget Bob

That sounds kind of gloomy, Dr. Saver. Do you have any advice for Connie and her husband on how to get better use out of their disposable income?

Dr. Saver

Financial planners suggest that setting up and sticking to a family budget is the first step toward financial success. I advise families to start by setting a monthly budget. To do this, you make a list of your income and expenses. Under income, list all the money you anticipate earning for the month. For most people, most income will be what they earn from their jobs. Then list your expenses. Under expenses, write all the expenses you think you will have in the month, item by item. Common expenses are rent, car payment, insurance, groceries, and so forth. Then, subtract your expenses from your income. I hope that this is a positive number! If it is—if you have more income than expenses—then you have surplus cash that can be put to other uses. If, however, the number is negative, then you will need to cut your expenses, increase your income, or spend some of your savings to get through the month.

Budget Bob

Here is our next caller: Calvin from California. You're on the air, Cal.

Calvin

Hello Dr. Saver. Thanks for taking my call. My wife and I started to write a monthly budget and we learned right away that not all expenses are the same. Some seem to stay pretty much the same each month while others change. Do other people have this same situation? Can you comment on the different types of household expenses?

Dr. Saver

Great question! Families ordinarily have what we call fixed expenses and variable expenses. Fixed expenses are ones that are relatively constant each month. These are a family's definite obligations such as a house payment, rent payment, car payment, medical insurance, and fuel for the car. These expenses are hard to change in the short term, so we say they are "fixed." Variable expenses are ones that are likely to change in the short term. Telephone, groceries, medical bills not covered by insurance, entertainment, recreation, charge account purchases, and so forth are variable expenses. These are expenses over which you have more short-term control.

Budget Bob

Dr. Saver, I sometimes hear advisors say, "Pay yourself first." In other words, set money aside from your disposable income to put into your savings plan. How does this idea of "pay yourself first" fit into the family's expenses?

EXERCISE 20.1 Continued

Dr. Saver

I tell my clients to include their savings goal in the fixed expenses part of their budget. I like this approach because it shows how important saving is to future individual and family financial health. Under the saving part of the budget, a family or individual could list funds saved for emergencies, as well as other cash set aside for long-term savings and investments.

Budget Bob

Here is our next caller, Minnie from Minnesota. You're on the air, Minnie.

Minnie

I just love this show, Dr. Saver. Here is my question. My sister Emily told me that she heard on television that people might have high incomes and still have a low net girth. What's all this about net girth? Is it true that people who have high incomes are also thin?

Dr. Saver

*Minnie, I think that you misunderstood your sister Emily. I think that she was referring to the idea of net **worth**, not net **girth.** Let me explain. People can have high incomes and still not be wealthy. When we measure wealth, we are measuring net worth. Here is how to figure your net worth. Net worth is determined by two factors. First, list your assets and their value. Assets are what a person owns including the value of any savings, house, car, and personal possessions. Next, list your liabilities. Liabilities are the money you owe others such as a home mortgage, car loan, credit card debt, college loans, and so forth. If your assets are greater than your liabilities, then you have a positive net worth. If your liabilities are greater than your assets, then you have a negative net worth. Individuals can have a large income and, due to their liabilities, still have a negative net worth.*

Minnie

Can I follow up on that last point? Do you mean to say that you can't tell whether a person is wealthy just by knowing where they live, what they drive, and where they travel?

Dr. Saver

That is exactly what I mean, Minnie. People who live in big homes, drive extravagant cars, and take around-the-world cruises probably have high incomes. That does not mean that they are wealthy. We measure wealth by calculating net worth. Many people of modest income have achieved a high net worth—many are millionaires—by living below their means.

Budget Bob

Well, Dr. Saver, that is all the time we have for today's show. Thank you for being with us.

Dr. Saver

You're welcome, Bob. Thanks for inviting me.

Budget Bob

Be sure to join us tomorrow when we will speak to Ms. Bonnie Bonds, another financial advisor. Bonnie's topic is "What Is Gross About Your Gross Income?" We hope you will tune in to the show tomorrow. We will be waiting for your call.

Questions

1. What is disposable income?

2. What does Dr. Saver recommend as the three parts of a family budget?

3. What are fixed and variable expenses? Use examples to illustrate each.

4. What does this idea of "pay yourself first" mean?

5. What is net worth?

EXERCISE 20.2A

John and Marcia: Monthly Spending Plan 1

John and Marcia are a young married couple. They have a two-year old child named Ashley and a goldfish named Shark. John manages a local shoe store. Marcia recently graduated from college and is a manager-trainee at a local bank. Their combined monthly income is $3,200. They want to have a successful marriage, and they want to be financially successful.

John and Marcia have enough income to provide an adequate lifestyle. Their apartment is comfortable but not lavish. They take care of themselves, Ashley, and Shark with sensible diets, exercise, and medical care. They view maintaining health, life, disability, and renter's insurance as essential. They pay for child care at Terrific Tots Day Care so that both of them can work. They keep up with all their financial commitments, such as making payments on Marcia's college loan. They regard saving for retirement as important. Like other individuals, they are locked into their fixed expenses, but they have more flexibility with the variable expenses.

Marcia and John know that they want a second car. It is difficult to manage their complex schedules—work, day care, grocery shopping, and trips to the doctor—with only one car. They recently set a goal to save up enough money in one year for the down payment on a second car.

John and Marcia are regular savers. They practice the idea of "paying yourself first." They currently have $175 withheld from their paychecks to provide a fund for emergencies. They plan to have $400 taken out for the next year to make the down payment on the second car.

Listed below are the "before" and "after" fixed expenses. The only one which has changed is "savings withheld." Figure out where they can draw the additional money for savings from their variable expenses. Also, answer the questions on the next page.

Monthly Budget	Before	After
Total income (both spouses work)	$3,200	$3,200
Fixed Expenses		
Housing	600	600
Life and disability insurance	60	60
Renter's insurance	15	15
Automobile insurance	80	80
Student loan	100	100
Savings withheld	175	400
Federal and state taxes	320	320
Social Security	245	245
Pension fund withheld	65	65
Total fixed expenses	**$1,660**	**$1,885**

VARIABLE EXPENSES

Meals (home)	300	______
Meals (away from home)	100	______
Utilities	180	______
Automobile fuel, maintenance	65	______
Medical	60	______
Child care	260	______
Clothing	55	______
Gifts and contributions	55	______
Magazines and newspapers	40	______
Home furnishings and appliances	40	______
Personal care	55	______
Entertainment	100	______
Vacation	120	______
Credit card	55	______
Miscellaneous/personal	55	______
Total variable expenses	**$1,540**	______
Total expenses	**$3,200**	**$3,200**

Questions

1. What are some examples of John and Marcia's fixed expenses?

2. What are some examples of John and Marcia's variable expenses?

3. John and Marcia have decided to practice the "pay yourself first" approach to saving for a second car. How do they pay themselves first?

4. Examine the monthly spending plan above. What sacrifices do you think John and Marcia should make in their variable expenses to meet their goal?

5. What are the benefits and costs of your recommended decisions for John and Marcia?

EXERCISE 20.2B

John and Marcia: Monthly Spending Plan 2

One year later, John and Marcia are pleased with their financial decisions. They have been able to reduce their expenses to purchase the second car. They have enjoyed the convenience of owning a second car, their income has increased, and Marcia's college loan has been paid off. But new challenges have arrived. The car payment is greater than the college loan was. While having two cars has made life much better, the extra car has added to insurance and car expenses. Also, increased income means the couple pays more in taxes and Social Security.

Marcia and John know that to be financially successful they need to begin acquiring better assets. Owning a home is on the top of their personal and financial wish list. They recently set a goal to save up enough money in no less than four years for a down payment on a "starter home."

John and Marcia currently have $400 withheld from their paychecks for savings. They plan to have another $100 taken out for the next year to start their home down payment fund.

Listed below are the "before" and "after" fixed expenses. The only fixed expense that has changed is "savings withheld." Figure out where they can draw the additional money for savings from their variable expenses. Also, answer the questions on the next page.

Monthly Budget	Before	After
Total income (both spouses work)	$3,520	$3,520
Fixed Expenses		
Housing	600	600
Life and disability insurance	60	60
Renter's insurance	15	15
Automobile insurance	130	130
Car loan	200	200
Savings withheld	400	500
Federal and state taxes	350	350
Social Security	270	270
Pension fund withheld	70	70
Total fixed expenses	**$2,095**	**$2,195**

VARIABLE EXPENSES

Meals (home)	285	______
Meals (away from home)	50	______
Utilities	180	______
Automobile fuel, maintenance	90	______
Medical	55	______
Child care	260	______
Clothing	55	______
Gifts and contributions	55	______
Magazines and newspapers	15	______
Home furnishings and appliances	40	______
Personal care	55	______
Entertainment	75	______
Vacation	100	______
Credit card	55	______
Miscellaneous/personal	55	______
Total variable expenses	**$1,425**	______
Total expenses	**$3,520**	**$3,520**

Questions

1. What is John and Marcia's new financial goal?

2. Examine the monthly spending plan above. What sacrifices do you think John and Marcia should make in their variable expenses to meet their goal?

3. What are the benefits and costs of your recommended decisions for John and Marcia?

EXERCISE 21.1

What Are Financial Institutions?

Financial institutions help people manage, protect, and increase their money. Individuals may use different types of financial institutions in different stages in their lives. While there are several different sorts of financial institutions to study, we will examine four:

- Commercial banks
- Savings and loan associations (S & Ls)
- Credit unions
- Brokerage firms

In the past, each type of financial institution offered specific and limited services. Banks took deposits in the form of checking accounts, savings accounts, and certificates of deposit and they granted credit to qualified individuals. Savings and loans offered savings accounts and home mortgages. Credit unions were a type of member-owned cooperative. Credit unions made low-interest loans available to their members. Brokerage firms were businesses that bought and sold stocks on an exchange, and offered other financial services.

Deregulation in the financial industry has blurred the lines between these institutions and increased competition among them. Deregulation means that laws were enacted to remove some of the restrictions (or regulations) that affected the industry. For example, savings and loans can offer many types of loans in addition to home mortgages as well as checking accounts. Many commercial banks can now sell stock.

Overview of Financial Services

DEPOSIT SERVICES

Types	Characteristics
Checking accounts	The convenience and safety of paying by check instead of cash.
Savings accounts and certificates of deposit (CDs)	Safe places to let your money grow.
Automated teller machines (ATMs)	Easy access to your money from multiple locations, 24 hours a day.
Direct deposits and automatic withdrawals	The ability to deposit money or pay bills automatically.
Deposit insurance	The guarantee that your deposits are insured by the federal government for up to $100,000 per depositor. Agencies which provide this insurance are FDIC (banks and S&Ls) or NCUA (credit unions).

CREDIT SERVICES

Types	Characteristics
Credit cards	The ability to access credit conveniently up to the amount of your approved credit limit.
Installment loans and credit lines	The opportunity to borrow for major items such as a new or used automobile, education, home improvement, and other personal or household items.
Mortgages	The opportunity to borrow for a home purchase.
Home equity loans	The ability to borrow against the equity in your home.
Student loans	The ability to borrow at below-market rates to pay for a college education.
Small business loans	The ability to borrow for the financial needs of a small business.

INVESTMENT SERVICES

Types	Characteristics
Retirement accounts (IRAs, SEPs, KEOGHs)	The ability to save money toward retirement on a tax-deferred basis.
Stocks, bonds, and mutual funds	The ability to invest in corporations and governments in order to meet your financial needs for the future.

Questions (2-5 continued on next page)

1. Name four common financial institutions.

Questions (continued)

2. How are financial institutions changing?

3. What are some of the common deposit services?

4. What are some of the common credit services?

5. What are some common investment services?

EXERCISE 21.2

Checking Out Checking Accounts

Financial institutions offer many kinds of services. Perhaps the most widely used financial service is the checking account. A checking account allows you to deposit money into an account. You then can write checks or drafts to withdraw money from the account as you wish. This type of account is also called a demand account because you can demand or use the money in your account as you wish.

Only the depositors can write checks on the account. Financial institutions usually charge a fee or require a minimum balance to maintain a checking account.

The checklist that follows provides an overview of steps involved in getting started with your first checking account.

Opening a checking account	• Take identification to the bank officer who handles new checking accounts. • Choose the type of checking account that best fits your needs. • Complete a signature card. • Make an opening deposit.
Choosing a checking account	There are three main types of checking accounts: • Special account: Service fees are charged at a low, flat rate with an additional fee for each check written. This account is often appropriate for a high school student. • Standard account: Set monthly fee with no check charge. May avoid a fee with a minimum balance. • Interest bearing account: Interest is paid if you maintain a minimum daily balance during the month.
Making a deposit	• Know the parts of a deposit slip. See the model in Illustration 21.1. • Write the date. • Write the amount of currency and coins to be deposited in the box marked "cash." • If checks are being deposited, write in the amount of each check. • Total the cash and check amounts. • Subtract any cash you wish to receive back. • Keep a copy of the deposit slip for your records. • Record the date and the amount of the deposit in your check register. Add the amount of the deposit to the balance.
Endorsing a check	• An endorsement is a signature on the back of a check instructing the bank on how the check may be cashed.

Endorsing a check *(continued)*	• A blank endorsement is simply your signature on the back of the check. This makes the check as good as cash to anybody who holds it. • A restrictive endorsement tags a check for a specific purpose, such as for deposit only to a checking or savings account. • A special endorsement allows you to transfer the check to another person. No one except the person named in the endorsement may cash or deposit the check.
Writing a check	• Know the parts of a check. See the completed check in Illustration 21.2. • Complete all the parts of the check including date, "pay to the order of" (payee), numeric amount, written amount, and signature line. If you wish, complete the memo line to indicate the purpose of the check. • Use a pen. • Write clearly. • Sign your name as it appears on the signature card. • When you make a mistake, write void on the check and keep the check for your records. • Be sure that you have enough money in your account to cover each check you write. • Record the number, date, payee, and amount of the check in your check register. Subtract the amount of the check from the balance.
Reconciling your checkbook	• Financial institutions send a monthly statement that summarizes the activity of your checking account including deposits, checks written, service charges, and any interest earned. • Compare your checkbook register to the monthly statement. Check off deposits and withdrawals. Record in the register any service charges or interest earned listed on the bank statement but not in the register. • Use the printed form sent by the financial institution with your statement to reconcile your checking account. • Write the ending balance as shown from the statement. • Add deposits to the ending balance that are listed in the register but not on the statement. • Subtract withdrawals listed in the register but not on the statement. • Note the adjusted balance; it should equal the checkbook register. • If the account does not balance, research possible explanations such as having missed checks that did not clear the account, fees charged, interest paid, calculation errors, or transposed numbers.
ATMs and debit cards	• Automated teller machines (ATMs) allow you to conveniently deposit, withdraw, or transfer funds, and verify your account balance. • ATMs use a PIN (personal identification number) to allow you to do a transaction. • A debit card is issued by many financial institutions. • A debit card allows you to have the amount of a purchase withdrawn directly and immediately from your checking account. • Be sure to keep receipts when you use your debit card, and record the transactions in your check register, including any additional changes.

Questions

1. What is a checking account?

2. Why do you suppose the signature card is important when you open a checking account?

3. What kind of a checking account is appropriate for most high school students?

4. What is a blank check endorsement for a check?

5. When should you void a check?

6. What is a debit card?

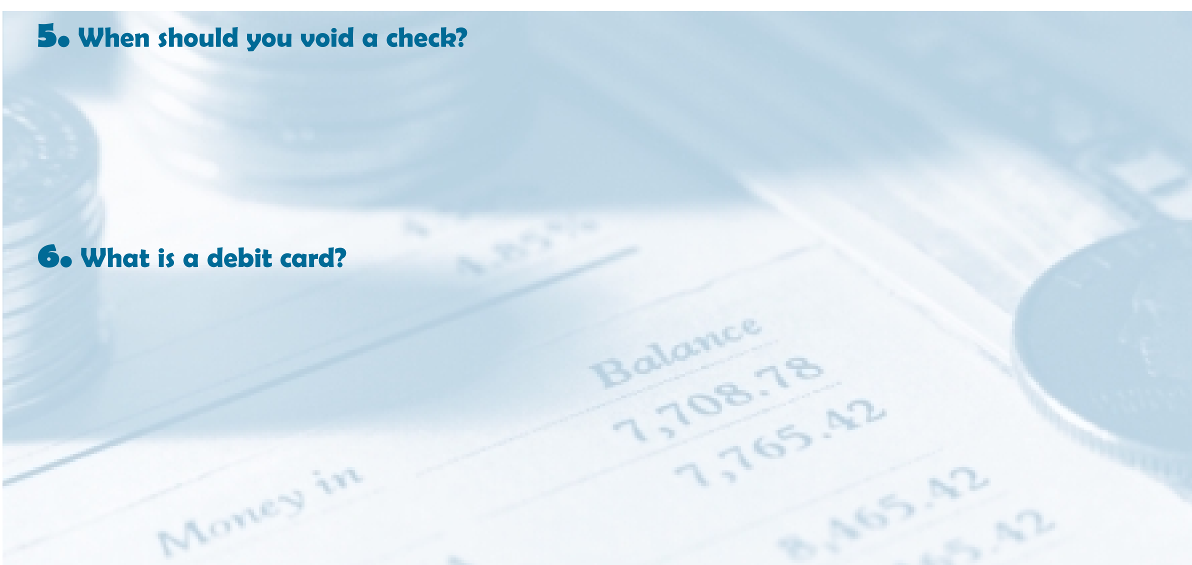
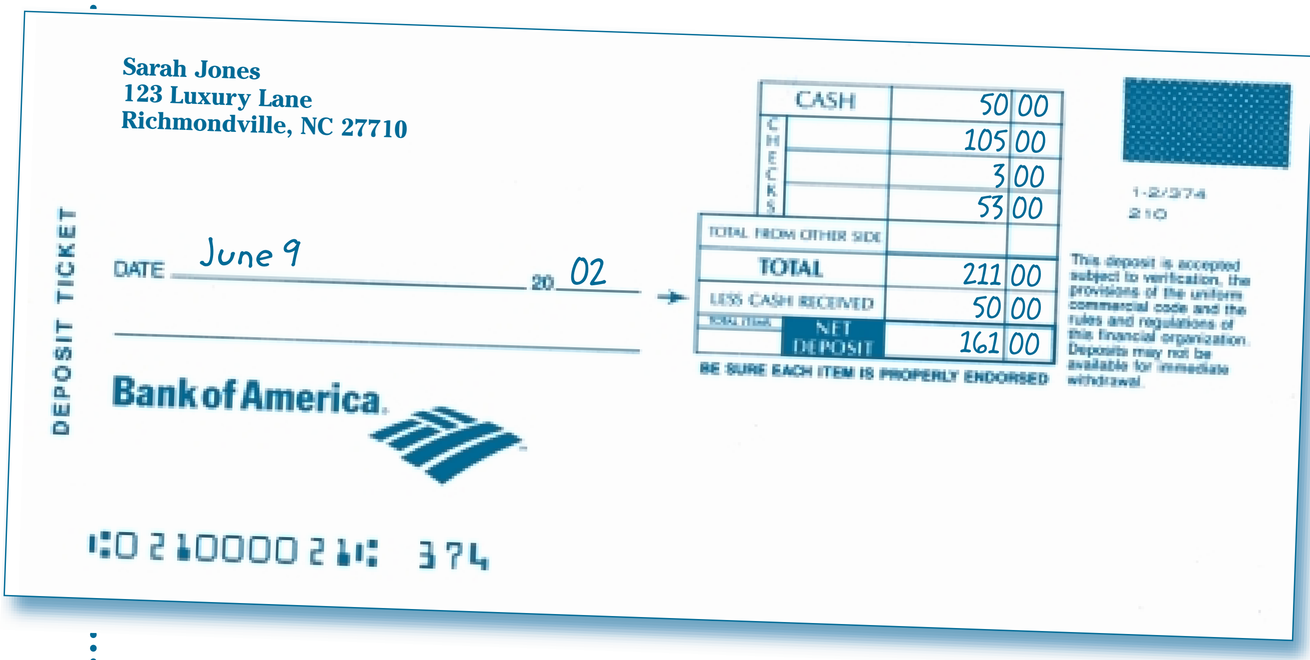


ILLUSTRATION 21.1

A Completed Deposit Ticket

Look at the sample deposit ticket as you read the procedures for filling one out.

1. Write the current date.
2. Write the amount of currency and coin to be deposited in the area for "cash."
3. If checks are being deposited, write the amount of each check separately in the area for checks.
4. Total the cash and checks and write that amount in the "total" box.
5. If you wish to receive cash back (usually when you are depositing only checks), write the amount in the "less cash received" box.


Sarah Jones
123 Luxury Lane
Richmondville, NC 27710

DEPOSIT TICKET

DATE June 9 20 02

CASH	50	00
CHECKS	105	00
	3	00
	53	00
TOTAL FROM OTHER SIDE		
TOTAL	211	00
LESS CASH RECEIVED	50	00
NET DEPOSIT	161	00

BE SURE EACH ITEM IS PROPERLY ENDORSED

1-2/374
210

This deposit is accepted subject to verification, the provisions of the uniform commercial code and the rules and regulations of this financial organization. Deposits may not be available for immediate withdrawal.

Bank of America

⑆0210000 21⑆ 374

ILLUSTRATION 21.2

The Finer Points of Writing a Check

Look at the sample check as you read the procedures for filling one out.

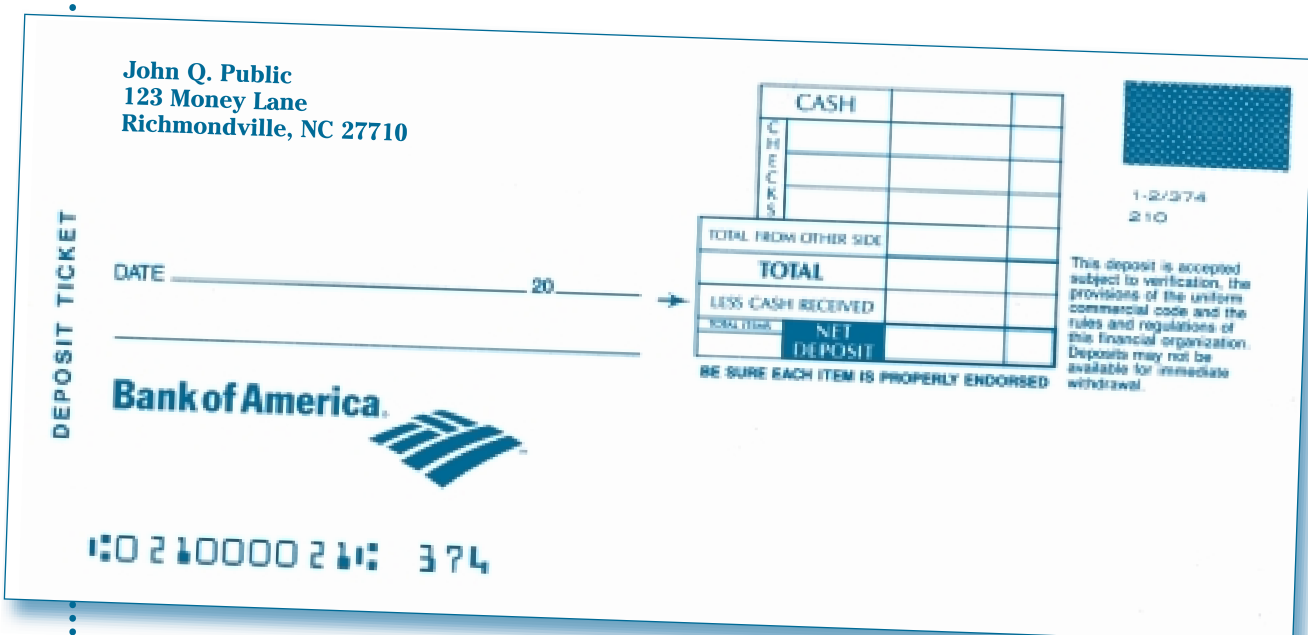
1. Write the current date.
2. Write the name of the person or company you would like to pay. This person is called the payee.
3. Enter the amount of the check in numbers, including a decimal point and cents. Start the numbers as close to the dollar sign as possible.
4. Enter the amount of the check in words. Start writing from the far left side of the line. Follow the dollar amount by the word *and*, then write the cents amount as a fraction, over 100. (If there are no cents, use 00.) Draw a line from the end of your writing to the end of the line so there is no additional room to insert words or numbers.
5. Sign your check the same way you signed the signature card when you opened your account.
6. Write the purpose of the check. You may also use this space to write the account or invoice number of the bill you are paying.

EXERCISE 21.3

Keeping a Checking Account

Instructions: Suppose that you have a checking account. Imagine that you are writing checks to businesses listed below and depositing money in the checking account. Complete the checks and the deposit tickets correctly and keep a record of each transaction in the check register.

March 1	Opened account with $250 deposit.
March 7	Paid $30 to CD Sales to buy some CDs which were on sale.
March 8	Paid $50 for sweater to A. J. Vitullo Company.
March 10	Paid $45.10 to the Acme Bicycle Shop for repairs to bicycle.
March 12	Paid Happy Pets Store $10.00 for pet supplies.
March 14	Deposited $50 gift money into account.
March 16	Paid $16 to Lawson High School for two tickets to area basketball game.
March 18	Took $50 out of account for spending money.


DEPOSIT TICKET

John Q. Public
123 Money Lane
Richmondville, NC 27710

DATE ____________________ 20____

CASH		
CHECKS		
TOTAL FROM OTHER SIDE		
TOTAL		
LESS CASH RECEIVED		
TOTAL ITEMS / NET DEPOSIT		

BE SURE EACH ITEM IS PROPERLY ENDORSED

1-2/374
210

This deposit is accepted subject to verification, the provisions of the uniform commercial code and the rules and regulations of this financial organization. Deposits may not be available for immediate withdrawal.

Bank of America

⑆021000021⑆ 374

DEPOSIT TICKET

John Q. Public
123 Money Lane
Richmondville, NC 27710

DATE ______________________ 20____

____

Bank of America

CASH		
CHECKS		
TOTAL FROM OTHER SIDE		
TOTAL		
LESS CASH RECEIVED		
TOTAL ITEMS / NET DEPOSIT		

BE SURE EACH ITEM IS PROPERLY ENDORSED

1-2/374
210

This deposit is accepted subject to verification, the provisions of the uniform commercial code and the rules and regulations of this financial organization. Deposits may not be available for immediate withdrawal.

⑆021000021⑆ 374

PLEASE BE SURE TO DEDUCT CHARGES THAT AFFECT YOUR ACCOUNT

CHECK #	DATE	TRANSACTION DESCRIPTION	WITHDRAWAL/ SUBTRACTIONS	✓ T	FEE IF ANY	DEPOSIT/ ADDITIONS	BALANCE


John Q. Public
123 Money Lane
Richmondville, NC 27710

0994

Date ______ 66-19/530 NC 73

Pay to the order of ______ $

______ Dollars

Security features are included. Details on back.

Bank of America

For ______ MP

053000196 000687941443 0994


John Q. Public
123 Money Lane
Richmondville, NC 27710

0995

Date ______ 66-19/530 NC 73

Pay to the order of ______ $

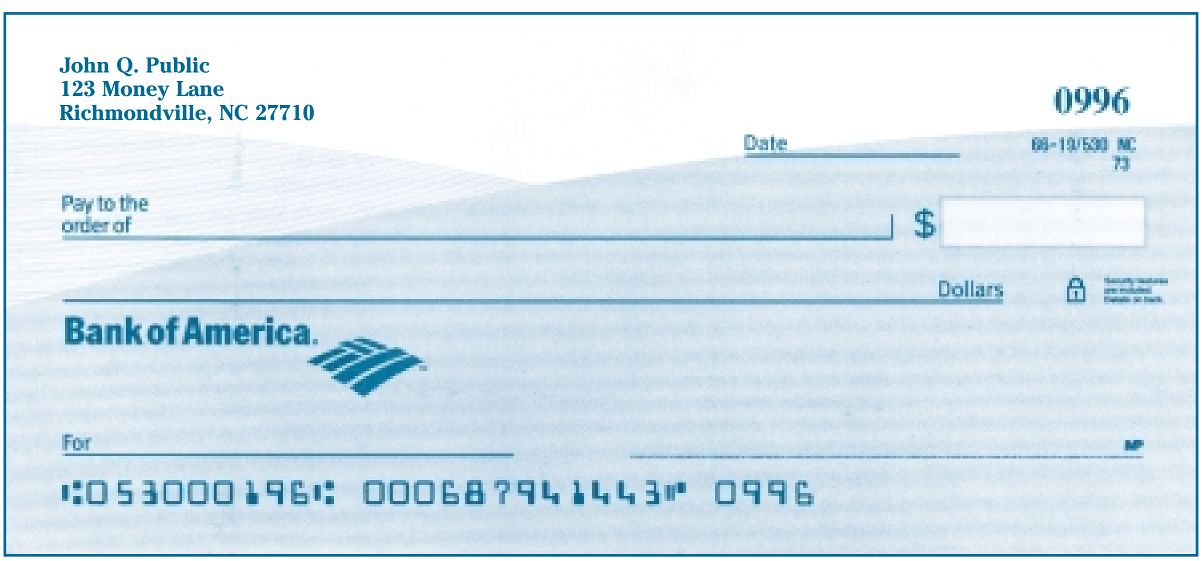
______ Dollars

Security features are included. Details on back.

Bank of America

For ______ MP

053000196 000687941443 0995


John Q. Public
123 Money Lane
Richmondville, NC 27710

0996

Date ______ 66-19/530 NC 73

Pay to the order of ______ $

______ Dollars

Security features are included. Details on back.

Bank of America

For ______ MP

053000196 000687941443 0996

John Q. Public
123 Money Lane
Richmondville, NC 27710

0997

Date ____________ 66-19/530 NC 73

Pay to the order of ____________ $ ______

______________________________ Dollars

Bank of America.

For ____________ ____________ MP

⑆053000196⑆ 000687941443⑈ 0997

John Q. Public
123 Money Lane
Richmondville, NC 27710

0998

Date ____________ 66-19/530 NC 73

Pay to the order of ____________ $ ______

______________________________ Dollars

Bank of America.

For ____________ ____________ MP

⑆053000196⑆ 000687941443⑈ 0998

John Q. Public
123 Money Lane
Richmondville, NC 27710

0999

Date ____________ 66-19/530 NC 73

Pay to the order of ____________ $ ______

______________________________ Dollars

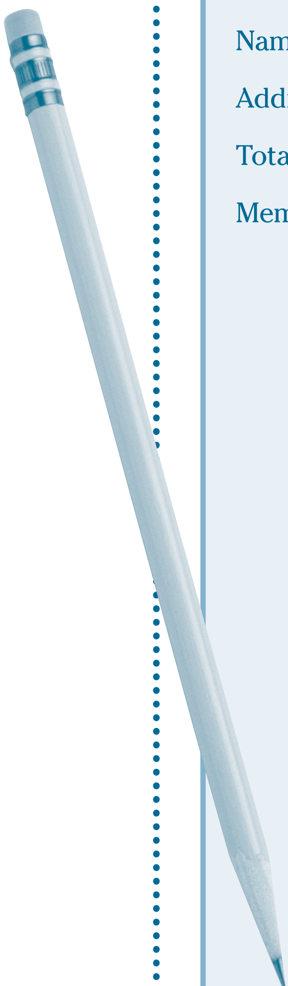
Bank of America.

For ____________ ____________ MP

⑆053000196⑆ 000687941443⑈ 0999

EXERCISE 21.4

Financial Services Survey



FACTS ABOUT FINANCIAL INSTITUTIONS

Name of financial institution ____

Address ____

Total number of locations __________ Hours/days ______________________________

Membership or other qualifications required to do business _______________________

Type of institution *(check one)*
- ❑ Bank
- ❑ Brokerage firm
- ❑ Credit union
- ❑ Savings & loan association

Survey conducted *(check one)*
- ❑ By phone
- ❑ In person
- ❑ Other ____________________

Check all financial services that this institution offers:

Deposit services
- ❑ Checking accounts
- ❑ Savings accounts
- ❑ Certificates of deposit (CDs)
- ❑ Direct deposit and automatic withdrawal
- ❑ Deposit insurance (such as FDIC)
- ❑ Automated teller machines (ATMs)

Credit services
- ❑ Credit cards
- ❑ Installment loans
- ❑ Lines of credit
- ❑ Mortgages
- ❑ Home equity loans
- ❑ Student loans
- ❑ Small business loans

Investment services
- ❑ Retirement accounts (IRAs, SEPs, KEOGHs)
- ❑ Stocks and bonds
- ❑ Mutual funds

EXERCISE 22.1

Choices and Risks

All choices involve risk. Let's consider driving a car. Everyone knows that there is always a risk of having an accident. You could cause an accident yourself or another driver could cause an accident that involves you. How can you reduce the risk of having an accident when driving? You have three choices. First, you can choose to stop driving. Ride the bus, ride a bike, or walk. Even though you are not required to drive, the no-driving alternative may seem extreme to you. Let's examine the remaining choices.

Second, you can become a safer driver. Take a course in defensive driving. Study the state road-safety manual. Pay attention in driver's education. Avoid driving during rush hours on dangerous roads and late at night. Third, you can purchase auto insurance. You can purchase insurance to protect you from financial loss for car repairs, medical costs, or lawsuits that result from an accident. You may still have a wreck, but the consequences will not be as bad as they would have been if you did not have insurance.

Your choices about driving are similar to many others. Usually your best way of reducing risk is to take actions yourself to reduce risks. For example, to reduce health problems, eat right, get plenty of exercise, get enough sleep, avoid drugs, and so forth. Buying health insurance is another way to reduce health-care cost risks. To reduce the chances of theft, install good locks, stop mail and newspaper deliveries when you are away, and keep areas around your house or apartment well lit. Buying homeowner's or renter's insurance is another way to reduce the risk of financial loss from theft.

The purpose of insurance is to spread out risks over many people. Let's consider an example. Imagine that the student council in a high school of 1,000 students wants to offer all students insurance against the theft of personal possessions from school lockers. The student council has decided to establish a locker insurance company. Suppose that students in this school have an average of $50 worth of personal stuff in each locker. Suppose further that an average of 10 in every 1,000 lockers are broken into each year. In a typical year, students in the school lose a total of $500 ($50 of stuff x 10 locker break-ins) in locker theft. If all 1,000 students wish to buy insurance, it would cost:

$$\frac{\text{\$500 loss}}{\text{1000 students}} = \text{\$.50 charge for each student for locker insurance}$$

If every student bought $.50 worth of locker insurance, they would be covered from financial damage due to locker break-ins. This is fundamentally how insurance companies work. Insurance companies charge a fee (a premium) paid by customers to provide protection against certain types of losses. The fee or premium would not only cover the losses but also the costs of operating the business and a profit.

Table 22.1 shows types of insurance you can buy for different types of risk. Study the table and you will be able to answer the questions at the end.

TABLE 22.1

Types of Insurance

Type of Insurance	Purpose	Examples of Coverage
AUTO	Provides financial protection from losses due to an auto accident or other damage to a car.	**Collision:** Provides for the repair or replacement of the policy owner's car damaged in an accident. **Liability:** Covers the cost of property damage or injuries to others caused by the policy owner. **Comprehensive:** Covers the cost of damage to an auto as a result of fire, theft, or storms.
HEALTH	Provides payment for certain health-care costs.	**Basic health:** Covers office visits, laboratory, hospital costs and routine care. **Major medical:** Protects against large bills from catastrophic illness or injury. **Dental and vision:** Covers some cost of routine exams and specific services.
RENTER'S	Provides financial protection in case of loss of personal possessions in a rental unit.	Reimburses policy owner for loss of possessions in a rental unit due to fire, theft, water damage, etc.
HOMEOWNER'S	Protects against financial loss from damage to your home or its contents, as well as injury to others on the property.	**Physical damage:** Reimburses for fire or water damage to house or other structures on the property. **Loss or theft:** Reimburses for personal property damaged or stolen. **Liability:** Protects against loss from a lawsuit for injuries to invited or uninvited guests.
LIFE	Provides financial protection to dependents of policy owner when policy owner dies.	**Term life:** Offers protection for a specified period of time. **Whole life:** Offers protection that remains in effect during the lifetime of the insured and acquires a cash value.
DISABILITY	Provides income over a specified period when a person is ill or unable to work.	Policy owner selects a replacement income for lost wages if an illness or accident prevents the person from working. Disability income is paid for a specified time after a waiting period.

Questions

1. All choices involve risks. Name two ways to reduce risks.

2. How does insurance work?

3. What is a premium?

4. What does each type of insurance provide?

- **Auto:**
- **Health:**
- **Renter's:**
- **Homeowner's:**
- **Life:**
- **Disability:**

5. In the case of auto insurance, what is the difference between collision and liability coverage?

6. In the case of health insurance, what is the difference between basic health and major medical coverage?

EXERCISE 22.2

The Big Risk

You have just graduated from high school or college, and you are single. You own a number of assets that you are thinking of insuring, including an automobile, inherited jewelry, a rare coin set, and the contents of your rented apartment.

Your employer provides a health insurance plan you can purchase. Examine the cost and the risk of each of the things you would like to insure below, and circle them. Do not spend more than $2,600; you may spend less. Indicate your choices below.

Renter's Insurance
(theft, fire, acts of nature)

Premium:	$100/year
Loss:	$2,800
Risk:	1 in 12
Card:	9
Deductible:	$250

Jewelry Insurance

Premium:	$45/year
Loss:	$3,400
Risk:	1 in 12
Card:	7
Deductible:	None

Automobile Insurance
(collision, comprehensive, liability)

Premium:	$1200/year
Loss:	$4,600
Risk:	8 in 12
Card:	5 - 12
Deductible:	$250

Health Insurance
(doctor visits, surgery)

Premium:	$650/year
Loss:	$1,200
Risk:	10 in 12
Card:	2 - 12
Deductible:	$10 co-payment

(Assuming 2 visits per year)

Life Insurance
(death)

Premium:	$300/year
Loss:	$100,000
Risk:	*below* 1 in 12
Card:	Must draw two 12s in a row
Deductible:	None

Rare Coin Insurance
(loss due to theft)

Premium:	$170/year
Loss:	$1,000
Risk:	1 in 12
Card:	4
Deductible:	None

Disability Insurance
(long-term injury, illness)

Premium:	$600/year
Loss:	$14,400
Risk:	7 in 12
Card:	6 - 12
Deductible:	None

My choices

Type of insurance	Premium

Adding Up Insurance

Card chosen 1	Year 2	Annual Premiums of Insurance Coverages You Chose 3	Losses Due to Unexpected Events When Insured (Deductibles, Co-pays) 4	Losses Due to Unexpected Events When Uninsured 5	Total Dollar Costs 6
EXAMPLE 1 6		0	0	$20,200	$20,200
EXAMPLE 2 6		$1,800 ($1,200 car insurance + $600 disability insurance)	$250 (Automobile Deductible) $0 (Disability)	$1,200 (Health)	$3,250
	1.				
	2.				
	3.				
	4.				
	5.				

TOTAL: ______________________

Questions for Discussion

1. How much were your losses over the period of the simulation?

2. What were the consequences of the insurance choices you made?

NOTES