Chapter 1: The Financial Planning Process

1.1 What is Personal Financial Planning?

**LEARNING OBJECTIVE:** Describe the personal financial planning process, and explain how the elements of a comprehensive financial plan fit together.

- Why Study Personal Financial Planning?
- What Are the Benefits of Personal Financial Planning?
- Why Do People Avoid Financial Planning?
- What Problems Can Be Caused by Poor Financial Planning?

**The Personal Financial Planning Process**

- Step 1: Organize Your Financial Information and Set Short-Term and Long-Term Goals
- Step 2: Analyze Your Current Financial Status
- Step 3: Identify and Evaluate Alternative Strategies for Achieving Your Goals
- Step 4: Implement Your Financial Plan
- Step 5: Monitor Your Progress and Revise Your Plan as Needed

**Case Study 1.1** The Naughtons Revise Their Financial Plan after a Job Loss

**Elements of a Comprehensive Financial Plan**

2.1 Organizing Your Financial Information

**LEARNING OBJECTIVE:** Develop a system for financial record-keeping, and prepare a personal balance sheet.

- What Financial Records Do You Need to Keep?
- Will You Need Them in the Future?
- How Long Should You Keep Them?
- Where Should You Keep Them?

**Summarizing Your Financial Condition**

- How Much Are You Worth Today?
- Organizing the Personal Balance Sheet
- Valuing Your Assets and Debts

**Case Study 2.1** Danielle Washington Develops a Balance Sheet

**2.2 Evaluating Your Personal Financial Situation**

**LEARNING OBJECTIVE:** Prepare a personal cash flow statement, and evaluate your financial situation using financial ratios.

**The Personal Cash Flow Statement**

- Cash Inflows
- Cash Outflows
- Net Cash Flow

**Case Study 2.2** Danielle Washington’s Personal Cash Flow Statement

**Using Financial Ratios**

- Measuring Liquidity
- Measuring Debt Usage
- Measuring Savings Adequacy
- How Do You Compare?

**2.3 The Time Value of Money**

**LEARNING OBJECTIVE:** Explain how compound interest benefits investors.

**The Power of Compound Interest**

**Time Value Calculation Methods**

- Three Ways to Calculate Time Value
- Using Timelines to Clarify the Timing of Cash Flows

**Future Value: How Much Will My Money Grow?**

- Future Value of a Lump Sum
- Future Value of an Annuity

**2.4 Present Value: How Much Do I Need Today to Reach a Future Goal?**

**LEARNING OBJECTIVE:** Calculate present value of funds to be received or paid in the future.

**Present Value of a Lump Sum**

**Present Value of an Annuity**

**Loan Payments**

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Chapter 3: Budgeting and Cash Management
Chapter 4 Tax Planning

4.1 The Federal Income Tax System

**LEARNING OBJECTIVE:** Understand the major features of the federal income tax system.

The Progressive Nature of the U.S. Tax System
Marginal Tax Rates
  - Tax Rate Schedules
  - Marginal versus Average Tax Rates
  - Inflation Indexing of Tax Brackets
Consider the Marginal Tax Effect in Making Financial Decisions

4.2 Filing Requirements

**LEARNING OBJECTIVE:** Determine whether you need to file a federal income tax return and which forms you should use.

Filing Status
  - Adjusted Gross Income and Taxable Income
  - IRS Forms

4.3 Federal Income Tax Calculation

**LEARNING OBJECTIVE:** Prepare a basic tax return.

Reporting Income
  - Total Income
  - Adjusted Gross Income
Deductions and Exemptions
  - Standard Deduction
  - Itemized Deductions
  - Exemptions
Calculation of Taxes Owed
  - Tax Table and Tax Schedules
  - Tax Credits
  - Does the Alternative Minimum Tax Apply?
  - Additional Taxes Owed by the Self-Employed
Determining Taxes Due or Refund to Be Received
Case Study 4.1 Will the Riveras Receive a Tax Refund?

4.4 Tax Planning Strategies

**LEARNING OBJECTIVE:** Establish financial planning strategies to legally minimize the taxes you pay.

Maximize Pre-tax Contributions to Qualified Benefit Plans
Reduce Applicable Tax Rate on Certain Income
Make Use of Available Deductions and Credits
Avoid Audits and Penalties
  - Enforcement of Tax Laws
  - What Are the Odds of Getting Audited?
  - Complexity of the Tax System

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Chapter 5 Credit

5.1 What is Consumer Credit?

**LEARNING OBJECTIVE:** Describe the role of consumer credit in your financial plan.

Types and Sources of Consumer Credit
  - Closed-End versus Open-End Credit
  - Sources of Consumer Credit
Ethics in Action: What’s the Harm in Payday Loans?
The Advantages and Disadvantages of Consumer Credit
  - Advantages of Consumer Credit
  - Disadvantages of Consumer Credit
5.2 Your Consumer Credit Plan

LEARNING OBJECTIVE: Maintain your creditworthiness, and understand your consumer credit rights.

Measuring Your Credit Capacity
- Using Financial Ratios to Measure Credit Capacity
- The Five C's of Credit
- Understanding Your Credit Score

When and How to Use Consumer Credit

Strategies for Reducing Debt
- Full Information from Prospective Lender
- Clear and Accurate Billing Statements
- Limits on Interest Rate Increases and Fees
- Freedom from Discrimination
- Know Why You Were Denied Credit
- Fair and Respectful Debt Collection
- Accuracy of Reported Credit Information
- Correcting Information in Your Credit Report

Bankruptcy
- Contact Your Creditors Directly
- Consult a Professional Credit Counselor
- File for Bankruptcy
- Chapter 7 Bankruptcy
- Chapter 13 Bankruptcy

5.3 Credit Cards

LEARNING OBJECTIVE: Evaluate credit card choices based on terms and costs.

Types of Cards
- Bank Credit Cards
- Retail Credit Cards
- Travel and Entertainment Cards
- Debit Cards
- Smart Cards and New Technology

Common Credit Card Contract Terms
- Annual Fees
- Annual Percentage Rate (APR)
- Transaction, Billing, and Due Dates
- Minimum Payment
- Penalties and Fees
- Finance Charge

5.4 Consumer Loans

LEARNING OBJECTIVE: Evaluate consumer loan choices based on your financial needs, loan terms, and costs.

Common Types of Consumer Loans
- Home Equity Loans
- Automobile Loans
- Student Loans

Comparing Consumer Loan Alternatives
- Secured versus Unsecured Loans
- Interest Rates
- Payment Arrangements
- Finance Charges
- Repayment of Principal
- Early Repayment of Installment Loans
- Other Loan Repayment Plans

6.2 Should You Lease or Buy a Car

LEARNING OBJECTIVE: Decide whether to lease or buy a vehicle, and negotiate the terms for purchase and financing.

Leasing versus Buying
- What is a Lease?
- What Determines the Cost of an Auto Lease?
- Closed-End versus Open-End Leases
- Lease Contracts

Negotiating the Auto Purchase Price
- Components of Auto Dealer Profit
- Negotiation Strategies

Making Consumer Complaints

6.3 Making Housing Decisions on a Budget

LEARNING OBJECTIVE: Evaluate your housing needs and budget.

Housing Needs over the Life Cycle

The Rent-versus-Buy Decision
- Types of Housing
- The Costs of Renting versus Buying
- Legal Issues for Tenants

How Much House Can You Afford?
- The Nonfinancing Costs of Home Ownership
- The Down Payment
- Expected Closing Costs
- Maximum Loan Amount and House Price

6.4 Mortgage Financing

LEARNING OBJECTIVE: Evaluate mortgage financing alternatives.

What is a Mortgage?
- Common Characteristics of Mortgage Loans
- Resale of Loans in the Secondary Market
- Types of Mortgages

Factors That Affect Mortgage Payments
- Interest Rate
- Term of the Loan
- Points
- Other Factors

When to Refinance
- Why Refinance?
- Costs of Refinancing

Case Study 6.2 The Nguyens Consider Refinancing Their Mortgage

6.5 Completing the Real Estate Transaction

LEARNING OBJECTIVE: Identify factors that affect home prices, and explain the other costs of completing a real estate transaction.

Determinants of Real Estate Value

The Home Buying Process
- Choosing a Broker
- How a Broker is Paid
- Your Legal Relationship with a Broker
- Negotiating the Contract
- Arranging the Mortgage Financing

The Closing

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Chapter 7 Insurance Cars and Homes

7.1 Managing Personal Risks

**LEARNING OBJECTIVE:** Apply the risk management process to identify risks and decide how to manage them.

**The Risk Management Process**
- Identify and Evaluate Property and Liability Risks
- Risk Management Methods
  - Avoid the Risk
  - Reduce the Risk
  - Transfer the Risk
  - Retain the Risk

7.2 How Insurance Works

**LEARNING OBJECTIVE:** Explain how risk pooling works, and define common insurance policy terminology.

**Risk Pooling and Insurance**
- Insurance Premiums
- Insurance Policy Terminology

7.3 Managing Homeowner's and Renter's Risks

**LEARNING OBJECTIVE:** Describe the loss coverage provided by homeowner's and renter's insurance and the factors that impact premiums.

**What Risks Do Homeowners and Renters Face?**
- Property Risk
- Liability Risk

**Ethics in Action:** Dog Owner's Dilemma
- Defenses to Liability Claims

**Insuring Your Home**
- Property Coverage
- Additional Losses Covered
- Liability Coverage

**Pricing of Homeowners Insurance**
- Location and Property Characteristics
- Coverage Purchased
- Deductibles and Discounts
- Your Risk Profile

**Case Study 7.1 How Does a Bad Credit History Affect Insurance Premiums?**
- **Umbrella Liability Insurance**

7.4 Auto Insurance

**LEARNING OBJECTIVE:** Explain your choices for auto insurance coverage and what factors are likely to increase your premiums.

**State Auto Insurance Laws**
- Policy Coverage
  - The Personal Automobile Policy (PAP)

**Case Study 7.2 Which Auto Policy Will Cover the Loss?**
- No-Fault Auto Insurance

**Auto Insurance Pricing Factors**
- How Much You Drive
- How Well You Drive
- Your Risk Characteristics
- Where You Drive
- Where You Park Your Car Overnights
- What Type of Vehicle Your Drive
- Who Your Insurance Is

7.5 Buying Insurance and Making Claims

**LEARNING OBJECTIVE:** Compare insurers based on quality, service, and price before buying a policy.

**Steps to Buying Property and Liability Insurance**
- The Role of Agents and Brokers
- Comparing Insurance Policies
- Using Internet Resources to Get Price Quotes and Evaluate Insurers
- Making a Claim on Your Insurance
- What to Do If You Have an Auto Accident

Chapter 8 Life Insurance and Long-Term Care Planning

8.1 Life Insurance and Your Financial Plan

**LEARNING OBJECTIVE:** Determine how much life insurance you need.

**Life Insurance Compared with Auto and Homeowner's Insurance**
- Factors That Affect Premiums

**Case Study 8.1 When Will Carson Die?**
- The Role of Insurance Company Investments
- Intended Use of Policy Proceeds

**Life Insurance Needs Analysis**
- Income-Multiple Method
- Financial Needs Method

**Case Study 8.2 How Much Life Insurance Does Arjun and Tanya Chopra Need?**
- Factors Affecting Your Life Insurance Needs

8.2 Buying Life Insurance

**LEARNING OBJECTIVE:** Select the type of life insurance that best meets your needs.

**Choosing the Type of Policy**
- Term Life Insurance
- Permanent Life Insurance
- Buy Term and Invest the Difference?

**Choosing an Insurer**
- Financial Strength
- Stock versus Mutual

**Choosing an Agent**

8.3 Reading Your Policy

**LEARNING OBJECTIVE:** Define key terms used in life insurance policies.

**Policy Declarations**
- Key Provisions in a Life Insurance Policy

**Ethics in Action: The Ethics of Viatical Settlements**
- Settlement Options

8.4 Planning For Long-term Care Costs

**LEARNING OBJECTIVE:** Explain the choices for funding long-term care needs.

**Long-Term Care Needs Analysis**
- Sources of Funds for Long-Term Care
- Medicare
- Medicaid
- Life Insurance Policies

**Long-Term Care Insurance**
- When Is the Best Time to Buy Long-Term Care Insurance?
- Tax Considerations
- Features to Look for in Long-Term Care Insurance
- Talking with Family about Long-Term Care Insurance

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Chapter 9 Employee Benefits: Health, Disability, and Retirement Plans

9.1 The Value of Employee Benefits

**LEARNING OBJECTIVE:** Explain the value of employee benefits as a component of compensation.

**Types of Benefits Offered by Employers**

- Why Benefits are Preferable to Cash Compensation
  - Lower Underwriting Costs
  - Lower Administrative Costs
  - Lower Taxes

**Case Study 9.1** Lori Evaluates Tax Savings from Employer-Provided Health Insurance

**Comparing Job Offers Based on Salary and Benefits**

- Comparing Salaries Based on Cost of Living

**Case Study 9.2** Lori Compares Salary Offers Based on Cost of Living

**Case Study 9.3** Lori Compares Job Offers Based on Salary and Benefits

9.2 Health Insurance and Your Financial Plan

**LEARNING OBJECTIVE:** Evaluate your health-related costs, and select appropriate health insurance to meet your needs.

**Health Insurance Needs Analysis**

- Expected Health-Care Costs
- National Trends in Health-Care Costs

**Health Care Reform**

- Types of Health Insurance Plans
  - Fee-for-Service Plans
  - Deductibles and Coinsurance
  - Managed-Care Plans
  - Dental and Vision Insurance Plans
  - Trends in Plan Type

**Government-Sponsored Health Insurance**

- The Medicare Program: Health Insurance for Seniors
- Medicaid: Health Insurance for the Poor
- COBRA Continuation Coverage

9.3 Planning For Disability Income

**LEARNING OBJECTIVE:** Analyze your disability income needs, and identify sources of disability income.

**Disability Needs Analysis**

- Sources of Disability Income
  - Employer-Sponsored Disability Income Protection
  - Individual Disability Insurance
  - Workers’ Compensation
  - Social Security Disability

**Case Study 9.4** Mateo Rivera Estimates His Disability Income Needs

9.4 Employer-Sponsored Retirement Plans

**LEARNING OBJECTIVE:** Explain the benefits of participating in employer-sponsored retirement plans.

**Tax Advantages of Qualified Plans**

**Defined-Benefit versus Defined Contribution Plans**

**Features of Defined Benefit Plans**

- Benefit Formula
- Vesting
- Portability
- Government–Guaranteed Benefits
- Disability, Survivors, and Retiree Health Insurance

**Features of Defined Contribution Plans**

- What is Your Employer’s Contribution Promise?
- Can You Contribute to the Plan?
- Who Makes the Investment Decisions?
- Retirement Plans for Small Businesses
- Limits on Contributions

Chapter 10 Saving for Distant Goals: Retirement and Education Funding

10.1 Developing a Retirement Plan

**LEARNING OBJECTIVE:** Estimate retirement income needs, and develop savings goals.

- What Are Your Retirement Goals?
- How Much Will You Need to Save for Retirement?

**Estimating Retirement Expenses**

- Estimating Expected Income and Income Shortfall
- Estimating Retirement Wealth Needed
- Estimating Monthly Savings Target

**Case Study 10.1** Camilla Hardin Develops a Plan for Retirement Saving

**Why Do So Many People Avoid Retirement Planning?**

- Myopia
- Ignoring Inflation
- Focusing on Averages
- It Won’t Happen to Me

10.2 Retirement Income from Employer Plans and Social Security

**LEARNING OBJECTIVE:** Explain how employer-sponsored retirement plans and Social Security can help you meet your retirement goals.

**Income from Employer-sponsored Plans**

- Income from DB Plans
- Income from DC Plans

**Income from Social Security**

- What is Social Security, and How Is It Funded?
- Who Is Eligible to Receive Benefits
- Fully Insured Status
- Normal Retirement Age
- Early or Delayed Retirement
- Spousal Benefits
- How Much Will Social Security Pay Me?
- Will Social Security Be Around When You Retire?
- Causes of Projected Insolvency
- Prospects for Reform

**Ethics in Action:** Cost of Living Increases for Social Security Beneficiaries

10.3 Individual Retirement Savings Alternatives

**LEARNING OBJECTIVE:** Explain why individual retirement accounts (IRAs) offer advantages over taxable savings accounts and annuities.

**Individual Retirement Accounts**

- Traditional IRAs
- Roth IRAs
- Taxes on Benefits Received

**Taxable Accounts**

- The Importance of Starting Early
- Earnings on Investment Make a Big Difference

**Annuities**

- Key Features of Annuities
- Taxes and Expenses
- Health and Life Expectancy
- Home Equity Loans and Reverse Annuity Mortgages

**Not on Track to Retire?**

10.4 Planning for Education Costs

**LEARNING OBJECTIVE:** Develop a plan for funding future education costs that incorporates government savings incentives.

- How Much Will Future Education Cost?
- How Much Will You Need to Save?

**Case Study 10.2** Funding Jake Johnson’s College Education

**Education Funding Plan**

- Government Programs to Help Fund Education Expenses
- Tax-Preferred Education Savings Plans
Chapter 11 The Fundamentals of Investing

11.1 Developing a Realistic Investment Plan
LEARNING OBJECTIVE: Develop a realistic investment plan to meet your long term financial goals, taking into account budgetary constraints, transaction costs, and taxes.

First Things First: Establishing a Firm Foundation
Establishing Investment Goals
How Much Do You Need, and When Do You Need It?
Case Study 11.1 Newlyweds Set Their Investment Goals
Obtaining the Money to Invest
Key Strategies for Investment Success
Start Early and Be Consistent
Take Advantage of Favorable Tax Rules
Minimize Transaction Costs
Be an Informed Investor
Keep Accurate Records

11.2 Understanding Your Investment Choices
LEARNING OBJECTIVE: Identify and define the major types of investments.

Investing by Lending and Owning
The Advantages and Disadvantages of Lending
The Advantages and Disadvantages of Owning

Major Asset Classes
Common Stock
Bonds
Money Market Securities
Preferred Stock
Real Estate
Derivatives
Mutual Funds

11.3 The Risk-Return Tradeoff
LEARNING OBJECTIVE: Compare investment alternatives based on return and risk.

Rate of Return
Risk
How Risk Averse Are You?
Factors Affecting Risk Attitudes

Types of Investment Risk
Inflation Risk
Interest-Rate Risk
Default Risk
Liquidity Risk
Market Risk

11.4 Diversification and Performance Evaluation
LEARNING OBJECTIVE: Evaluate portfolio performance relative to a similarly diversified benchmark index.

How Diversification Works
Asset Allocation
Evaluating Performance against a Benchmark
Dow Jones Industrial Average
S&P 500 Index
Other Stock Market Indexes

Active versus Passive Investing
Can Active Investors Beat the Market?
Are Markets Efficient?
Passive Investing Strategies
Does Timing Matter to Passive Investors?

Chapter 12 Investing in Stock and Bonds

12.1 Investing in Common Stock
LEARNING OBJECTIVE: Describe the characteristics and classifications of common stock.

What is Common Stock?
Why Do Companies Issue Stock?
What Are the Rights and Obligations of Stock Ownership

Advantages of Stock Investing
No Management Responsibility
Higher Long-Run Returns
Liquidity
Diversifiable Risk

Disadvantages of Stock Investing
Risk
No Control

Classification of Common Stock
Income versus Growth Stocks
Blue Chip Stocks
Cyclical versus Defensive Stocks
Industry and Sector
Market Capitalization

Measures of Common Stock Performance

12.2 Investing in Bonds
LEARNING OBJECTIVE: Describe the characteristics and classifications of bonds.

What is a Bond?
The Purpose of Bonds

Types of Bonds
Classification by Type of Issuer
Ethics in Action: Mortgage-Backed Securities
Classification by Bond Characteristics

Bond Terminology
Prospectus
Trustee
Face Value
Maturity Date
Coupon Rate and Payment
Callable Bonds
Convertible Bonds

Bond Value
Why Do Investors Buy Bonds?
Predictable Income Stream
Matching Timing of Cash Flow Needs
Lower Risk
Diversification
Profit on Price Changes

12.3 Investing in Preferred Stock
LEARNING OBJECTIVE: Compare the features of preferred stock with those of common stock and bonds.

What is Preferred Stock?

Preferred Stock Valuation
Contract Terms Affecting Preferred Stock Cash Flows
Callability
Cumulative Dividends
Fixed versus Adjustable Dividends
Convertibility

The Benefits and Risks of Preferred Stock
12.4 Securities Markets

**LEARNING OBJECTIVE:** Describe the operation and regulation of the securities markets.

**Primary versus Secondary Market**

**Securities Exchanges**
- The Rise of Electronic Trading
- Listing of Securities

**Buying and Selling Stocks and Bonds**
- Bid and Ask Price
- Types of Orders
- Long versus Short
- Types of Brokerage Accounts

**Regulation of Securities Markets**
- Information Disclosure Requirements
- Insider Trading
- Circuit Breakers
- Other Regulations

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13.4 Speculative Investments

**LEARNING OBJECTIVE:** Explain why investments in precious metals, gems, collectibles, and derivatives are speculative.

**Precious Metals and Gems**

**Collectibles and Art**

**Financial Derivatives**
- Advantages of Investing in Derivatives
- Risks of Investing in Derivatives
- Using Derivatives to Reduce Risk

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**Chapter 14 Estate Planning**

14.1 What is Estate Planning?

**LEARNING OBJECTIVE:** Identify key components of an estate plan, and determine whether you need one.

**The Estate Planning Process**

**Who Needs an Estate Plan?**

**Key Components of an Estate Plan**

**Ethics in Action: Terri Schiavo's Life-or-Death Experience**

**Organizing Financial and Legal Documents**

14.2 Methods of Transferring Property

**LEARNING OBJECTIVE:** Explain the importance of having a valid will and arranging in advance for easy transfer of assets to your heirs.

**Preparing a Valid Will**
- Capacity to Make the Will
- Common Elements of a Will
- Should a Lawyer Draft Your Will?
- Making Changes to Your Will

**Passing Property Outside of a Will**
- Ownership of Assets
- Beneficiary Designation

14.3 Estate and Gift Taxes

**LEARNING OBJECTIVE:** Estimate the size of your estate and the taxes that would be owed upon your death.

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13.1 What is a Mutual Fund?

**LEARNING OBJECTIVE:** Distinguish different types of investment companies based on key characteristics.

**What Does a Fund Investor Actually Own?**

**Types of Investment Companies**
- Open-End Funds
- Closed-End Funds
- Exchange-Traded Funds
- Unit Investment Trusts
- Real Estate Investment Trusts

**Classification of Mutual Funds**
- Classification by Investment Objective
- Classification by Portfolio Composition

13.2 Mutual Fund Investing

**LEARNING OBJECTIVE:** Explain the advantages and costs of investing in mutual funds versus individual securities.

**The Advantages of Mutual Fund Investing**
- Diversification
- Professional Money Management
- Liquidity
- Dividend Reinvestment
- Beneficiary Designation
- Withdrawal Options

**The Costs of Mutual Fund Investing**
- Shareholder Fees
- Fund Expenses
- Comparing Costs
- Mutual Fund Classes by Fee Structure

**Selecting and Evaluating Funds**
- The Mutual Fund Selection Process
- How Many Funds?
- The Mutual Fund Transaction

13.3 Real Estate Investment

**LEARNING OBJECTIVE:** Identify the advantages and disadvantages of direct and indirect real estate investments.

**Your Home as an Investment**
- Advantages of Direct Real Estate Investment
- Disadvantages of Direct Real Estate Investment

**Indirect Real Estate Investment**
- Real Estate Investment Trusts
- Mortgage-Backed Securities
- Limited Partnership

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