

Budgeting 101



One of the greatest satisfactions in life is having a sense of control over your finances. Through careful planning and the use of simple money management techniques, you and your family can feel more confident about your ability to live within your means, handle emergencies, reduce debt, and save for the future.

Financial awareness is defined as understanding where you are, where you want to go, and what you want to do with your money. Understanding how to manage money and credit, and developing the discipline to do it well, can make a real difference in your life. The tips, guidelines, worksheets, and quizzes that follow are designed to help you understand and improve your financial situation. They are organized to help you take the four basic steps toward successful money management.

4 Basic Steps:

- 1) Assess Your Financial Situation
- 2) Set Financial Goals
- 3) Create a Budget
- 4) Commit to a Savings Plan

You Can Do It

It will take some effort to follow these steps completely. The process may require making some changes, and these changes, whether big or small, may seem difficult or awkward at first. Remember that in addition to remaining both flexible and realistic during this process, you must also be honest with yourself, believe in yourself, and be open to alternatives. You have the power to take control of your money.



STEP 1

Assess Your Financial Situation

To start your self-assessment and motivate yourself to do better, complete the following quiz. Check **A** for **Always**, **S** for **Sometimes** and **N** for **Never**.

As a rule, do you:

- | | | | |
|--|---|---|---|
| 1. Pay the rent/mortgage payment and utility bills on time? | A | S | N |
| 2. Save 10 percent of your net income? | A | S | N |
| 3. Keep three months of your net income in reserve for emergencies? | A | S | N |
| 4. Plan ahead for large expenses such as taxes and insurance? | A | S | N |
| 5. Set goals and keep a budget for your net income? | A | S | N |
| 6. Spend no more than 20 percent of your net income for credit payments, excluding home mortgage? | A | S | N |
| 7. Comparison shop for the purchase of most items? | A | S | N |
| 8. Use credit only for expensive purchases or when you have the money in the bank to cover the charge? | A | S | N |
| 9. Maintain a checking account register and balance it every month? | A | S | N |
| 10. Keep yourself financially updated by reading consumer articles? | A | S | N |

TOTAL A: ___ S: ___ N: ___

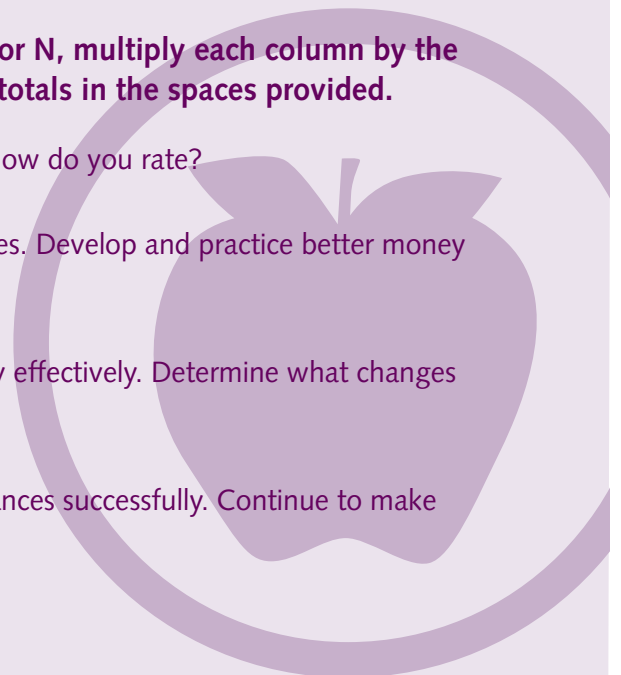
Scoring: Total up the number of times you circled A, S, or N, multiply each column by the appropriate number of points listed below and put the totals in the spaces provided.

Never = 0 Points, **Sometimes** = 1 Point, **Always** = 2 Points. How do you rate?

0 – 10 Points: Indicates a need to take control of your finances. Develop and practice better money management skills.

11 – 15 Points: Reflects a good effort to manage your money effectively. Determine what changes can be made to improve your financial well-being.

16 – 20 Points: Demonstrates the ability to manage your finances successfully. Continue to make money management a priority in your household.



Calculate Net Worth

On your financial journey, knowing where you are starting from simply means knowing what you own (assets) and what you owe (liabilities). Assets are defined as physical property, such as a home or a car, or intangible rights, such as money owed to you by someone else. Liabilities are debts that you owe to someone else such as a mortgage, an auto loan, credit card debt, or other types of loans. These are totals, not monthly payments. Below you will find a chart designed to help you estimate your net worth.

ASSETS

Cash and Equivalents

Cash \$ _____
 Checking/Savings Account \$ _____
 Cash Value: Life Insurance
 and Annuities \$ _____
 Other \$ _____

Real Property (Market Value)

Real Estate \$ _____
 Car \$ _____
 Personal Property \$ _____

Investments

Certificates of Deposit \$ _____
 Bonds \$ _____
 Mutual Funds \$ _____
 Stocks \$ _____
 Others \$ _____

Retirement Accounts

IRA \$ _____
 Pension Fund (vested bal.) \$ _____
 Other \$ _____

Other \$ _____

TOTAL ASSETS: \$ _____

LIABILITIES

Mortgage (principal only) \$ _____

Other Debt

Car Loans \$ _____
 Home Improvement Loans \$ _____
 Student Loans \$ _____
 Other Loans \$ _____
 Credit Cards \$ _____

Taxes Owed

Federal \$ _____
 State and Local \$ _____

Contractual Obligations

eg., Leases, Tuition \$ _____

TOTAL LIABILITIES: \$ _____

ASSETS \$ _____

minus(-) _____

LIABILITIES \$ _____

equals (=)

NET WORTH: \$ _____

The Outcome

A positive net worth indicates that your assets are larger than your liabilities. A negative net worth indicates that your liabilities are larger than your assets. *Pay attention to your trend year-after-year. The direction your net worth is moving says more about financial habits than one year of data alone.*

STEP 2

Set Financial Goals

Developing specific financial goals and writing them down is a key step in the money management process. Establishing goals will help you determine where you want to go financially, and recording your goals will motivate you to make the changes necessary to achieve them. Because each family member has a different perspective on what he or she considers a financial priority, it is important to make goal-setting a family affair. Create a list of financial priorities with your family and discuss the similarities and differences of these priorities. Then, decide together which items will become your goals. It is essential for every family member to commit to the agreed upon goals.

FINANCIAL GOALS WORKSHEET

Date: _____

	Goal	Target Date	Cost Estimate	Amount Already Saved/Paid	Amount Needed Per Month To Reach Goal
Short-term goals: Financial priorities that can be accomplished within one year.	1.	_____	_____	_____	_____
	2.	_____	_____	_____	_____
	3.	_____	_____	_____	_____
	4.	_____	_____	_____	_____
Mid-term goals: Financial priorities that can be accomplished in one to five years.	1.	_____	_____	_____	_____
	2.	_____	_____	_____	_____
	3.	_____	_____	_____	_____
	4.	_____	_____	_____	_____
Long-term goals: Financial priorities that may take five years or more to accomplish.	1.	_____	_____	_____	_____
	2.	_____	_____	_____	_____
	3.	_____	_____	_____	_____
	4.	_____	_____	_____	_____

STEP 3

Create a Budget

Now that you have established your financial destination by setting goals, you are faced with the task of getting there. Creating a realistic monthly budget or spending plan provides you with the vehicle to get you on your way. To create a budget, you need to know how much money is available, where the money is being spent, and what adjustments need to be made.

The Budget Process

- Record monthly income
- Record monthly expenses
- Compare income to expenses

Record Monthly Income

Document your monthly income on the Income Worksheet provided. Follow the directions, remembering to list all sources of income your household will use to offset expenses.

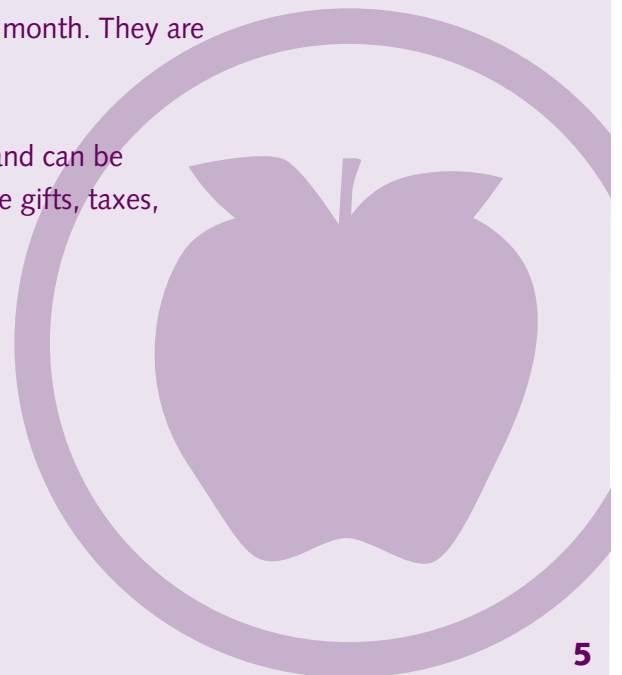
Record Monthly Expenses

Recording monthly expenses means documenting and tracking exactly what you spend your money on. Use the Expense Worksheet provided. Your expenses can be divided into one of these categories:

Fixed expenses usually do not fluctuate and require a set payment on a weekly or monthly basis. Fixed expenses are generally the most difficult to change. These include expenses like rent or mortgage payment, insurance premiums, and child care.

Variable expenses vary from week to week or month to month. They are the most flexible and can be a multitude of things.

Periodic expenses generally occur once or twice a year and can be unpredictable. They include items such as car repair, large gifts, taxes, and home maintenance.



Income Worksheet (monthly)

Step 1:

Sources of Paychecks. List all sources of monthly earned income of all individuals living in the household involved in the family budget. This should include full-time, part-time, and self-employment income.

Step 2:

Monthly Gross Income. List the amount of income received before deductions. If paid weekly, base income on four paychecks per month (48 pay periods/year). If paid every other week (26 pay periods/year), base income on two paychecks per month (24 pay periods/year). The additional paychecks in each case would be listed in Step 6 below.

Step 3:

Deductions. List all monthly deductions from each source of income. Loans owed to an employer, bank, or credit union should be listed on the Debt Load Worksheet, not here.

Step 4:

Monthly Net Income. Subtract all deductions from the monthly gross income to arrive at the monthly net income.

Step 5:

Other Monthly Income. List monthly income from other sources. Remember this is income you receive on a regular basis even though it may not be from employment. Examples: Social Security, Rentals, Disability Compensation, Temporary Assistance to Needy Families, Alimony, Industrial Compensations, Annuities, Stock Dividends, Child Support, Royalties, Allotments, Boarders, etc.

Step 6:

Additional Periodic Income. List extra paychecks, bonuses, income tax refunds, etc., divided into a monthly amount.

Step 7:

Total Monthly Net Income. Add Steps 4, 5, and 6 together for your total monthly net income. If total net income from all sources is not sufficient to accomplish your goals, look for ways of revising income and/or the expenses that are deducted from your pay. Examples: Federal income tax exemptions, insurance coverage, savings, etc.

Income Worksheet (continued)

	Household Paycheck #1	Household Paycheck #2	Household Paycheck #3	Total
1. Sources of Paychecks				
2. Monthly Gross Income				
3. Deductions				
Federal Income Tax				
FICA/Retirement				
Medical Insurance				
Life Insurance				
Dental Insurance				
Co. Stock Purchase				
Payroll Deduction Saving (401k)				
Union Dues				
Child Support				
Other				
Other				
4. Monthly Net Earned Income				
5. Other Monthly Income				
6. Additional Periodic Income				
7. Total Monthly Net Income				

Expense Worksheet (monthly)

FIXED

Rent or Mortgage Payment	\$ _____
Home Equity/2nd Mortgage	\$ _____
Health Insurance	\$ _____
Homeowners Insurance	\$ _____
Car Loan Payment	\$ _____
Auto Insurance	\$ _____
Child Support/Alimony	\$ _____
Savings	\$ _____
Other	\$ _____
Total Fixed Expenses:	\$ _____

VARIABLES

Food at Home (Groceries)	\$ _____
Meals & Snacks on Job	\$ _____
School Lunches	\$ _____
Meals Out	\$ _____
Electricity	\$ _____
Gas/Heating	\$ _____
Water/Sewer	\$ _____
Garbage/Recycling	\$ _____
Phone/Long Distance/Cellular	\$ _____
Cable/Satellite	\$ _____
Internet Charges	\$ _____
Gasoline	\$ _____
Bus Fares/Parking Tolls	\$ _____
Family Clothing	\$ _____
Dry Cleaning/Laundromat	\$ _____
Cleaning Supplies/Personal Items	\$ _____
Barber & Beauty Shop	\$ _____

VARIABLES (cont.)

Children's Allowance	\$ _____
Charitable Contributions	\$ _____
Babysitter	\$ _____
School/Tuition/Activities	\$ _____
Tobacco/Alcohol	\$ _____
Recreation	\$ _____
Books/Newspapers/Magazines	\$ _____
Videos/Books/Music/Movies	\$ _____
Hobbies/Lessons	\$ _____
Dentist	\$ _____
Medicine/Co-pays	\$ _____
Bank/Credit Union Charges/ATM	\$ _____
Child Expenses	\$ _____
Pet Expenses	\$ _____
Other	\$ _____
Total Variable Expenses:	\$ _____

PERIODIC

Taxes (Property, Excise, etc.)	\$ _____
Back-to-school	\$ _____
Car Repairs/Tires	\$ _____
Inspection/Registration	\$ _____
Gifts/Holiday Expenses	\$ _____
Maintenance/Repair	\$ _____
Home Misc.	\$ _____
Total Periodic Expenses:	\$ _____
TOTAL MONTHLY EXPENSES:	\$ _____
(-) MONTHLY NET INCOME:	\$ _____
(=) SURPLUS/DEFICIT (+ or -):	\$ _____

Compare Income to Expenses

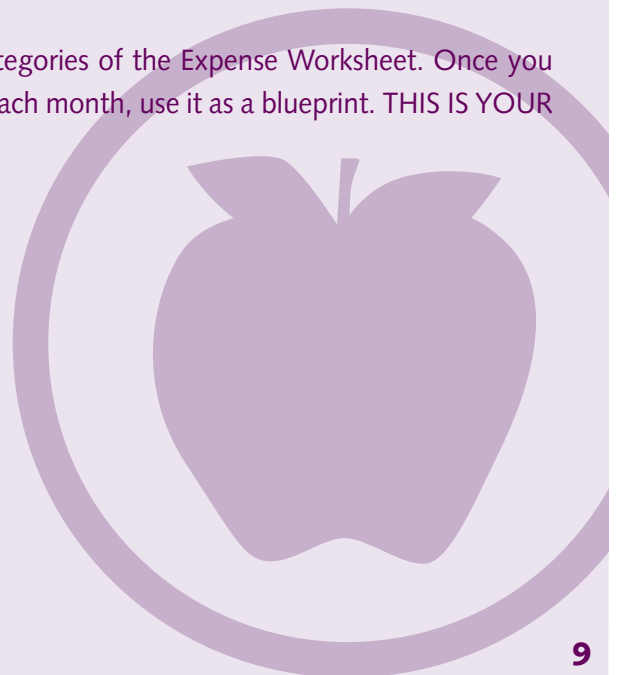
You are now ready to compare your monthly income to your monthly expenses and determine what, if any, changes are necessary. On the bottom section of the worksheet, total all of your actual fixed, variable, and periodic expenditures and subtract that figure from your Total Net Income for the month.

If your result is a positive number, this indicates that excess income exists and that your income is sufficient to support the monthly expenses you have documented. If your result is a negative number, this indicates that a shortage exists and your income is not sufficient to support your monthly expenses. With a shortage, you have three options: increase your monthly income, decrease your monthly expenses, or do a combination of both.

Decreasing your monthly expenses may be the easiest and provides the most immediate solution. Review monthly expenses using these pointers:

- Eat out less. The convenience of fast food and restaurants can cost hundreds of dollars a month—thousands of dollars a year.
- Curb habits. The daily routine of buying a \$3 cup of coffee can add up to over \$1,000 a year.
- Comparison shop. For household goods and groceries, check the unit per weight or number quantity price. Look for sales on items you need to purchase.
- Shop with a list. Resist impulsive buying.
- Trade in your car for a more fuel-efficient vehicle or carpool to reduce gas expenses.
- Evaluate the importance (and true need) of everyday luxuries such as cell phones, cable TV, entertainment, nonessential clothing, and designer haircuts.

As you make reductions, adjust the figures in the appropriate categories of the Expense Worksheet. Once you have balanced the equation so the income covers your expenses each month, use it as a blueprint. THIS IS YOUR BUDGET!



Budgeting Works

Successful money management begins with the creation of a household budget. Although the process may seem difficult and time-consuming, it is vital for gaining control of your finances as well as reaching your financial goals.

A working budget is more than a formula for the spending of future income. It becomes the family's plan for saving as well as spending and a road map for reaching your goals. While it requires you to estimate your available income and to make decisions about spending those funds, your budget will help you implement a money management plan for your future.

A successful budget should:

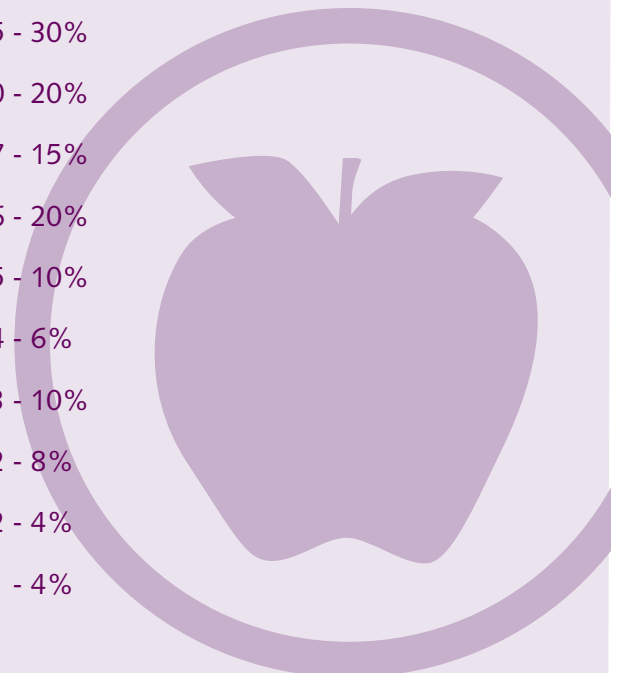
- Help increase savings
- Prevent impulsive spending
- Determine what you can afford
- Identify expenses that can be reduced
- Help repay debt

There is no single “budget formula” that is successful for all households. Every household chooses to spend money in its own way, to meet its own needs. The secret to successful budgeting is to develop a realistic plan that is workable for your family and unique circumstances, and then follow it.

Budget Allocation Guide

The allocation range below is a guide. You should not exceed the maximum range for any of these categories.

<u>Category</u>	<u>Range</u>
Housing	35 - 40%
Food	15 - 30%
Personal Debt	10 - 20%
Utilities	7 - 15%
Transportation	6 - 20%
Savings	5 - 10%
Insurance	4 - 6%
Clothing	3 - 10%
Health	2 - 8%
Personal Care	2 - 4%
Misc. Items	1 - 4%



STEP 4

Commit to a Savings Plan

Saving by regularly setting aside part of your income is an essential component of any money management plan. In addition to the money set aside, saving provides the opportunity to earn money through compound interest. Savings can provide the money needed to manage regular financial obligations, and increase financial security and a sense of well-being. Develop and commit to a savings plan that includes money for these situations:

- Periodic living expenses – Each pay period, set aside the amount that is budgeted for an expense but not actually spent during that pay period. Use a savings account or interest-bearing checking account in which funds can be easily deposited and withdrawn, and will yield some interest.
- An emergency fund – Each pay period, set aside the amount that is budgeted until the goal of a 3–6 month living expense cushion is achieved. Put it into a short-term Certificate of Deposit (CD) or a Money Market account.
- Short-, mid-, and long-term goals – Set aside money each month to fund financial goals. Select an interest bearing account for the short range goals, and a savings instrument, such as a CD, for saving between nine months and two years. If saving for more than two years, consult an investment advisor for more options.

Money can be saved or invested—and there are differences between the two. Both allow your money to work for you. But the differences between savings and investment products arise in the rate of return and amount of risk involved. Questions that should be considered when evaluating a savings or an investment instrument are:

- What is the interest rate?
- For how long must I invest the money?
- Can I have access to it at any time or is there a penalty if it is withdrawn early?
- Are there tax penalties if I withdraw the money early?
- What risks will be associated with my investment?

How do you calculate how fast your investments will grow? Use the Rule of 72: Any interest rate divided into the number 72 will give you the number of years necessary to double your money:

	3% = Doubles in 24 years		6% = Doubles in 12 years		9% = Doubles in 8 years	
0 years	Initial Investment	\$2,000	Initial Investment	\$2,000	Initial Investment	\$2,000
24 years	Money Doubles Once	\$4,000	Money Doubles Twice	\$8,000	Money Doubles 3 Times	\$16,000
48 years	Money Doubles Twice	\$8,000	Money Doubles 4 Times	\$32,000	Money Doubles 6 Times	\$128,000

Take Control

You've determined your budget, and you know how to get where you want to be financially. To help ensure success, ask everyone in your household to follow this personal money management commitment:

Communicate: Take the time to talk about each other's needs and wants so that everyone feels a part of the plan.

Cooperate: Be prepared to compromise and work cooperatively. Agree within the family that everyone will take turns getting what he or she wants and even giving up something that is wanted. Work toward a financial partnership.

Control: Every family member must exercise control and avoid unnecessary spending. Strive to live within the family's income and to limit the use of credit to preset limits. Make savings a family priority. Then together, you can take control of your financial future.

Internet Site Addresses

Some of the most useful Internet sites providing current information on various personal finance topics are included in the list below.

Credit Counseling:

www.moneymanagement.org
www.greenpath.com

Credit Report Information:

*By law, everyone is entitled to a **free copy** of their credit report from each bureau **once a year**. The first time you request your report, ask for all three. Moving forward, it may be beneficial to stagger your requests so that you can check on your report more frequently. Getting your credit score will require paying some kind of fee.*

www.annualcreditreport.com
www.equifax.com
www.experian.com
www.transunion.com

To be taken off credit card solicitation list:

www.dmachoice.org
www.optoutprescreen.com

Websites for general penny pinching:

www.stretcher.com
www.debtproofliving.com

To learn more, visit our online "Financial Resources" at umassfive.coop



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800.852.5886 • www.umassfive.coop

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