

# Managing Your Money

## LESSON DESCRIPTION AND BACKGROUND

This lesson introduces some basics of money management. By means of a radio call-in show script, students learn about setting up a family budget and distinguishing between income and net worth. To practice making budgeting decisions, the students make budgeting recommendations for a young family.

Lesson 8 correlates with national standards for economics and personal finance as shown in Tables 1-2 in the introductory section of the publication.

## ECONOMIC AND PERSONAL FINANCE CONCEPTS

- Budget
- Disposable income
- Fixed expense
- Net worth
- Variable expense

## OBJECTIVES

At the end of this lesson, the student will be able to:

- Identify and explain the meaning of key terms such as **disposable income**, family **budget**, **variable expense**, **fixed expense**, occasional expense, and **net worth**.
- Identify the elements of a typical monthly family budget including income, expenses, and savings.
- Make spending recommendations for a fictional young family, taking account of the costs and benefits involved.

## TIME REQUIRED

Two 45-minute class periods

## MATERIALS

- A copy for each student of **Theme 3 Introduction** from the *Student Workbook*
- Five copies of **Exercise 8.1** from the *Student Workbook*
- A copy for each student of **Exercise 8.2A**, **8.2B**, and **8.3** from the *Student Workbook*

## ADDITIONAL RESOURCES



To download visuals, find related lessons, correlations to state standards, interactives, and more visit <http://fffl.councilforeconed.org/9-12/lesson8>.

## PROCEDURE

1. Explain that the purpose of this lesson is to help the students understand some key aspects of planning their financial future. Stress the idea that decisions about how to use income are similar to other decisions. There are advantages and disadvantages to various choices. Remind the students that financial sacrifices can be difficult to make when the costs must be paid in the present and most of the benefits occur in the future.
2. Distribute a copy of **Theme 3 Introduction** from the *Student Workbook*. Ask the students to read the section to become acquainted with the concepts presented in this theme.
3. Ask for five students to volunteer to participate in a call-in show activity. Distribute a copy of **Exercise 8.1** from the *Student Workbook* to each of these students. Determine which of the volunteers will play the roles of Budget Bob, Dr. Penny Saver, Connie from Connecticut, Calvin from California, and Minnie from Minnesota. Have the students read the script in front of the class. When they have read the script, thank them for participating in the activity and ask the class the questions that appear at the end of the script. Discuss the answers with the class.

- a. What is disposable income? (**Disposable income is the money you have left to spend or save as you wish after all required deductions [e.g., taxes, Social Security, retirement-plan contributions] have been taken out of your gross pay.**)
- b. What does Dr. Saver recommend as the three parts of a family budget? (**A family budget should include a listing of income, expenses, and savings. Some students may note that savings can be included as part of family expenses. This is one way to make sure that a family makes a commitment to saving.**)
- c. What are fixed and variable expenses? Use examples to illustrate each. (**Fixed expenses are ones that are relatively constant each month, such as a house payment, rent payment, and car payment. Variable expenses are ones that are likely to change or can be changed in the short term. Examples include telephone bills, groceries, medical bills not covered by insurance, entertainment, recreation, and charge account purchases.**)
- d. What does "pay yourself first" mean? (**Some savers include their savings goal in the fixed expenses part of their budget. This means that they make a commitment to saving in the same way that they are committed to paying expenses like car and house payments.**)
- e. What is net worth? (**Net worth is a measure of wealth. It is the current value of assets minus liabilities. [Liabilities are debts you owe.]**)
4. Give each student a copy of **Exercise 8.2A** from the *Student Workbook*. Ask the students to read the background information about John and Marcia. When they have finished reading, ask the class:
- a. Who are John and Marcia? (**A young, married couple working to support one child.**)
- b. What is their lifestyle? (**They live in a comfortable apartment, enjoy some small luxuries, and keep up with all their bills.**)
- c. What is their immediate financial goal? (**To save enough money for a down payment on a second car.**)
5. Ask the students to examine the part of **Exercise 8.2A** that shows Marcia and John's fixed and variable expenses for Spending Plan 1. Ask the students to answer the questions that appear after the budgets. Discuss the answers.
- a. What are some examples of John and Marcia's fixed expenses? (**Housing, life and disability insurance, renter's insurance, automobile insurance, student loan, etc.**)
- b. What are some examples of John and Marcia's variable expenses? (**Meals, utilities, automobile fuel, medical care, child care, clothing, etc.**)
- c. John and Marcia have decided to practice the "pay yourself first" approach to saving for a second car. How do they pay themselves first? (**They have the amount that they want to save taken out of their pay automatically, as if they were paying off a fixed expense.**)
- d. Examine John and Marcia's monthly spending plan. What sacrifices do you think John and Marcia should make in their variable expenses to meet their goal? Note: at-home food expenses can't be reduced below \$220. (**Answers will vary. Accept any reasonable answers.**)
- e. What are the benefits and costs of your recommended decisions for John and Marcia? (**The benefit is that the combination of choices will allow John and Marcia to save enough for the down payment on the second car they wish to buy. The cost is giving up some of the things they would like to do and have right now.**)

**CLOSURE**

Use the following questions to review the lesson:

- What is disposable income? (**Disposable income is the money that you have left after taxes, Social Security, contributions to retirement accounts, and other required deductions have been taken out of gross pay.**)
- What are three parts of a family budget? (**A family budget should include a listing of income and expenses, plus a plan for saving.**)
- What are fixed expenses? (**Fixed expenses are ones that are relatively constant each month, such as a house payment, rent payment, and car payment. Many experts in personal finance believe savings should be treated as a fixed expense.**)
- What are variable expenses? (**Variable expenses are ones that are likely to change in the short term. Examples include telephone bills, groceries, medical bills not covered by insurance, entertainment, recreation, and charge account purchases.**)
- What is net worth? (**Net worth is the current value of assets minus liabilities.**)
- Including monthly payments for taxes and insurance (TI), what is John and Marcia's expected house payment? ( **$\$840 + \$210 = \$1,050$ , representing PITI.**)
- Do John and Marcia have enough flexibility in their budget to accommodate the additional costs of homeownership (mortgage payment, taxes, insurance, and higher utilities)? (**Not right now. Their total expenses will be  $\$5,500$ , representing fixed expenses of  $\$3,240$  and variable expenses of  $\$2,260$ . They will need to adjust some of their variable expenses to balance their budget.**)
- If not, what are some expenses they may need to reduce in order to afford the home they want? (**Accept any reasonable answers. Students should enter the new plan for variable expenses in the Homeowner column in the budget form from Exercise 8.2B.**)
- A rule of thumb for some lenders is to qualify you for a mortgage if the payments you would incur meet two criteria: a) the monthly mortgage payment with taxes and insurance will be less than 28 percent of your monthly gross income, and b) the monthly mortgage payment of principal, interest, taxes, and insurance plus other monthly consumer debt payments (such as a car loan and minimum credit card payments) will not exceed 36 percent of your gross monthly income. Would the loan that John and Marcia are considering meet these lending criteria? (**Yes.  $\$5,400 \times .28 = \$1,512$ ; the monthly PITI is expected to be  $\$1,050$ ;  $\$5,400 \times .36 = \$1,944$ ; John and Marcia's monthly PITI plus other consumer debt [car loan and credit card payment] is  $\$1,480$ .)**)
- Do you think John and Marcia can afford to pay 28 percent of their monthly gross income as a monthly house payment? Why or why not? (**Answers will vary. John and Marcia currently expect to have monthly PITI payments of  $\$1,050$ . To have this monthly payment increase to  $\$1,512$  would stretch their budget and cause them to make adjustments to their variable expenses. They**

**ASSESSMENT**

Give each student a copy of **Exercise 8.3** from the *Student Workbook*. Explain to the students that they will use information from **Exercise 8.2B** to complete the answers in this exercise. The goal of the exercise is to use the information provided to determine whether John and Marcia can afford to buy a \$150,000 home. Ask the students to read the exercise and answer the questions. Note: they will also need a copy of **Exercise 8.2B** to answer the questions. Answers are as follows:

**Answers to Exercise 8.3:**

- What would the monthly payment be for this loan? ( **$\$840$  PI; PI is Principal and Interest.**)

**would be “house poor.” They would find it difficult to purchase new home furnishings and appliances. And if they experienced an unexpected financial setback [such as the loss of a job], they might be unable, for some time, to make their house payments. It is safer to estimate how much you can afford to spend on a home using your budget than to rely on the lender’s qualifying ratios that don’t take your individual expenses into account.)**

### EXTENSION

Give each student a copy of **Exercise 8.2B** from the *Student Workbook*. It shows Marcia and John's fixed and variable expenses for Spending Plan 2. In this new situation, John and Marcia want to save money for a down payment on a home.

Ask the students to make their recommendations about how John and Marcia might reduce their expenses to achieve the goal of saving for a home. Ask them to answer the questions that follow the income and spending plan. Possible answers include the following:

- What is John and Marcia's new financial goal? **(Saving for a down payment for their first home.)**
- Examine the monthly spending plan. What sacrifices do you think John and Marcia should make in their variable expenses to meet their goal? **(Answers will vary. Accept any reasonable answers.)**
- What are the benefits and costs of your recommended decisions for John and Marcia? **(The benefit is that the combination of choices will allow John and Marcia to become homeowners. The cost is sacrificing some things they would like to do and have right now.)**