Spending Plans

What is a Spending Plan?

An income and expense statement sometimes referred to as a budget which records both planned and actual income and expenses over a period of time

A budget

Spending Plan for:		
Time Period:		
	Planned Amount	Actual Amount
Income		
Earned Income		
Wages or salary before deductions		
Unearned Income		
Money from savings and investments to help pay expenses during this time period		
Received Income from Government Programs		
Total Income	$	$
Expenses		
Deductions Often Taken from Paychecks		
Contributions to retirement programs (401k, 403b, pension, IRA)		
Federal income tax and state income tax		
Social Security and Medicare		
Saving and Investing (Pay Yourself First)		
Contribution to savings and investments		
Insurance Premiums		
Health, automobile, home or renters, life		
Housing Costs		
Transportation Costs		
Food Costs		
Family Member Care		
Communication and Computers		
Telephone landline, cell phone, Internet, cable/satellite television		
Medical Costs Not Covered by Insurance		
Clothing and Personal Care		
Educational Expenses		
Pet Care		
Entertainment		
Gifts and Charitable Contributions		
Credit Costs		
Student loan, credit card, other loan payments		
Total Expenses	$	$
Net Gain or Net Loss (Income less Expenses)	$	$

Why is a Spending Plan an important part of financial planning?
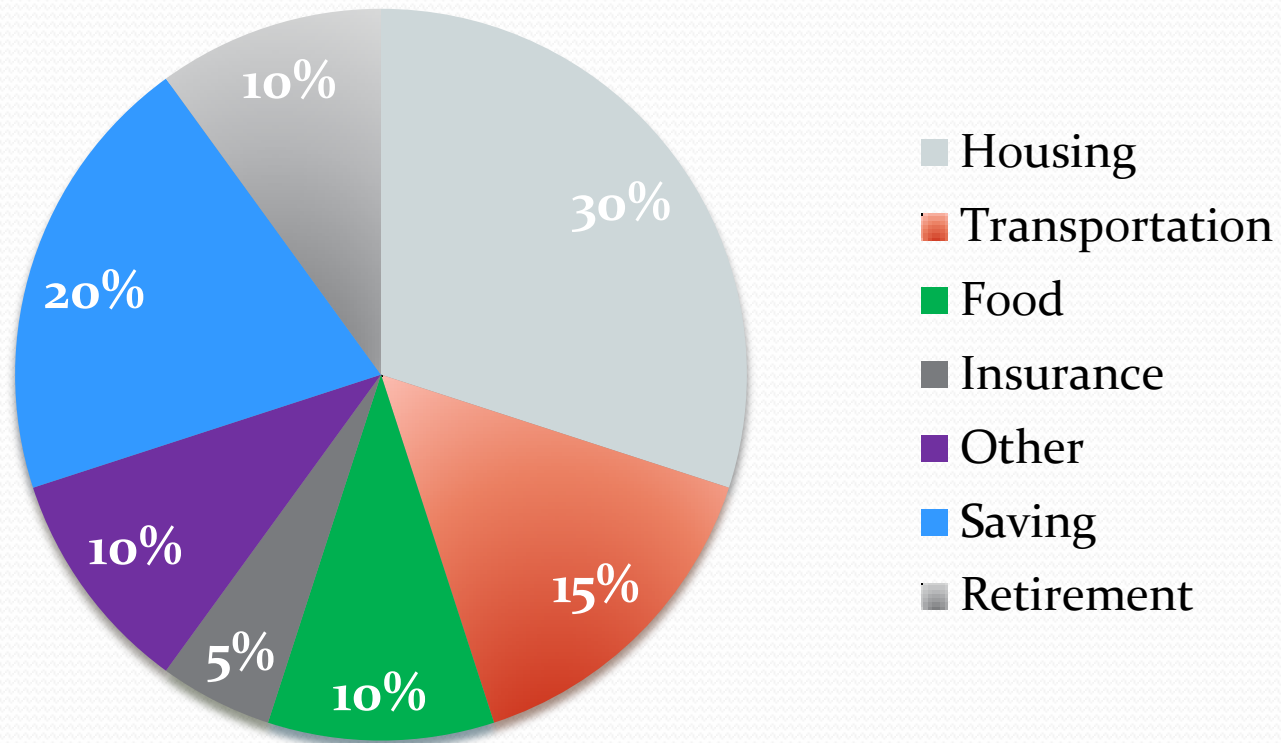
Help manage your money in a positive manner

Analyze the opportunity costs of your trade-offs to maximize financial well-being

Increase net worth

Helps set and reach goals
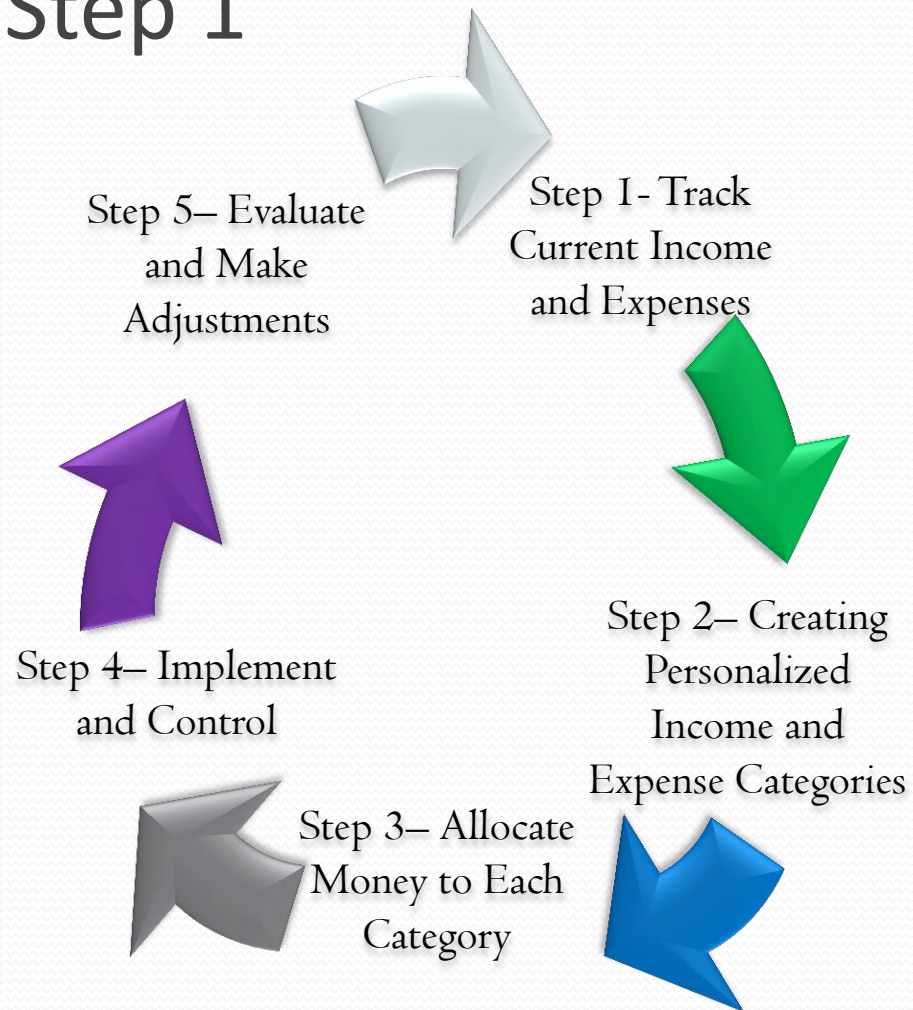
Spending Plan Pie Chart

5 Steps of Budgeting
Developing a Budget – Step 1

- **Track current income and expenses**
  - Individuals will determine what income and expenses they have within a give period of time
    - Usually concurrent with an individual's pay day
      - Monthly
      - Bi-monthly

Step 5– Evaluate and Make Adjustments

Step 1- Track Current Income and Expenses

Step 2– Creating Personalized Income and Expense Categories

Step 4– Implement and Control

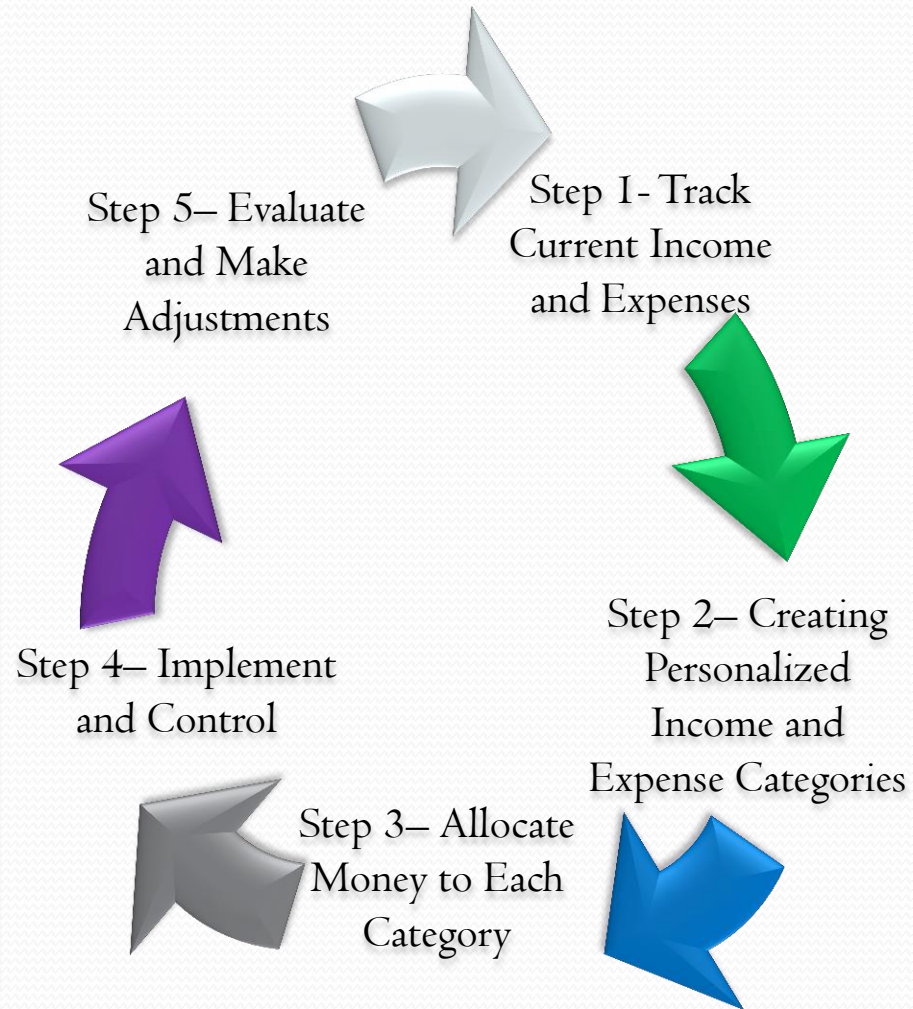Step 3– Allocate Money to Each Category

Tracking Methods

Must work for the individual!
There is not one right method!

1. Carrying a small notebook and writing down all expenses
2. Keep all receipts
3. Use a debit card if your financial institution creates spending reports for your account
4. Input information into a cell phone

# Creating personalized income and expenses categories – Step 2

- Each Budget is unique because of individual and family values
- Categories are based upon the individuals/families income and expenses

Step 5– Evaluate and Make Adjustments

Step 1- Track Current Income and Expenses

Step 4– Implement and Control

Step 2– Creating Personalized Income and Expense Categories

Step 3– Allocate Money to Each Category

Housing

- **Housing**
  - Housing is the largest of the four major expenditures
  - Approximately 30% of an individual's net income
    - **Monthly payment** (Mortgage) – A fee charged each month to live in a home
    - **Utilities** – include electricity, water, and garbage fees

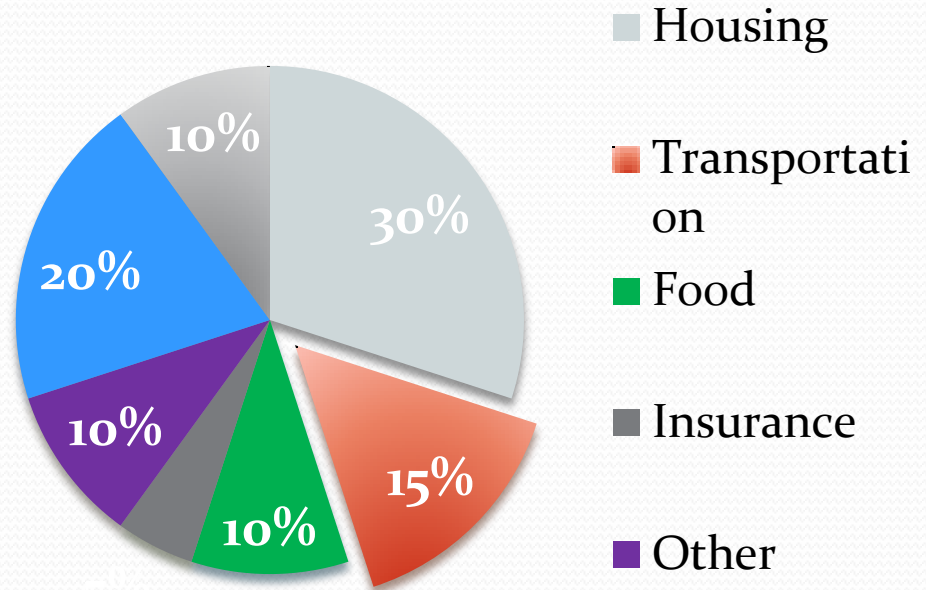- Housing
- Transportation
- Food
- Insurance
- Other
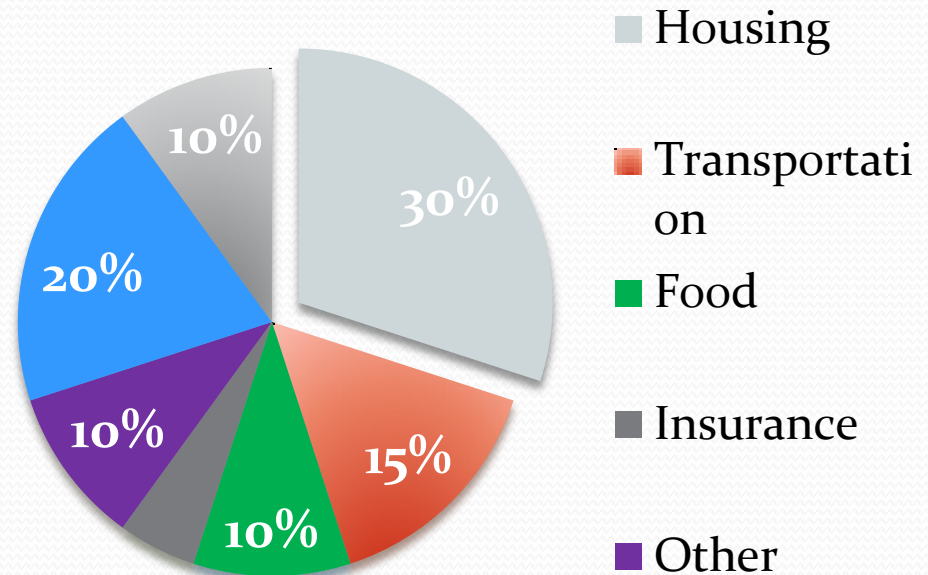
Transportation

- **Transportation**
  - The second largest major expenditures
  - Approximately 15% of an individual's net income
    - **Monthly payment** – is made if a loan is taken out to purchase a vehicle

Housing

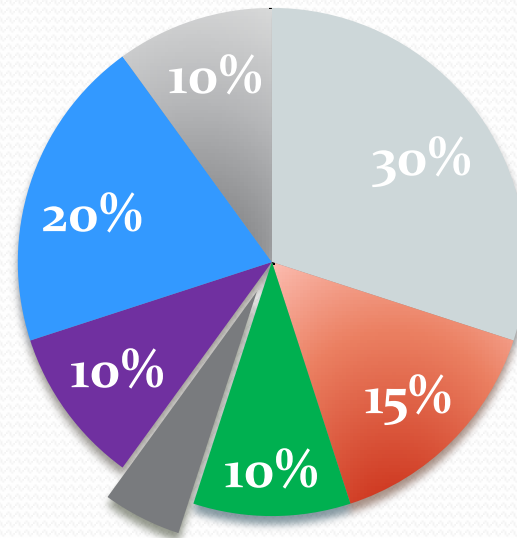Transportation

Food

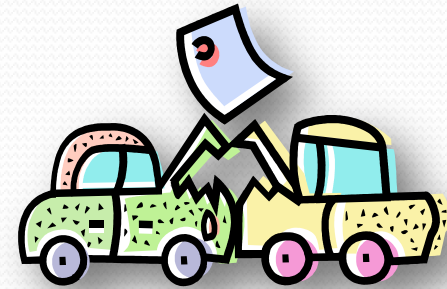Insurance

Other

30%

15%

10%

10%

20%

10%

Food

- **Food**
  - The third most expensive category within an individual's Budget
  - Approximately 10% of an individual's net income

Legend:
- Housing
- Transportation
- Food
- Insurance
- Other

Pie chart values: 30%, 15%, 10%, 10%, 20%, 10%
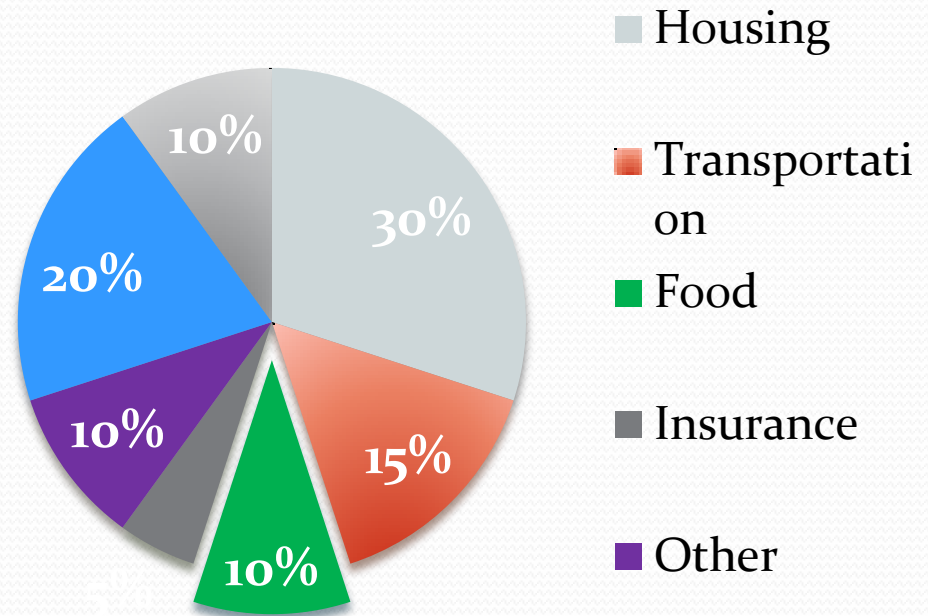
Insurance

- **Insurance**
  - Arrangement between an individual and an insurance company to protect the individual against risk
    - **Risk** is uncertainty about a situation's outcome
  - Approximately 5% of an individual's income

Housing 30%

Transportation 15%

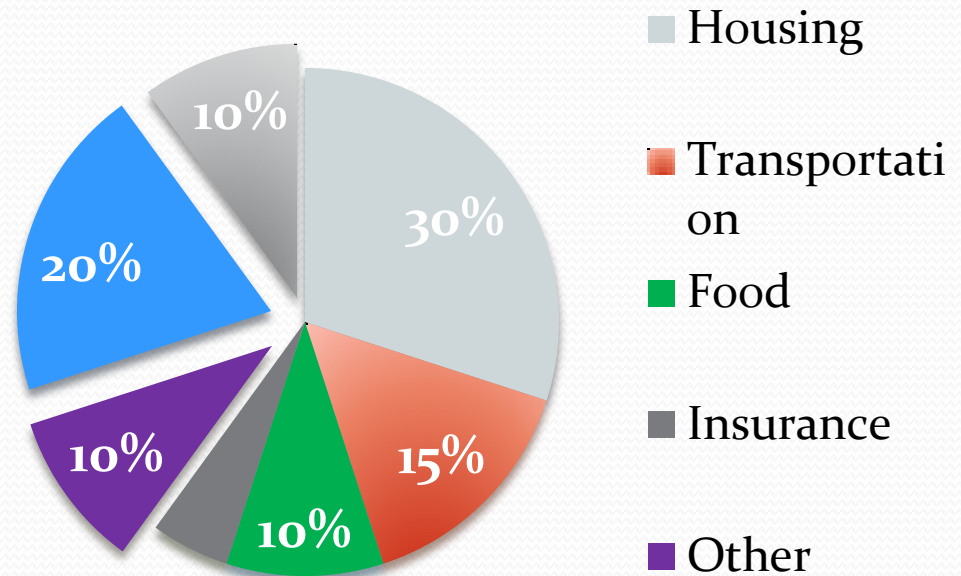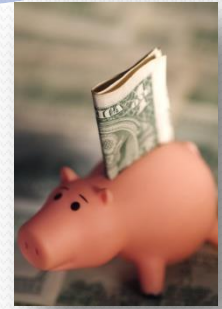Food 10%

Insurance

Other 10%

20%

10%

Additional expenses

- **Savings and investing**
  - Save 3-6 months of income that is available in a liquid account for emergencies
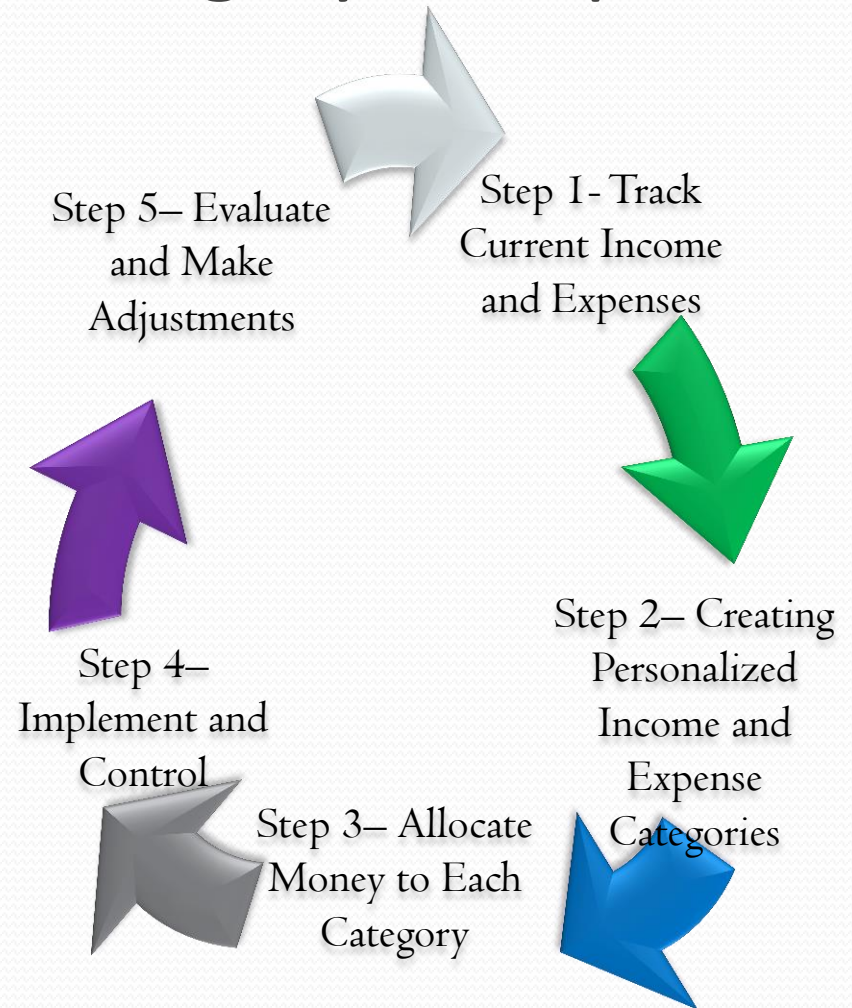- **Other**
  - Fulfills <u>additional needs</u> and accounts for 10% of an individual's net income

Legend:
- Housing
- Transportation
- Food
- Insurance
- Other

Pie chart values: 30%, 15%, 10%, 10%, 20%, 10%

Allocate money to each category – Step 3

- Reference tracking from step one to be realistic about expenditures and income
  - Think if there were any unique expenses in the past month that should be included
- Consider changes that need to be made
  - Identify ways to implement that change
- Consider financial goals and money that needs to be allocated

Step 5– Evaluate and Make Adjustments

Step 1- Track Current Income and Expenses

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When allocating money consider:

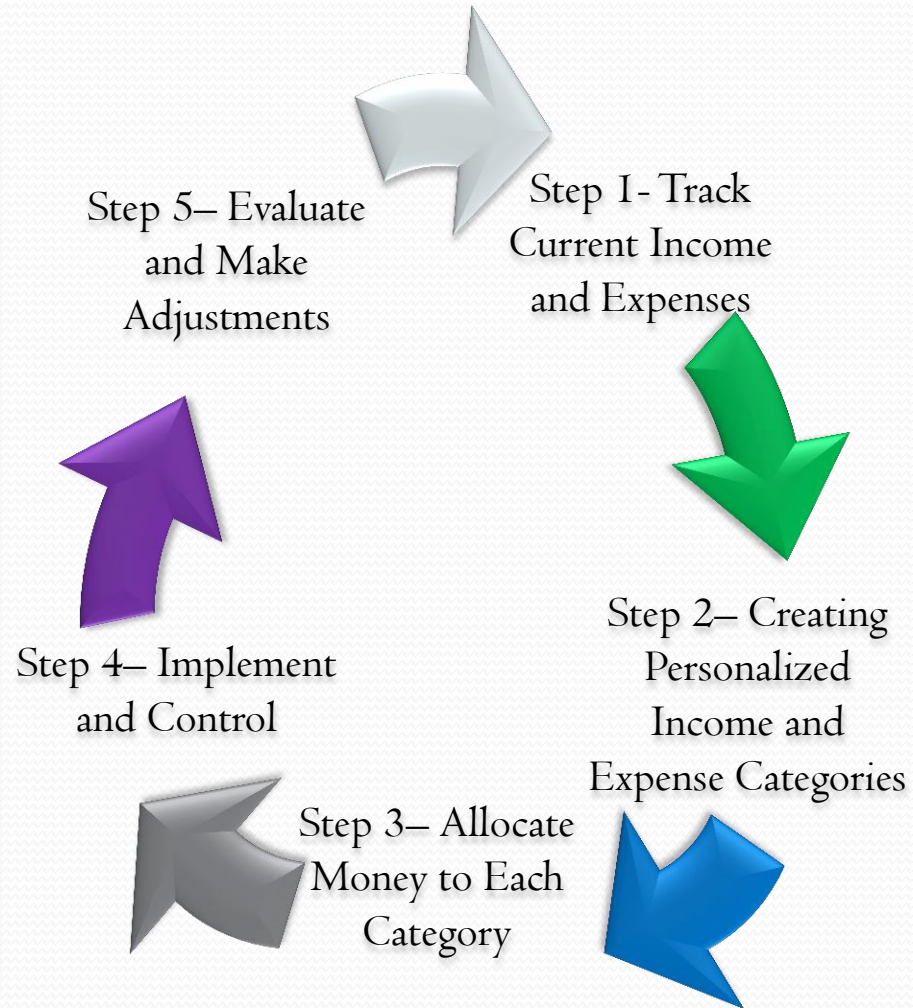| Trade-offs and opportunity costs	Goals	Contractual expenses

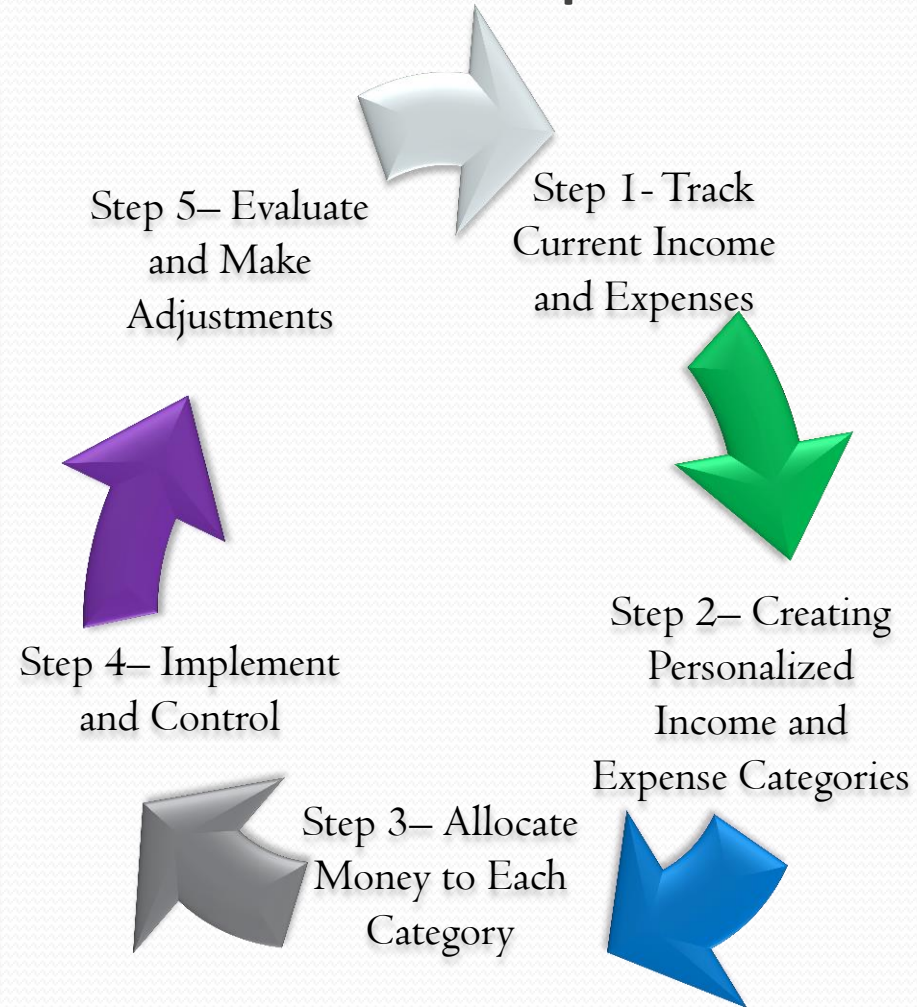| Contractual	Non-contractual
Required to pay expense for a specific amount of time - not easy to reduce or eliminate	Easy to reduce or eliminate
Rent, Internet, Cell phone	Food, entertainment

Implement and control – Step 4

- Must develop control systems to track their income and expenses
  1. **Envelope systems** – individuals place the actual budget amount of cash from a paycheck into a specific envelope system for the expense
  2. **Electronic budgeting systems** – Multiple types of software are available for consumers to use to help keep track of their financial records

Step 5– Evaluate and Make Adjustments

Step 1- Track Current Income and Expenses

Step 4– Implement and Control

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Step 3– Allocate Money to Each Category

Evaluate and make adjustments – Step 5

- Assess if Budget is working
- Make changes if necessary
- Analyze if goals are being met
- Begin the process again

Step 5– Evaluate and Make Adjustments

Step 1- Track Current Income and Expenses

Step 4– Implement and Control

Step 2– Creating Personalized Income and Expense Categories

Step 3– Allocate Money to Each Category

Bathtub Analogy

Always have more money coming in than out!
Work towards building wealth!

- **Revenue** (money in)
- **Net worth** (wealth)
- **Flexible Expenses** (money out) - can vary each month in the amount owed and are not contractual
- **Fixed Expenses** (money out) - may have a fixed amount due each month and are contractual

Wages, interest, and tips… all income is Revenue

Net worth statement
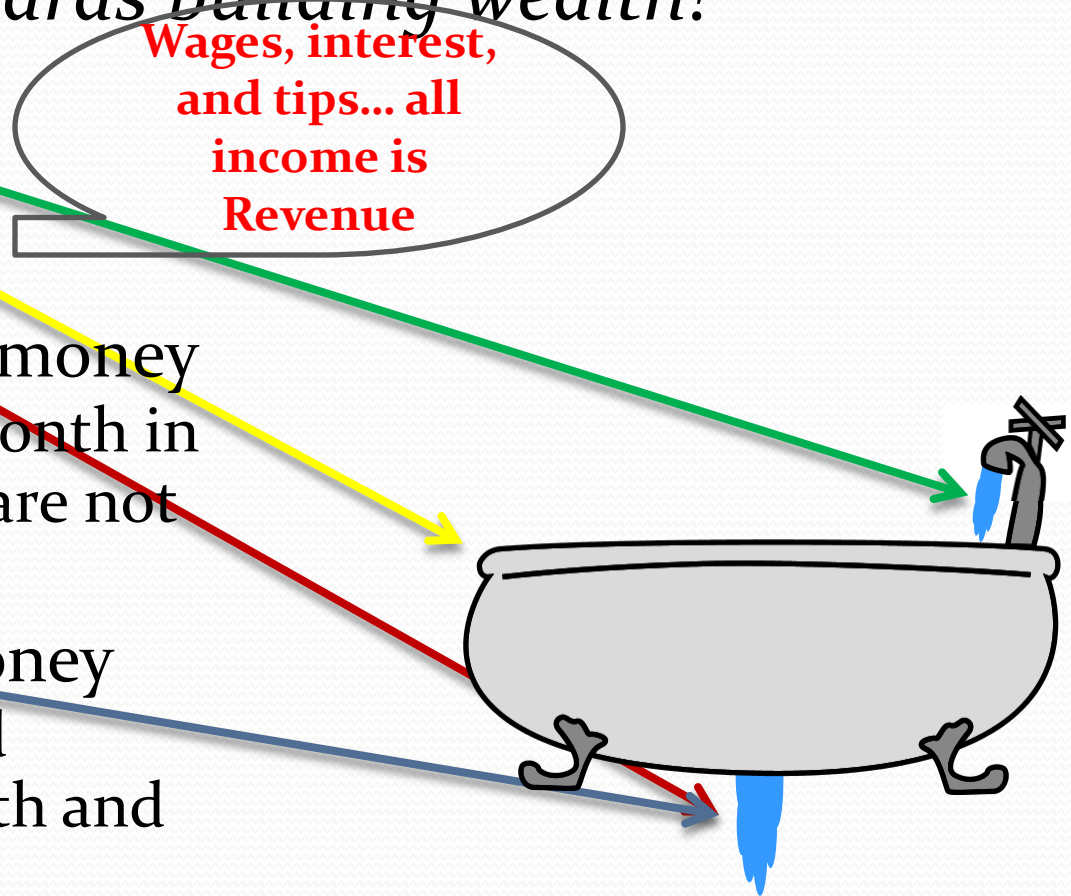
Assets	⇒	Liabilities	⇒	Net Worth

- A **net worth statement** describes an individual or family's overall financial condition on a specified date
- The components include:
    - **Assets** – Everything a person owns with monetary value
    - **Liabilities** – Debts or what is owed to others
    - **Net worth** - the amount of money left when liabilities are subtracted from assets (indicates wealth)

Who is Wealthier?

Juanita – earns $35,000 per

Assets	
Home	$60,000
Retirement	$24,000
Automobile	$8,000
Total Assets	$92,000
Liabilities	
College loan	$6,000
Mortgage	$35,000
Total Liabilities	$41,000
Net Worth	**$51,000**

Alexis – earns $100,000 per

Assets	
Home	$75,000
Retirement	$35,000
Automobile	$8,000
Total Assets	$118,000
Liabilities	
College loan	$10,000
Automobile loan	$4,000
Credit card debt	$20,000
Mortgage	$65,000
Total Liabilities	$99,000
Net Worth	**$19,000**