

# Building **W**·ealth

A BEGINNER'S GUIDE TO SECURING YOUR FINANCIAL FUTURE



FEDERAL RESERVE BANK OF DALLAS

Revised and Expanded Edition

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*Buying a home, saving for retirement or for children's education, or even effectively managing the family budget now requires more financial sophistication than ever before. Financially literate consumers make the financial marketplace work better, and they are better-informed citizens as well.*

Ben S. Bernanke, Chairman,  
Federal Reserve System

*Building Wealth: A Beginner's Guide to Securing Your Financial Future* offers introductory guidance to individuals and families seeking help to develop a plan for building personal wealth. While a comprehensive discussion of accounting, finance and investment options is beyond the scope of this workbook, it presents an overview of personal wealth-building strategies. For more information and assistance, consult the resource guide at the back. For additional copies of this workbook (also available in Spanish), call (800) 333-4460, ext. 5254, or order from the Dallas Fed's web site, [www.dallasfed.org](http://www.dallasfed.org). An animated CD-ROM version of this guide has been developed for individuals to use at their home computer or for multiple users in classrooms and computer labs. This interactive program is also available at [www.dallasfed.org](http://www.dallasfed.org).

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# Building Wealth

You can create personal wealth. It's possible to meet your financial goals. By choosing to budget, save and invest, you can pay off debt, send your child to college, buy a comfortable home, start a business, save for retirement and put money away for a rainy day. Through budgeting, saving and investing, and by limiting the amount of debt you incur, all these goals are within your reach.

## DEFINING WEALTH

Some people consider themselves wealthy because they live in a very expensive house and travel around the globe. Others believe they are wealthy simply because they're able to pay their bills on time. What we are talking about here is financial wealth and what it means to you. In the following space, write your definition.

Examples: Wealth is...

1. *being able to put my kids through college.*
2. *having enough money to buy a house.*

Wealth is...

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_

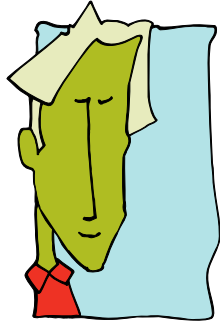
Now that you have defined what wealth means to you, how do you acquire it?

Building wealth requires having the right information, planning and making good choices. This workbook provides basic information and a systematic approach to building wealth. It is based on time-honored principles you probably have heard many times before—budget to save; save and invest; control debt; and protect the wealth you accumulate.



# ① Wealth Creation: Learn the Language

You want to create personal wealth, right? So does Bob.



Bob

Bob is 35 and works for a manufacturing company. He looked at his finances and realized that at the rate he was going, there wouldn't be enough money to meet his family's financial goals. So he chose to embark on a personal wealth-creation strategy. His first major step was to pick up a copy of this workbook for guidance. Bob began by learning the language of wealth creation. The first lesson was to understand the meaning of **assets**, **liabilities** and **net worth**. They make up this very important formula:

$$\text{ASSETS} - \text{LIABILITIES} = \text{NET WORTH}$$

*Accumulating wealth—as distinct from just making a big income—is the key to your financial independence. It gives you control over assets, power to help shape the corporate and political landscape, and the ability to ensure a prosperous future for your children and their heirs....*

Rev. Jesse L. Jackson, Sr. and Jesse L. Jackson, Jr.,  
*It's About the Money!*

A wealth-creating **asset** is a possession that generally increases in value or provides a return, such as:

- A savings account.
- A retirement plan.
- Stocks and bonds.
- A house.

Some possessions (like your car, big-screen TV, boat and clothes) are assets, but they aren't wealth-creating assets because they don't earn money or rise in value. A new car drops in value the second it's driven off the lot. Your car is a tool that takes you to work, but it's not a wealth-creating asset.

A **liability**, also called debt, is money you owe, such as:

- A home mortgage.
- Credit card balances.
- A car loan.
- Hospital and other medical bills.
- Student loans.

**Net worth** is the difference between your assets (what you own) and your liabilities (what you owe). Your net worth is your wealth.

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**The market value of a home is an asset; the mortgage, a liability. Let's say your house is worth \$120,000, but your mortgage is \$80,000. That means your equity in the home is \$40,000. Equity contributes to your net worth.**

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To calculate how much he is worth, Bob used the following formula: **Assets – Liabilities = Net Worth**. He made a balance sheet listing all his assets and all his liabilities. He listed his wealth-building assets first.

Bob discovered his net worth is \$21,600. Using Bob’s balance sheet as an example, figure your own net worth. Be sure to add any assets and liabilities you have that are not listed here. Remember that net worth is your wealth. Are you worth as much as you want to be?

Bob's Balance Sheet	
Wealth-building assets	Amount
Cash	\$ 1,500
Savings account	1,000
Stocks, bonds and other investments	5,000
401 (k) retirement plan /IRA	25,000
Market value of home	0
Other assets	
Market value of car	14,000
<b>Total assets</b>	<b>\$ 46,500</b>

Liabilities	Amount
Home mortgage	\$ 0
Home equity loan	0
Car loan balance	13,000
Credit card balances	3,000
Student loan	5,000
Child support*	2,400
Miscellaneous liabilities	1,500
<b>Total liabilities</b>	<b>\$ 24,900</b>
<b>Net worth</b>	<b>\$ 21,600</b>

\*Represents one year of payments.

My Balance Sheet	
Wealth-building assets	Amount
Cash	
Savings account	
Stocks, bonds and other investments	
401 (k) retirement plan /IRA	
Market value of home	
Other assets	
Market value of car	
<b>Total assets</b>	

Liabilities	Amount
Home mortgage	
Home equity loan	
Car loan balance	
Credit card balances	
Student loan	
Child support*	
Miscellaneous liabilities	
<b>Total liabilities</b>	
<b>Net worth</b>	

## ② Budget to

What would you like your net worth to be

5 years from now? \$ \_\_\_\_\_

10 years from now? \$ \_\_\_\_\_

### SET FINANCIAL GOALS

*If you make a good income each year and spend it all, you are not getting wealthier.*

*You are just living high.*

Thomas J. Stanley and William D. Danko,

*The Millionaire Next Door*

Most people who have built wealth didn't do so overnight. They got wealthy by setting goals and striving to reach them. Bob set two short-term goals: (1) to save \$3,000 a year for three years to have \$9,000 for a down payment on a house, and (2) to pay off his \$3,000 credit card debt within two years. Bob also set two long-term goals: (1) to save and invest enough to have \$25,000 in 15 years for his children's college education, and (2) to have \$5,000 a month to live on when he retires in 30 years.

A personal wealth-creation strategy is based on specific goals. In preparing your goals:

- Be realistic.
- Establish time frames.
- Devise a plan.
- Be flexible; goals can change.

In the space provided, list your top goals.

#### Example: Short-term

1. *In one year, save \$500 for my emergency fund.*
2. *In three years, save \$5,000 for a down payment on a house.*

#### Example: Long-term

1. *In eight years, save \$15,000 to help my child with college.*

#### My short-term goals are:

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_

#### My long-term goals are:

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_

Now you, like Bob, can choose how to meet those goals. This is where budgeting to save comes into play.

## DEVELOP A BUDGET AND LIVE BY IT

When it comes to finances, people generally fall into the following groups. Where do you fit in?

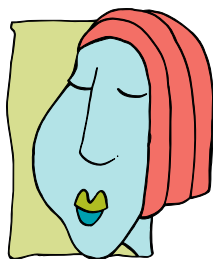
**Planners** control their financial affairs. They budget to save.

**Strugglers** have trouble keeping their heads above rough financial waters. They find it difficult to budget to save.

**Deniers** refuse to see that they're in financial trouble. So they don't see a need to budget to save.

**Impulsives** seek immediate gratification. They spend today and let tomorrow take care of itself. They couldn't care less about budgeting to save.

Knowing what kind of financial manager you are will help determine what changes to make. To maximize your wealth-creating ability, you want to be a planner, like Betty.



Betty

Betty is a single parent with one child. "I have to budget in order to live on my modest income. I have a little notebook I use to track where every dime goes. Saving is very important to me. When my son was born, I started investing every month in a mutual fund for his college education. I am proud to say that I control my future. I have bought my own home and provided for my son, and I've never bounced a check. You must have common sense regarding money!"



Lynne

Lynne, by contrast, is an impulsive. Lynne has a good job, makes good money and lives a pretty comfortable life, but her bank statement tells a different story. She has no savings or investments, owns no property and has no plans for retirement. Plus, she's got a lot of credit card debt, lives from paycheck to paycheck and doesn't budget.

You can choose to be like Lynne, or you can follow Betty's road to wealth creation by learning to budget and save.

A budget allows you to:

- Understand where your money goes.
- Ensure you don't spend more than you make.
- Find uses for your money that will increase your wealth.

To develop a budget, you need to:

- Calculate your monthly income.
- Track your daily expenses.
- Determine how much you spend on monthly bills.

## Track Day-to-Day Spending

One day, Lynne, the impulsive, realized that to create wealth she had to become more like Betty and plan her financial future. To start, Lynne analyzed her finances to see how much money she made and how she was spending it. She set a goal to save \$125 a month to put toward her wealth-creation goals. First, she calculated her income. Then she added up her monthly bills.

She also carried a little notebook in her purse for jotting down her daily spending, whether by cash or debit card, check or credit card. Here is a page from her notebook.



### Lynne's Day-to-Day Spending

Date	Expense	Cash/debit/check	Charge
1/2	Breakfast, Get-N-Go	\$ 3.56	
1/2	Coffee	.90	
1/2	Lunch		\$ 6.75
1/2	Soft drink	1.25	
1/2	Gas for car		46.00
1/2	Drinks with friends	10.00	
1/2	Groceries		50.00
1/2	Dinner	10.00	
1/2	Newspaper	.50	
1/3	Bacon and eggs, Moonlight Diner	4.95	
1/3	Newspaper	.50	
1/3	Coffee	.90	
1/3	Lunch with coworkers		5.72
1/3	Dinner		15.00
1/3	Dress		45.00
1/3	Soft drink	1.25	
1/3	Trip to the movies	15.00	
1/4	Breakfast	3.50	
1/4	Coffee	.90	
1/4	Lunch	5.75	
1/4	Cookies	1.25	
1/4	Newspaper	.50	
1/4	Birthday present	15.00	
1/4	Dinner		6.77
1/5	Breakfast	3.25	
1/5	Coffee	.90	
1/5	Soft drink	1.25	
1/5	Newspaper	.90	
1/5	Magazine	3.95	
1/6	Breakfast	3.25	
1/6	Coffee	.90	
1/6	Newspaper	.50	
1/6	Lunch	4.50	
1/6	Cookies	1.25	
1/6	Jacket		50.00
1/6	Video rental	3.95	



## Get a Handle on Income and Expenses

Lynne used the information from tracking her day-to-day expenses to develop a monthly budget. When Lynne reviewed her budget, she realized she was spending more than she earned. Lynne knew if she were ever going to save \$125 a month, she had to cut her expenses, earn more money, or both. She worked overtime at her company, which increased her take-home pay. She bought fewer clothes, discontinued premium cable TV channels, carpooled to work to cut gas consumption and reduced her spending on eating out and entertainment. Tracking her expenses paid off. Lynne successfully developed a budget that enables her to save \$125 each month.

Here is her budget. If Lynne sticks to it, she will have \$125 a month that she can:

- Put in a savings account.
- Invest in a 401(k) retirement plan at work.
- Invest in an individual retirement account (IRA).
- Invest in stocks, bonds or mutual funds.
- Use to pay off debt.

These are just some of the wealth-building choices available when you budget to save.

	Current income	Income changes	New budget
Take-home pay	\$ 2,235		\$ 2,235
Overtime pay		\$ 40	\$ 40
Pension, Social Security benefits			
Investment earnings <i>not reinvested</i>			
Interest on savings accounts			
Alimony/child support			
Other income			
<b>Total income</b>	<b>\$ 2,235</b>	<b>\$ 40</b>	<b>\$ 2,275</b>

	Current expenses	Spending changes	New budget
Rent	\$ 680		\$ 680
Renter's insurance	20		20
Electricity	60		60
Gas	30		30
Water	25		25
Telephone	50		50
Cable TV/Internet service	55	-20	35
Insurance (life, disability)	0		0
Charitable donations	0		0
Credit card interest payment	25		25
Groceries	200		200
Clothing	130	-30	100
Day care/tuition	0		0
Car loan	300		300
Car insurance	75		75
Gas for car	145	-20	125
Meals out & entertainment	425	-50	375
Miscellaneous daily expenses	100	-50	50
<b>Total expenses</b>	<b>\$ 2,320</b>	<b>\$ -170</b>	<b>\$ 2,150</b>
<b>Monthly net (income - expenses)</b>	<b>\$ -85</b>		<b>\$ 125</b>
<b>Available to save or invest</b>	<b>\$ 0</b>		<b>\$ 125</b>

Using Lynne's budget as an example, track your income and expenses. Identify changes you can make to increase your income or decrease your expenses, and develop a new budget that includes more savings. Be sure to make reasonable budget changes that you can live with month to month.

To help you maintain the discipline to save:

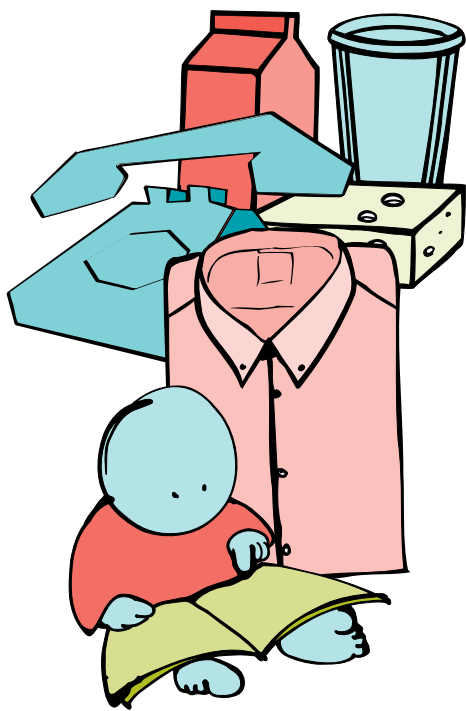
- Save every month.
- Have savings automatically deducted from your paycheck or checking account.
- Base your budget on what's left.

In other words, get on automatic pilot and stay there.

How much do you currently save each month? \$ \_\_\_\_\_

How much are you *going* to save each month? \$ \_\_\_\_\_

You have now successfully budgeted to save. The next step is saving and investing.



### My Monthly Budget

	Current income	Income changes	New budget
Take-home pay			
Overtime pay			
Pension, Social Security benefits			
Investment earnings <i>not</i> reinvested			
Interest on savings accounts			
Alimony/child support			
Other income			
<b>Total income</b>			

	Current expenses	Spending changes	New budget
Rent/House Payment			
Property insurance			
Electricity			
Gas			
Water			
Telephone			
Cable TV/Internet service			
Insurance (life, disability)			
Charitable donations			
Credit card interest payment			
Groceries			
Clothing			
Day care/tuition			
Car loan			
Car insurance			
Gas for car			
Meals out & entertainment			
Miscellaneous daily expenses			
<b>Total expenses</b>			
<b>Monthly net (income - expenses)</b>			
<b>Available to save or invest</b>			

## ③ Save and Invest

*Take the power of compound interest seriously—and then save.*

Dwight R. Lee and Richard B. McKenzie,  
*Getting Rich in America*

You have budgeted and identified an amount to save monthly. Where are you going to put your savings? By investing, you put the money you save to work making more money and increasing your wealth. An *investment* is anything you acquire for future income or benefit. Investments increase by generating income (interest or dividends) or by growing (appreciating) in value. Income earned from your investments and any appreciation in the value of your investments *increase* your wealth.

### GET GUIDANCE

There is an art to choosing ways to invest your savings. Good investments will make money; bad investments will cost money. Do your homework. Gather as much information as you can. Seek advice from personnel at your bank or other trained financial experts. Read newspapers, magazines and other publications. Identify credible information sources on the Internet. Join an investment club. Check out the information resources listed in the resource guide at the back of this publication.

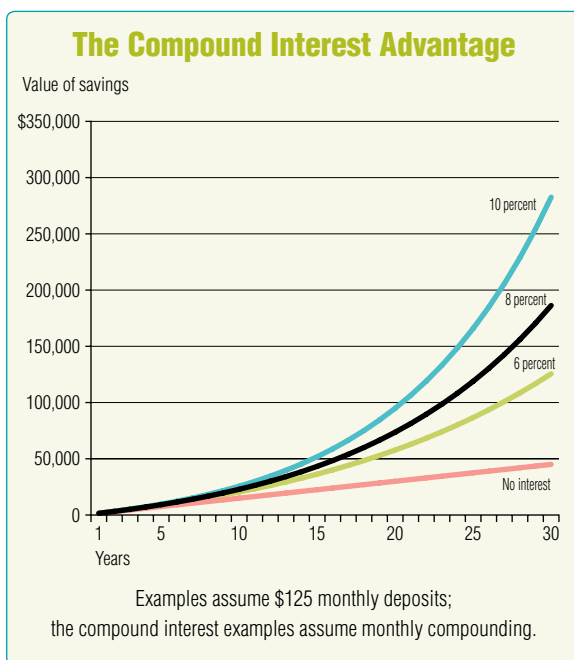
### TAKE ADVANTAGE OF COMPOUND INTEREST

*Compound interest* helps you build wealth faster. Interest is paid on previously earned interest as well as on the original deposit or investment. For example, \$5,000 deposited in a bank at 6 percent interest for a year earns \$308 if the interest is compounded monthly. In just 5 years, the \$5,000 will grow to \$6,744.

Let's see how interest compounds on Lynne's savings. Assume that Lynne saves \$125 a month for 30 years and the interest on her savings is compounded monthly.

The chart to the left shows how compound interest at various rates would increase Lynne's savings compared with simply putting the money in a shoebox. This is compound interest that you earn. And as you can see from Lynne's investment, compounding has a greater effect after the investment and interest have increased over a longer period.

There is a flip side to compound interest. That is compound interest you are charged. This compound interest is charged for purchases on your credit card. Chapter 4, "Take Control of Debt," discusses this type of interest.



## UNDERSTAND THE RISK-EXPECTED RETURN RELATIONSHIP

*An investment in knowledge always pays the best interest.*

Benjamin Franklin

### HOW MUCH RISK DO YOU WANT TO TAKE?

Here are some things to think about when determining the amount of risk that best suits you.

**Financial goals.** How much money do you want to accumulate over a certain period of time? Your investment decisions should reflect your wealth-creation goals.

**Time horizon.** How long can you leave your money invested? If you will need your money in one year, you may want to take less risk than you would if you won't need your money for 20 years.

**Financial risk tolerance.** Are you in a financial position to invest in riskier alternatives? You should take less risk if you cannot afford to lose your investment or have its value fall.

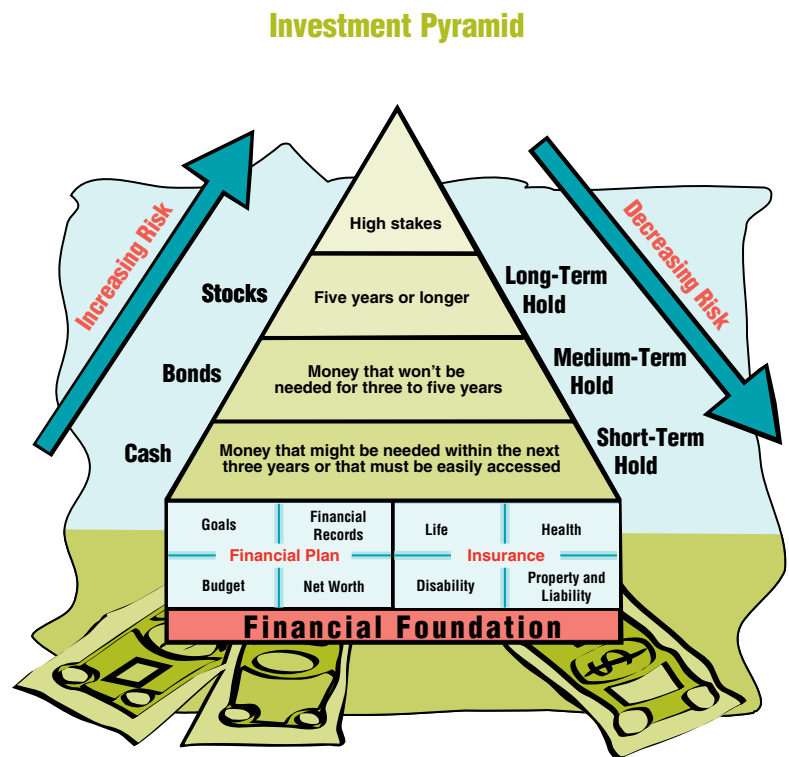
**Inflation risk.** This reflects savings' and investments' sensitivity to the inflation rate. For example, while some investments such as a savings account have no risk of default, there is the risk that inflation will rise above the interest rate on the account. If the account earns 5 percent interest, inflation must remain lower than 5 percent a year for you to realize a profit.

When you are saving and investing, the amount of expected return is based on the amount of risk you take with your money. Generally, the higher the risk of losing money, the higher the expected return. For less risk, an investor will expect a smaller return.

For example, a savings account at a financial institution is fully insured by the Federal Deposit Insurance Corp. up to \$250,000\*. The return—or interest paid on your savings—will generally be less than the expected return on other types of investments.

On the other hand, an investment in a stock or bond is not insured. The money you invest may be lost or the value reduced if the investment doesn't perform as expected.

After deciding how much risk you are able to take, you can use the investment pyramid to help balance your savings and investments. You should move up the pyramid only after you have built a strong foundation.



NOTE: Information not intended as specific individual investment advice.

SOURCES: National Institute for Consumer Education, Eastern Michigan University; AIG VALIC.

\*A temporary increase for the standard insurance amount per depositor to \$250,000 is in effect through December 31, 2013. From [www.fdic.gov](http://www.fdic.gov): "On January 1, 2014, the standard insurance amount will return to \$100,000 per depositor for all account categories except IRAs and other certain retirement accounts, which will remain at \$250,000 per depositor."

## TOOLS FOR SAVING

The simplest way to begin earning money on your savings is to open a savings account at a financial institution. You can take advantage of compound interest, with no risk.

Financial institutions offer a variety of savings accounts, each of which pays a different interest rate. The box below describes the different accounts. Find the best one for your situation and compare interest rates and fees. You can choose to use these typical accounts to save for the near future or for years down the road.

### Individual Development Accounts

In some communities, people whose income is below a certain level can open an individual development account (IDA) as part of a money-management program organized by a local nonprofit organization. IDAs are generally opened at a local bank. Deposits made by the IDA account holder are often matched by deposits from a foundation, government agency or other organization. IDAs can be used for buying a first home, paying for education or job training, or starting a small business.

Training programs on budgeting, saving and managing credit are frequently part of IDA programs.

Find out about IDAs by calling CFED at (202) 408-9788, or visit its web site at [www.idanetwork.org](http://www.idanetwork.org).

### Types of Savings Accounts

#### Savings account (in general)

- Access your money at any time.
- Earn interest.
- Move money easily from one account to another.
- Savings insured by the FDIC up to \$250,000.

#### Money market account

- Earn interest.
- Pay no fees if you maintain a minimum balance.
- May offer check-writing services.
- Savings insured by the FDIC up to \$250,000.

#### Certificate of deposit (CD)

- Earn interest during the term (three months, six months, etc.).
- Must leave the deposit in the account for the entire term to avoid an early-withdrawal penalty.
- Receive the principal and interest at the end of the term.
- Savings insured by the FDIC up to \$250,000.

## TOOLS FOR INVESTING

Once you have a good savings foundation, you may want to diversify your assets among different types of investments. Diversification can help smooth out potential ups and downs of your investment returns. Investing is not a get-rich-quick scheme. Smart investors take a long-term view, putting money into investments regularly and keeping it invested for five, 10, 15, 20 or more years.

### Bonds—Lending Your Money

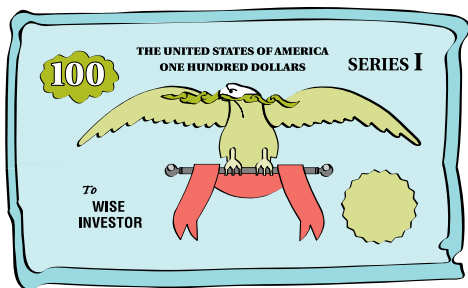
**Bonds.** When you buy bonds, you are lending money to a federal or state agency, municipality or other issuer, such as a corporation. A bond is like an IOU. The issuer promises to pay a stated rate of interest during the life of the bond and repay the entire face value when the bond comes due or reaches maturity. The interest a bond pays is based primarily on the credit quality of the issuer and current interest rates. Firms like Moody's Investor Service and Standard & Poor's rate bonds. With corporate bonds, the company's bond rating

### A Good Rule of Thumb

The Rule of 72 can help you estimate how your investment will grow over time. Simply divide the number 72 by your investment's expected rate of return to find out approximately how many years it will take for your investment to double in value.

Example: Invest \$5,000 today at 8 percent interest. Divide 72 by 8 and you get 9. Your investment will double every nine years. In nine years, your \$5,000 investment will be worth about \$10,000, in 18 years about \$20,000 and in 27 years, \$40,000.

The Rule of 72 also works if you want to find out the rate of return you need to make your money double. For example, if you have some money to invest and you want it to double in 10 years, what rate of return would you need? Divide 72 by 10 and you get 7.2. Your money will double in 10 years if your average rate of return is 7.2 percent.



is based on its financial picture. The rating for municipal bonds is based on the creditworthiness of the governmental or other public entity that issues it. Issuers with the greatest likelihood of paying back the money have the highest ratings, and their bonds will pay an investor a lower interest rate. Remember, the lower the risk, the lower the expected return.

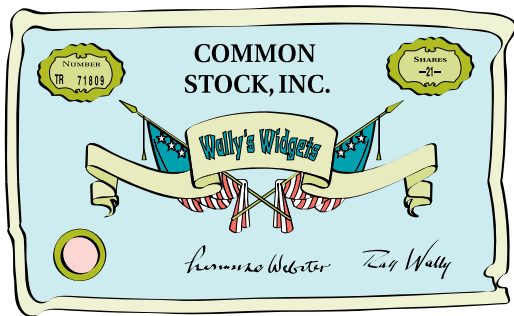
A bond may be sold at face value (called *par*) or at a premium or discount. For example, when prevailing interest rates are lower than the bond's stated rate, the selling price of the bond rises above its face value. It is sold at a premium. Conversely, when prevailing interest rates are higher than the bond's stated rate, the selling price of the bond is discounted below face value. When bonds are purchased, they may be held to maturity or traded.

**Savings bonds.** *U.S. savings bonds* are government-issued and government-backed. There are different types of savings bonds, each with slightly different features and advantages. *Series I* bonds are indexed for inflation. The earnings rate on this type of bond combines a fixed rate of return with the annualized rate of inflation. Savings bonds can be purchased in denominations ranging from \$50 to \$10,000.

**Treasury bonds, bills and notes.** The bonds the U.S. Treasury issues are sold to pay for an array of government activities and are backed by the full faith and credit of the federal government. *Treasury bonds* are securities with terms of more than 10 years. Interest is paid semi-annually. The U.S. government also issues securities known as Treasury bills and notes. *Treasury bills* are short-term securities with maturities of three months, six months or one year. They are sold at a discount from their face value, and the difference between the cost and what you are paid at maturity is the interest you earn. *Treasury notes* are interest-bearing securities with maturities ranging from two to 10 years. Interest payments are made every six months. *Treasury Inflation Protected Securities (TIPS)* offer investors a chance to buy a security that keeps pace with inflation. Interest is paid on the inflation-adjusted principal.

Bonds, bills and notes are sold in increments of \$1,000. These securities, along with U.S. savings bonds, can be purchased directly from the Treasury through TreasuryDirect at [www.treasurydirect.gov](http://www.treasurydirect.gov).

Some government-issued bonds offer special tax advantages. There is no state or local income tax on the interest earned from Treasury and savings bonds. And in most cases, interest earned from municipal bonds is exempt from federal and state income tax. Typically, higher income investors buy these bonds for their tax benefits.



### Stocks—Owning Part of a Company

When you buy *stock*, you become a part owner of the company and are known as a *stockholder*, or *shareholder*. Stockholders can make money in two ways—receiving dividend payments and selling stock that has appreciated. A *dividend* is an income distribution by a corporation to its shareholders, usually made quarterly. *Stock appreciation* is an increase in the value of stock in the company, generally based on its ability to make money and pay a dividend. However, if the company doesn't perform as expected, the stock's value may go down.

There is no guarantee you will make money as a stockholder. In purchasing shares of stock, you take a risk on the company making a profit and paying a dividend or seeing the value of its stock go up. Before investing in a company, learn about its past financial performance, management, products and how the stock has been valued in the past. Learn what the experts say about the company and the relationship of its financial performance and stock price. Successful investors are well informed.



### Mutual Funds—Investing in Many Companies

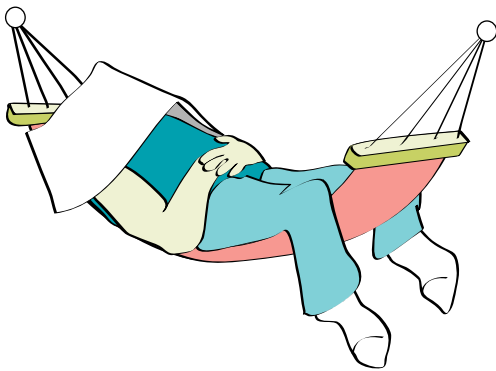
*Mutual funds* are established to invest many people's money in many firms. When you buy mutual fund shares, you become a shareholder of a fund that has invested in many other companies. By diversifying, a mutual fund spreads risk across numerous companies rather than relying on just one to perform well. Mutual funds have varying degrees of risk. They also have costs associated with owning them, such as management fees, that will vary depending on the type of investments the fund makes.

Before investing in a mutual fund, learn about its past performance, the companies it invests in, how it is managed and the fees investors are charged. Learn what the experts say about the fund and its competitors.

Stocks, bonds and mutual funds can be purchased through a full-service broker if you need investment advice, from a discount broker, or even directly from some companies and mutual funds. Remember, when investing in these products:

- Find good information to help you make informed decisions.
- Make sure you know and understand all the costs associated with buying, selling and managing your investments.
- Beware of investments that seem too good to be true; they probably are.

## INVEST FOR RETIREMENT



Have you ever thought about how much money you will need when you retire? Will you save enough today to meet your future needs at prices higher than today's due to *inflation*? Many people don't save enough for retirement. Use the following chart to calculate how much you need to invest today to achieve your retirement goal. For example, suppose you are 20 years old and would like to have \$1 million when you retire at age 65. If you can invest \$13,719 today, it will grow to \$1 million over the next 45 years if it earns a constant 10 percent return, compounded annually. You never have to add another dime to your initial investment.

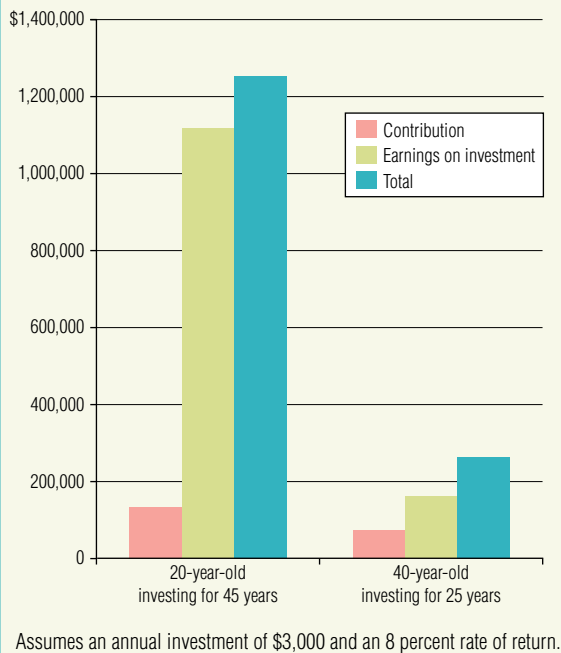
How old are you? \_\_\_\_\_

How much do you want saved by retirement? \_\_\_\_\_

Invest Today to Meet Retirement Goals at Age 65					
Age	Amount invested				
20	\$ 2,743	\$ 5,487	\$ 8,232	\$ 10,976	\$ 13,719
25	4,419	8,838	13,257	17,676	22,095
30	7,117	14,234	21,351	28,468	35,585
35	11,462	22,924	34,386	45,847	57,309
40	18,460	36,919	55,378	73,838	92,296
45	29,729	59,458	89,186	118,915	148,644
50	47,879	95,757	143,635	191,514	239,392
55	77,109	154,217	231,326	308,435	385,543
60	124,185	248,369	372,553	496,737	620,921
65	\$ 200,000	\$ 400,000	\$ 600,000	\$ 800,000	\$ 1,000,000

Assumes a 10 percent return that is compounded annually.

## Invest in an IRA: The Sooner You Start, the Better



## Individual Retirement Accounts

An individual retirement account (IRA) lets you build wealth and retirement security. The money you invest in an IRA grows tax-free until you retire and are ready to withdraw it. You can open an IRA at a bank, brokerage firm, mutual fund or insurance company. IRAs are subject to certain income limitations and other requirements you will need to learn more about, but here is an overview of what they offer.

You can contribute up to \$4,000 a year to a *traditional IRA*, as long as you earn \$4,000 a year or more. A married couple with only one person working outside the home may contribute a combined total of \$8,000 to an IRA and a *spousal IRA*. Individuals 50 years of age or older may make an additional “catch-up” contribution of \$1,000 a year, for a total annual contribution of \$5,000. Money invested in an IRA is deductible from current-year taxes if you are not covered by a retirement plan where you work and your income is below a certain limit.

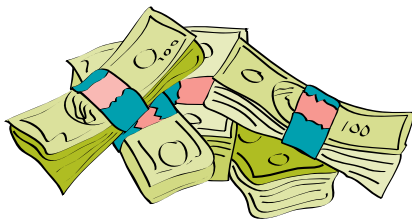
You don’t pay taxes on the money in a traditional IRA until it is withdrawn. All withdrawals are taxable, and there generally are penalties on money withdrawn before age 59½. However, you can make certain withdrawals without penalty, such as to pay for higher education, to purchase your first home, to cover certain unreimbursed medical expenses or to pay medical insurance premiums if you are out of work.

A *Roth IRA* is funded by after-tax earnings; you do not deduct the money you pay in from your current income. However, after age 59½ you can withdraw the principal and any interest or appreciated value tax-free.

## 401(k) Plans

Many companies offer a 401(k) plan for employees’ retirement. Participants authorize a certain percentage of their before-tax salary to be deducted from their paycheck and put into a 401(k). Many times, 401(k) funds are professionally managed and employees have a choice of investments that vary in risk. Employees are responsible for learning about the investment choices offered.

By putting a percentage of your salary into a 401(k), you reduce the amount of pay subject to federal and state income tax. Tax-deferred contributions and earnings make up the best one-two punch in investing. In addition, your employer may match a portion of every dollar you invest in the 401(k), up to a certain percentage or dollar amount.



### How Much Extra Savings Is a Tax-Deferred Investment Worth?

If you pay taxes, which most of us do, a tax-deferred investment will be worth the amount you invest multiplied by the tax rate you pay. For example, if your federal tax rate is 15 percent and you invest \$3,000 in an IRA, you'll save \$450 in taxes. So in effect, you will have spent only \$2,550 for a \$3,000 investment on which you will earn money. A good wealth-creation plan maximizes tax-deferred investments.

As long as the money remains in your 401(k), it's tax-deferred. Withdrawals for any purpose are taxable, and withdrawals before age 59½ are subject to a penalty. Take full advantage of the retirement savings programs your company offers—and understand thoroughly how they work. They are great ways to build wealth.

### Qualified Plans

If you're self-employed, don't worry. There is a retirement plan for you. A qualified plan (formerly referred to as a Keogh plan) is a tax-deferred plan designed to help self-employed workers save for retirement.

The most attractive feature of a qualified plan is the high maximum contribution—up to \$42,000 annually. The contributions and investment earnings grow tax-free until they are withdrawn, when they are taxed as ordinary income. Withdrawals before age 59½ are subject to a penalty.

Check the IRS web site—[www.irs.gov](http://www.irs.gov)—for current information on tax-deferred investments.

## OTHER INVESTMENTS **Investing in Your House**

### Building Equity Quicker—A Comparison

Mortgage term	30 years	15 years
Loan amount	\$ 118,000	\$ 118,000
Months to pay	360	180
Annual percentage rate	7.5%	7.0%
Monthly payment	\$ 825	\$ 1,061
Total interest	\$ 179,030	\$ 72,911
Interest savings	—	\$ 106,119

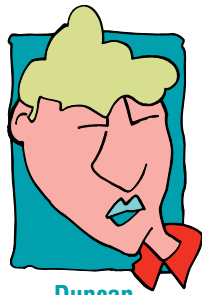
Remember Bob in Chapter 1, who started reading this workbook to create wealth? Practicing what he read, Bob reduced his debt, increased his savings and is now ready to buy a house. He has a sizable down payment saved, so right from the beginning he will have equity in his home.

**Equity**, in this case, is the difference between the market value of the house and the balance on Bob's mortgage. As Bob pays his mortgage, he increases his equity. Plus, over time, his house may rise in value—giving him more money if he chooses to sell it. Knowing that the more equity he has in his house, the wealthier he will be, Bob takes a 15-year mortgage rather than the more traditional 30-year mortgage. This will enable him to own his house in 15 years. Of course, Bob will make higher monthly payments on his mortgage than he would have, but he will build equity quicker and ultimately pay less interest.

By making higher monthly payments, Bob not only will own his house outright in 15 years, but he will save \$106,119 in interest payments. Making higher monthly payments, of course, means budgeting. Bob chose to budget extra money each month out of his paycheck—and make wise spending choices—so he can do just that.

## Start Your Own Business

You can also start and invest in your own business as part of a wealth-creation plan. This requires planning, know-how, savings and an entrepreneurial spirit. Starting a small business can be risky, but it is one of the most significant ways individuals have to create personal wealth.



Duncan

Duncan had a dream—he wanted to own a business. He worked for a printing company for 10 years and learned every aspect of the business. He and his wife saved every month until they had a sizable nest egg. When they felt the timing was right, they bought a printing press and computer equipment and set up shop in an old warehouse. Duncan's wife kept her job so they would have steady income and benefits while the business got off the ground.

For the next five years, Duncan worked long hours and put all the income back into the business to help it grow. He gave his customers good service, attracted more customers and paid close attention to his expenses. By the sixth year, the business was profitable and Duncan and his wife were well on the way to owning a successful, ongoing enterprise that will increase their personal wealth.

None of this would have been possible without budgeting and saving. Duncan was able to use the couple's savings to invest in his talents and entrepreneurial spirit.

## Other Investment Alternatives

You also can invest in other things that may not earn a dividend or interest but may rise in value over time, such as land, rare coins, antiques and art. If you are knowledgeable about these types of investments, they might be the right choice for you.

Now it's time to plan your investment strategy. List the investment options you are going to learn more about and weigh them against your wealth-creation goals, time frame and risk tolerance.

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_
4. \_\_\_\_\_
5. \_\_\_\_\_

We have seen that by budgeting to save, saving and investing, wealth can be created. But what if debt limits your ability to save and invest? The next chapter discusses controlling debt.



---

## ④ Take Control of Debt

Remember the definition of net worth (wealth)?

**Assets** – **Liabilities** = **Net Worth**

*I owe, I owe, so it's off to work I go.*

Bumper sticker on a 1972 Chevy

Liabilities are your debts. Debt reduces net worth. Plus, the interest you pay on debt, including credit card debt, is money that cannot be saved or invested—it's just gone. Debt is a tool to be used wisely for such things as buying a house. If not used wisely, debt can easily get out of hand. For example, putting day-to-day expenses—like groceries or utility bills—on a credit card and not paying off the balance monthly can lead to debt overload.

### WHY PEOPLE GET INTO TROUBLE WITH DEBT

Lots of people are mired in debt. In some cases, they could not control the causes of their debt. However, in some instances they could have.

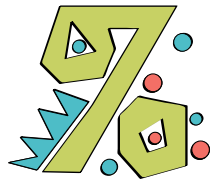
Many people get into serious debt because they:

- Experienced financial stresses caused by unemployment, medical bills or divorce.
- Could not control spending, did not plan for the future and did not save money.
- Lacked knowledge of financial and credit matters.

### Tips for Controlling Debt

- Develop a budget and stick to it.
- Save money so you're prepared for unforeseen circumstances. You should have at least three to six months of living expenses stashed in your rainy day savings account, because as the poet Longfellow put it, "Into each life some rain must fall."
- When faced with a choice of financing a purchase, it may be a better financial decision to choose a less expensive model of the same product and save or invest the difference.
- Pay off credit card balances monthly.
- If you must borrow, learn everything about the loan, including interest rate, fees and penalties for late payments or early repayment.

## SPEAKING OF INTEREST



When you take out a loan, you repay the *principal*, which is the amount borrowed, plus *interest*, the amount charged for lending you the money.

Remember the discussion about earning compound interest in Chapter 3? The interest on your monthly balance is a good example of compound interest that you pay. The interest is added to your bill, and the next month interest is charged on that amount *and* on the outstanding balance.

The bottom line on interest is that those who know about interest earn it; those who don't, pay it.

## AVOID CREDIT CARD DEBT

Planners, like Betty, rarely use credit cards. When they do, they pay off their balances every month. When a credit card balance is not paid off monthly, it means paying interest—often 20 percent or more a year—on everything purchased. So think of credit card debt as a high-interest loan.

### The Tale of Two Spenders and the Big-Screen TV

Remember Betty, the planner? She saved up for the “extras.” When she had enough money in her savings account, she bought a big-screen TV for \$1,500. She paid cash.

Her friend Tim is an impulsive spender. He seeks immediate gratification using his credit cards, not realizing how much extra it costs. Tim bought the same TV for \$1,500 but financed it on a store credit card with an annual interest rate of 22 percent. At \$50 a month, it took him almost four years to pay off the balance.

While Betty paid only \$1,500 for her big-screen TV, Tim paid \$2,200—the cost of the TV plus interest. Tim not only paid an extra \$700, he lost the opportunity to invest the \$700 in building his wealth.

Do you need to reduce your credit card debt? Here are some suggestions.

- Pay cash.
- Set a monthly limit on charging, and keep a written record so you don't exceed that amount. (Remember your daily expense sheet from Chapter 2? Use it to keep track.)
- Limit the number of credit cards you have. Cut up all but one of your cards. Stash that one out of sight, and use it only in emergencies.
- Choose the card with the lowest interest rate and no (or very low) annual fee. But beware of low introductory interest rates offered by mail. These rates often skyrocket after the first few months.
- Don't apply for credit cards to get a free gift or a discount on a purchase.
- Steer clear of blank checks that financial services companies send you. These checks are cash advances that may carry a higher interest rate than typical charges.
- Pay bills on time to avoid late charges or increased interest rates.

## BEWARE THE PERILS OF PAYDAY LOANS AND PREDATORY LENDERS



Pauline

People can get deep in debt when they take out a loan against their paycheck. They write a postdated check in exchange for money. When they get paid again, they repay the loan, thus the name *pay-day loan*. These loans generally come with very high, double-digit interest rates. Borrowers who can't repay the money are charged additional fees for an extension, which puts them even deeper in debt. Borrowers can continue to pay fees to extend the loan's due date indefinitely, only to find they are getting deeper in debt because of the steep interest payments and fees.

Predatory lenders often target seniors and low-income people they contact by phone, mail or in person. After her husband died, 73-year-old Pauline got plenty of solicitations from finance companies. She was struggling to make ends meet on her fixed income. To pay off her bills, she took out a \$5,000 home equity loan that carried a high interest rate and excessive fees. Soon she found she was even deeper in debt, so she refinanced the loan once, then again, and again, paying fees each time.

Pauline's children discovered her situation and paid off the loan. The lessons here are:

- Don't borrow from Peter to pay Paul.
- Never respond to a solicitation that makes borrowing sound easy and cheap.
- Always read the fine print on any loan application.
- Seek assistance from family members, local credit counseling services or others to make sure a loan is right for you.

## KNOW WHAT CREDITORS SAY ABOUT YOU

Those who have used credit will have a credit report that shows everything about their payment history, including late payments.

The information in your credit report is used to create your credit score. A credit score is a number generated by a statistical model that objectively predicts the likelihood that you will repay on time. Banks, insurance companies, potential landlords and other lenders use credit scores.

Credit scores range from under 500 to 800 and above and are determined by payment history, the amount of outstanding debt, length of your credit history, recent inquiries on your credit report and the types of credit in use. Factors not considered in a credit score include age, race or ethnicity, income, job, marital status, education, length of time at your current address, and whether you own or rent your home.

### What's on YOUR Credit Report?

Consumers have the right to receive annually a free copy of their credit report from each of the three major credit reporting companies:

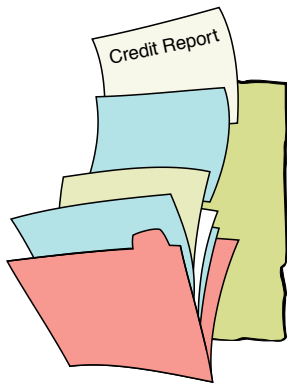
**Equifax:** 1-800-685-1111; [www.equifax.com](http://www.equifax.com)

**Experian:** 1-800-397-3742; [www.experian.com](http://www.experian.com)

**Trans Union:** 1-800-888-4213; [www.transunion.com](http://www.transunion.com)

The three nationwide consumer credit reporting companies have set up a toll-free telephone number and one central web site for ordering free reports:

1-877-322-8228; [www.annualcreditreport.com](http://www.annualcreditreport.com)



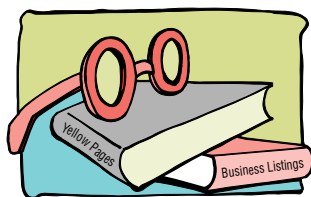
A credit report that includes late payments, delinquencies or defaults will result in a low credit score and could mean not getting a loan or having to pay a much higher interest rate. The higher your score, the less risk you represent to the lender.

Review your credit report at least once a year to make sure all information is accurate. If you find an error, the Fair Credit Reporting Act requires credit reporting companies and those reporting information to them to correct the mistake. To start the process of fixing an error:

- Contact the credit reporting company online, by fax or certified letter, identifying the creditor you have a dispute with and the nature of the error.
- Send the credit reporting company verifiable information, such as canceled checks or receipts, supporting your complaint.
- The credit reporting company must investigate your complaint within 30 days and get back to you with its results.
- Contact the creditor if the credit reporting company investigation does not result in correction of the error. When you resolve the dispute, ask the creditor to send the credit reporting company a correction.

If the issue remains unresolved, you have the right to explain in a statement that will go on your credit report. For example, if you did not pay a car repair bill because the mechanic didn't fix the problem, the unpaid bill may show up on your credit report, but so will your explanation.

## KEEP YOUR GOOD NAME



Every month, go back to your budget and plan carefully to ensure your bills are paid before their due dates. Betty, the planner, makes sure she pays her bills on time. Betty gets paid twice a month. She has her paycheck set up for direct deposit so she doesn't have to scramble to get to the bank on payday. With her first paycheck each month, she pays her mortgage (which she has set up on auto debit), cable TV and utility bills. Out of the second check, Betty makes her car payment (also on auto debit) and has a monthly deposit automatically made to her savings account. Betty has found that "auto-pilot" really simplifies budgeting and saving.

If you believe you are too deep in debt:

- Discuss your options with your creditors before you miss a payment.
- Seek expert help, such as Consumer Credit Counseling Services, listed in your local telephone directory.
- Avoid "credit repair" companies that charge a fee. Many of these are scams.

## SAVE MONEY BY CHOOSING THE RIGHT LOAN

### \$15,000 Car Loan for 5 Years

Lender	Interest rate	Total interest
Pixley Bank and Trust	6.5%	\$2,609.53
XYZ Savings and Loan	7.5%	\$3,034.15
Joe's Auto Sales	15.0%	\$6,410.94

If you have good credit, you may want to take out a loan to purchase a house or to cover educational expenses—both are investments in the future. But regardless of how the money is spent, a loan is a liability, or debt, and decreases your wealth. So choose loans carefully.

Shop and negotiate for the lowest interest rate. The interest you save can be invested to build wealth. Take a look at the chart to the left. In this example, it is obvious that Pixley Bank and Trust would charge the lowest interest over the term of the loan. What's not obvious is that your credit score may determine which interest rate you are offered. Use an online auto loan calculator to compare rates.

## SAVE MONEY BY PAYING LOANS OFF EARLY

You can save interest expense by increasing your monthly payments or choosing a shorter payment term on your loan.

Betty, the planner, knew her new car would cost more than the sticker price because she would have to pay interest on the loan from the bank. After checking her options, she chose a shorter payment term with higher payments. Betty budgeted enough money each month to make the higher payments. By doing this, she will reduce the amount of interest she ultimately pays.

The chart on the left shows how shorter terms with higher payments would affect the total amount and interest on Betty's \$15,000 car loan.

Avoid the trap of getting “upside down”—owing more on the car than it is worth when you sell or trade it in. Betty's car will be paid for in three years, and she plans on driving it for at least eight years. Once her car is paid for, she will continue to budget for the car payment but will invest the money to further build her wealth.

### \$15,000 Car Loan at 8 Percent Interest

	3-year	4-year	5-year
Number of payments	36	48	60
Payment	\$ 470	\$ 366	\$ 304
Total paid	\$ 16,922	\$ 17,577	\$ 18,249



## TAKE STEPS TO CONTROL YOUR DEBT

Credit card	Debt	Interest rate	Monthly interest*
Department Store A	\$ 500	19.5%	\$ 8.13
XYZ Bank	\$ 1,250	17%	\$ 17.71
BHA Finance Co.	\$ 1,000	22%	\$ 18.33
Store B	\$ 250	15%	\$ 3.13
<b>Total</b>	<b>\$3,000</b>		<b>\$ 47.30</b>

\*Interest rate divided by 12 months multiplied by the amount of debt.

Credit card	Debt	Interest rate	Monthly interest
<b>Total</b>			

As you can see, a big part of building wealth is making wise choices about debt. You need to maximize assets and minimize liabilities to maximize net worth. To manage debt, you need to know how much you have and develop strategies to control it.

When Bob decided to reduce his \$3,000 credit card debt, he analyzed his debt and developed a strategy. He listed the balance, interest rate and monthly interest on each credit card. He checked his credit score and shopped for the best rate on a new credit card. Then he transferred all his balances to that card. He cut up the old credit cards and used the interest he saved to pay toward the principal balance. He used the new card only for emergencies.

What is your credit card debt situation? Using the chart to the left, do an analysis of your own.

**My strategy for reducing credit card debt includes:**

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_

## GUARD YOUR IDENTITY

Just as you protect the security of your home with locks for your windows and doors, you should take steps to protect your identity. Secure your financial records, Social Security number and card, account numbers, and all passwords and PINs (personal identification numbers). A periodic check of your credit report can alert you if someone is illegally using credit products in your name. If you suspect unauthorized access, contact the three major credit reporting companies and place a fraud alert on your name and Social Security number.

### Some Tips to Protect Your Identity:

- Shred or destroy your bank and credit card statements and all other private records before tossing them in the trash.
- Give out your Social Security number only when absolutely necessary, and never carry both your Social Security card and driver's license in your wallet.
- Pick up mail promptly from your mailbox, and never leave outgoing mail with paid bills in an unsecured mailbox.
- Don't give out personal information on the phone, through the mail or on the Internet unless you're sure you know whom you're dealing with.

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## ⑤ Protect Your Wealth

*It is unwise to be too sure of one's own wisdom. It is healthy to be reminded that the strongest might weaken and the wisest might err.*

Mahatma Gandhi

After working hard to create personal wealth, you need to protect it. People acquire insurance to protect themselves from major financial loss. Insurance is simply a promise of reimbursement for a loss in return for a premium paid. When shopping for insurance products, consumers should match their needs with what the product offers and seek out the best deal. A solid credit history is also important because insurers use credit information to price homeowners insurance policies. You can buy insurance to cover all kinds of risks, but basic needs can be met with property, health and life insurance.

### PROPERTY INSURANCE **Auto Insurance**



State law requires that all motor vehicles have **liability** insurance to cover injury to other people or damage to their property. If you have a loan on your vehicle, your lender will also require physical damage coverage on it.

You may select a higher **deductible** (the amount you pay out of pocket before insurance kicks in) and receive a more affordable rate on the **premium** (the cost of the policy). If you have your emergency savings in place, you will feel more confident about taking out a higher-deductible policy, which will lower your premium costs.

### **Home Insurance**

**Homeowners insurance** covers your home and possessions. The personal liability coverage in a homeowners policy protects you from loss resulting from any injuries that may occur on your property. Your mortgage lender will require you to carry a certain amount of insurance coverage as long as the mortgage is in place. You may also consider a higher-deductible insurance plan to save money on your homeowners coverage.

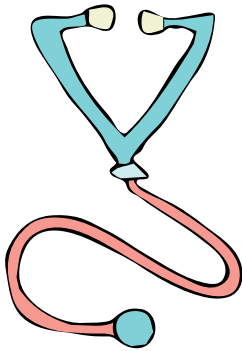
Standard homeowners coverage insures your home and its contents against loss from such risks as fire and theft. You may require special insurance for flood, earthquake or other risks specific to your area. Contact your state department of insurance for more information on insurance in high-risk areas.

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Another type of household protection, a *home warranty*, is a service contract that protects the homeowner from unexpected costs for repair or replacement of major systems. These might include heating and air-conditioning, plumbing, electrical systems or a water heater. Sellers will sometimes provide a one-year home warranty to give potential buyers added confidence. The homebuyer then has the option of renewing the warranty at the end of the year.

If you are renting your home or apartment, you should purchase *renters* or *contents insurance* to cover your possessions against loss from fire or theft. Your landlord's insurance will only cover damage to the building, not its contents. Also, if someone is hurt in your rented home, that liability is yours, not the landlord's.

## HEALTH INSURANCE **Medical Insurance**



Medical insurance pays for some, but not all, of your doctor, hospital and prescription drug costs. Many people have significant levels of debt because they didn't have medical insurance or they didn't have savings to pay the expenses that weren't covered by their health plan. Late payments and defaults on medical debt may be reported on credit reports and affect a person's credit score.

Premiums are lower on employer-provided health insurance because risk is spread over a larger group of people. Take advantage of the lower costs that employer-sponsored health plans offer, but expect to pay part of the premium out of your paycheck. In addition to medical insurance, many employers offer dental and vision plans, often at low cost.

**Flexible spending accounts.** People who are insured through their employer should consider participating in a flexible spending account (FSA) if it is offered. An employer-sponsored FSA allows employees to save pretax dollars in an account to cover deductibles, co-pays, prescription and over-the-counter drugs, and other health expenses not covered by insurance. Employees need to plan their FSA spending so they have enough saved to cover their uninsured medical expenses but not more than they can use in one year plus two and a half months. On March 15 every year, money left in an FSA from the previous year is forfeited.

If you have health insurance and your employer doesn't offer a flexible spending account, you should make sure your emergency savings account is adequate to provide a safety net against unexpected medical costs.



**Health savings accounts.** If you do not have health insurance or you need more affordable insurance, a high-deductible health plan (HDHP), coupled with a health savings account (HSA), provides medical insurance coverage and a tax-free opportunity to save for future medical needs. The premium for an HDHP is generally lower than for traditional health insurance because the deductible (the amount you pay before the insurance kicks in) is higher.

That's where the health savings account comes in. HSAs are set up at banks or other financial institutions to pay for current and future health-related costs that occur before the deductible is met and insurance takes over. Contributions to an HSA are tax-deductible, up to certain limits, even if you do not itemize deductions on your income tax return. Interest earned on the HSA account is not taxable, and withdrawals are tax-free if used for qualified medical expenses. An HSA is portable, so it stays with you even if you change jobs or retire. Plus, unspent savings in an HSA can grow year-to-year.

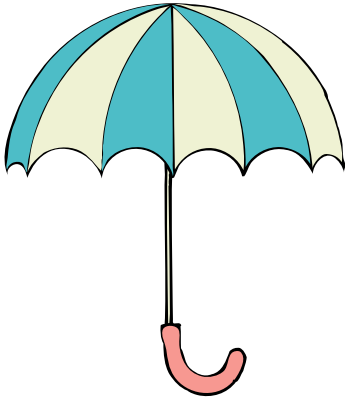
For more information about HSAs, go to [www.treasury.gov/offices/public-affairs/hsa](http://www.treasury.gov/offices/public-affairs/hsa).

**Health insurance for children.** Every state provides free or low-cost health insurance for children in low- to moderate-income households. For more information about state programs, contact the U.S. Department of Health and Human Services at 877-Kids Now (877-543-7669) or go to [www.insurekidsnow.gov](http://www.insurekidsnow.gov).

### **Disability Insurance**

Statistics show that you have a higher risk of becoming disabled than of dying before age 65. Disability insurance helps you pay living expenses if you are sick or injured and unable to work for a long time. Your employer may offer this insurance in its benefits plan. It is a good idea to buy this protection even if you have to pay for part of the premium.

## LIFE INSURANCE



The need for life insurance depends on a person's circumstances. In the event of your death, life insurance pays money to the person you choose (your beneficiary). Life insurance helps give financial protection to your children, spouse, parents or even your business.

While some types of life insurance offer savings and investment components to keep the future cost of premiums lower or to increase the death benefit, they are not a substitute for a savings or investment plan. Low-cost term insurance, often available through your employer, can offer protection for young families.

Personal accident insurance may also offer a cushion to families if a member dies or is seriously injured in an accident. This kind of insurance is often available through your employer or other provider at relatively low cost.

## LONG-TERM CARE INSURANCE

If you or a family member became very ill and needed a nursing home, who would pay for it? You would, until all your assets, and those of your spouse, are exhausted. Only then would government assistance help cover these needs. Long-term care insurance is not medical insurance, but it pays for such health-related items as nursing home, assisted living or in-home care.

Generally, the need for long-term care comes late in life, but insurance premiums are much less expensive when you are younger. Some employers offer access to long-term care insurance for employees to purchase, but most consumers have to find coverage themselves. Shopping for long-term care insurance takes research, common sense and attention to the policy's details.

### Tips for Protecting Your Wealth

There are many types of property, health and life insurance, so do your research and seek good advice.

- Take advantage of group insurance through your employer or other associations you may have.
- Study the needs of your family and decide how much you can afford to pay.
- Shop around and get at least two quotes.
- Consider a higher deductible to lower your premium.
- Ask about other discounts that may be available (for a good driving record, safety equipment, multiple policies with the same provider, etc.) to reduce your cost of coverage.
- Review your insurance coverage annually to make sure you have appropriate coverage as your situation changes.
- Like all investments, be sure to get all the facts before parting with your hard-earned money.

### Buy Insurance Wisely

Insure U, a web site sponsored by the National Association of Insurance Commissioners representing insurance regulators from across the United States, has more information on buying all types of insurance at [www.insureuonline.org](http://www.insureuonline.org).

# Review

## Redefining Wealth ▶

Now that you've read this workbook and thought about the information it contains, how would you define wealth? In the space provided, write your definition. Then compare it with the definition you wrote back on page 1. Has your definition of wealth changed?

## Resetting Your Financial Goals ▶

Now, write your financial goals and compare them with your original goals. Keep these new goals with your definition of wealth. Periodically refer to your goals and measure your **Assets** – **Liabilities** = **Net Worth** to make sure your wealth-building program stays on track.

## Using Key Wealth-Building Strategies ▶

Now, write your own strategies for building wealth. Keep in mind the following:

- Educate yourself about money.
- Establish financial goals.
- Create a budget.
- Save each month, using automatic deduction.
- Take advantage of compound interest.
- Take advantage of tax-deferred investments.
- Research and learn about the best investments for you based on your financial goals, time horizon and tolerance for risk.
- Control debt.
- Protect your wealth.

Start budgeting, saving and investing *today*. Every day counts in building wealth.



Wealth is:

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My short-term goals are:

1. \_\_\_\_\_

2. \_\_\_\_\_

3. \_\_\_\_\_

My long-term goals are:

1. \_\_\_\_\_

2. \_\_\_\_\_

3. \_\_\_\_\_

My strategies for building wealth are:

1. \_\_\_\_\_

2. \_\_\_\_\_

3. \_\_\_\_\_

My strategies for controlling debt are:

1. \_\_\_\_\_

2. \_\_\_\_\_

3. \_\_\_\_\_

*Clip the box and put it where you will see it often: inside your checkbook, on your computer monitor, where you pay your bills, on your bathroom mirror. Keep your definition of wealth and your goals firmly implanted in your mind and use your wealth-creating and debt-controlling strategies every day.*



# Glossary

**Acceleration clause** A stipulation in a loan contract stating that the entire balance becomes due immediately if other contract conditions are not met.

**Accrued interest** Interest that has been earned but not received or recorded.

**Amortization** Liquidation of a debt by making periodic payments over a set period, at the end of which the balance is zero.

**Annuity** A series of equal payments made at regular intervals, with interest compounded at a specified rate.

**Appreciation** An increase in the value or price.

**Asset** Anything an individual or business owns that has commercial or exchange value.

**Auto debit** The deduction from a checking or savings account of funds that are automatically transferred to a creditor each month. Some lenders offer interest rate discounts if loan payments are set up on auto debit at the beginning of the loan.

**Balance** The amount owed on a loan or credit card or the amount in a savings or investment account.

**Balance sheet** A financial statement showing a “snapshot” of the assets, liabilities and net worth of an individual or organization on a given date.

**Bankruptcy** A legal proceeding declaring that an individual is unable to pay debts. Chapters 7 and 13 of the federal bankruptcy code govern personal bankruptcy.

**Beneficiary** The person designated to receive the proceeds of a life insurance policy.

**Budget** An itemized summary of probable income and expenses for a given period.

**Capital** Cash or other resources accumulated and available for use in producing wealth.

**Cash flow** Money coming to an individual or business less money being paid out during a given period.

**Certificate of deposit (CD)** A type of savings account that earns a fixed interest rate over a specified period of time.

**Collateral** Assets pledged to secure a loan.

**Common stock** A kind of ownership in a corporation that entitles the investor to share any profits remaining after all other obligations have been met.

**Compound interest** Interest computed on the sum of the original principal and accrued interest.

**Credit** The granting of money or something else of value in exchange for a promise of future repayment.

**Credit card** A plastic card from a financial services company that allows cardholders to buy goods and services on credit.

**Credit report** A loan and bill payment history, kept by a credit reporting company and used by financial institutions and other potential creditors to determine the likelihood a future debt will be repaid.

**Credit reporting company** An organization that compiles credit information on individuals and businesses and makes it available for a fee.

**Credit score** A number generated by a statistical model that objectively predicts the likelihood that a debt will be repaid on time.

**Credit union** A cooperative organization that provides financial services to its members.

**Creditor** A person, financial institution or other business that lends money.

**Debit** Charges to an account.

**Debit card** A plastic card similar to a credit card that allows money to be withdrawn or the cost of purchases paid directly from the holder's bank account.

**Debt** Money owed; also known as a *liability*.

**Debt service** Periodic payment of the principal and interest on a loan.

**Deductible** The amount of loss paid by an insurance policyholder. The deductible may be expressed as a specified dollar amount or a percent of the claim amount.

**Delinquency** The failure to make timely payments under a loan or other credit agreement.

**Direct deposit** The electronic transfer of a payment from a company to an individual's checking or savings account. Many employers offer direct deposit of paychecks.

**Diversification** The distribution of investments among several companies to lessen the risk of loss.

**Dividend** A share of profits paid to a stockholder.

**Equity** Ownership interest in an asset after liabilities are deducted.

**Face value** The principal amount of a bond, which will be paid off at maturity.

**Fair market value** The price a willing buyer will pay and a willing seller will accept for real or personal property.

**Federal Deposit Insurance Corp. (FDIC)** A federally chartered corporation that insures bank deposits up to \$250,000.

**Finance company** A company that makes loans to individuals.

**Financing fee** The fee a lender charges to originate a loan. The fee is based on a percentage of the loan amount; one point is equivalent to 1 percent.

**Flexible spending account** An employer-sponsored account that allows employees to save pretax dollars to cover qualified medical or dependent care expenses.

**Foreclosure** The legal process used to force the payment of debt secured by collateral whereby the property is sold to satisfy the debt.

**401(k) plan** A tax-deferred investment and savings plan that serves as a personal retirement fund for employees.

**Health savings account** A tax-advantaged personal savings account, set up to be used exclusively for medical expenses; must be paired with a high-deductible health insurance policy.

**High-deductible health plan** A health insurance policy that requires the policyholder to pay more out-of-pocket medical expenses but usually has lower premiums than traditional health insurance plans.

**Individual development account (IDA)** A type of savings account, offered in some communities, for people whose income is below a certain level.

**Individual retirement account (IRA)** A retirement plan, offered by banks, brokerage firms, mutual funds and insurance companies, to which individuals can contribute each year on a tax-deferred basis.

**Inflation** A sustained increase in the prices of goods and services.

**Installment plan** A plan requiring a borrower to make payments at specified intervals over the life of a loan.

**Insurance premium** The amount of money required for coverage under a specific insurance policy for a given period of time. Depending on the policy agreement, the premium may be paid monthly, quarterly, semiannually or annually.

**Interest** A fee for the use of money over time. It is an expense to the borrower and revenue to the lender. Also, money earned on a savings account.

**Interest rate** The percentage charged for a loan, usually a percentage of the amount lent. Also, the percentage paid on a savings account.

**Investing** The act of using money to make more money.

**Investor** An organization, corporation, individual or other entity that acquires an ownership position in an investment, assuming risk of loss in exchange for anticipated returns.

**Leverage** The ability to use a small amount of money to attract other funds, including loans, grants and equity investments.

**Liability** Money an individual or organization owes; same as debt. Also, a kind of insurance for the policyholder's legal obligation to pay for either bodily injury or property damage caused to another party.

**Lien** A creditor's claim against a property, which may entitle the creditor to seize the property if a debt is not repaid.

**Liquidity** The ease with which an investment can be converted into cash.

**Load** The fee a brokerage firm charges an investor for handling transactions.

**Loan** A sum of money lent at interest.

**Management fee** The fee paid to a company for managing an investment portfolio.

**Market value** The amount a seller can expect to receive on the open market for merchandise, services or securities.

**Maturity** The time when a note, bond or other investment option comes due for payment to investors.

**Money market account** A type of savings account offered by a financial institution.

**Mortgage** A temporary and conditional pledge of property to a creditor as security for the repayment of a debt.

**Municipal bond** A bond issued by cities, counties, states and local governmental agencies to finance public projects, such as construction of bridges, schools and highways.

**Mutual fund** A pool of money managed by an investment company.

**Net worth** The difference between the total assets and total liabilities of an individual.

**Par value** The nominal, or face, value of a stock or bond, expressed as a specific amount on the security.

**Predatory lending** Targeting loans to seniors, low-income and other people to take advantage of their financial status or lack of financial knowledge.

**Pretax** A person's salary before state and federal income taxes are calculated.

**Prime rate** The lowest interest rate on bank loans, offered to preferred borrowers.

**Principal** The unpaid balance on a loan, not including interest; the amount of money invested.

**Promissory note** A written promise on a financial instrument to repay the money plus interest.

**Qualified plan** A tax-deferred retirement plan for the self-employed.

**Return** The profit made on an investment.

**Revenue bond** A type of municipal bond backed by revenue from the project the bond finances.

**Risk** The possibility of loss on an investment.

**Savings account** A service depository institutions offer whereby people can deposit their money for future use and earn interest.

**Stock option** The right to buy or sell a corporation's stock at a predetermined price or calculable formula; sometimes used as part of employee compensation.

**Stockholder** A person who owns stock in a company and is eligible to share in profits and losses; same as *shareholder*.

**Tax-deferred** Phrase referring to money that is not subject to income tax until it is withdrawn from an account, such as an individual retirement account or a 401(k) account.

**Term** The period from when a loan is made until it is fully repaid.

**Terms** Provisions specified in a loan agreement.

**Treasury bill** A short-term investment issued by the U.S. government for a year or less.

**Treasury bond** A government security with a term of more than 10 years; interest is paid semiannually.

**Treasury Inflation-Protected Security (TIPS)** A Treasury bond or note that is tied to inflation so that the principal amount of the investment increases or decreases according to the annual inflation rate.

**Treasury note** A government security with a maturity that can range from two to 10 years; interest is paid every six months.

**U.S. savings bond** A nontransferable, registered bond issued by the U.S. government in denominations of \$50 to \$10,000.



# Wealth-Building Resource Guide

## INTRODUCTION

The following resources can be used to learn more about building personal wealth. The list includes sources of information on financial literacy for adults and youth, budget and debt management, and consumer protection. This guide is not intended to be all-inclusive; there are many additional national, state and local resources that can provide additional information on building wealth for a more secure financial future.

## PERSONAL FINANCIAL EDUCATION

### AARP

(888) 687-2277  
[www.aarp.org](http://www.aarp.org)

### America Saves

(202) 387-6121  
[www.americasaves.org](http://www.americasaves.org)

### American Bankers Association Education Foundation

(800) 226-5377  
[www.aba.com/abaef/consumers.htm](http://www.aba.com/abaef/consumers.htm)

### American Council of Life Insurance

(202) 624-2000  
[www.acli.com](http://www.acli.com)

### American Financial Services Association Education Foundation

(202) 296-5544  
[www.afsaef.org](http://www.afsaef.org)

### American Institute of Certified Public Accountants

(888) 777-7077  
[www.360financialliteracy.org](http://www.360financialliteracy.org)

### American Savings Education Council

(202) 659-0670  
[www.choosetosave.org](http://www.choosetosave.org)

### The Beehive/One Economy

(202) 393-0051  
[www.thebeehive.org](http://www.thebeehive.org)

### CFED

(202) 408-9788  
[www.cfed.org](http://www.cfed.org)

### Fannie Mae

(202) 752-7000  
[www.fanniemae.com](http://www.fanniemae.com)

### Federal Citizen Information Center

(800) 878-3256  
[www.consumer.gov](http://www.consumer.gov)  
[www.pueblo.gsa.gov](http://www.pueblo.gsa.gov)

### Federal Deposit Insurance Corporation

(877) 275-3342  
[www.fdic.gov/consumers/consumer/moneysmart](http://www.fdic.gov/consumers/consumer/moneysmart)

### Federal Reserve Board

(212) 720-6134  
[www.federalreserveeducation.org](http://www.federalreserveeducation.org)

### Freddie Mac

(703) 903-2000  
[www.freddiemac.com](http://www.freddiemac.com)  
[www.freddiemac.com/creditsmart](http://www.freddiemac.com/creditsmart)  
[www.freddiemacfoundation.org](http://www.freddiemacfoundation.org)

### Internal Revenue Service

(800) 829-1040  
[www.irs.gov](http://www.irs.gov)

### Louisiana Bankers Association

(225) 387-3282  
[www.lba.org](http://www.lba.org)

### Louisiana Cooperative Extension

(225) 578-4161  
[www.lsuagcenter.com](http://www.lsuagcenter.com)

### State of Louisiana – Office of Financial Institutions

(225) 925-4660  
[www.ofi.state.la.us](http://www.ofi.state.la.us)

### National Credit Union Administration

(703) 518-6340  
[www.ncua.gov](http://www.ncua.gov)

### National Endowment for Financial Education

(303) 741-6333  
[www.nefe.org](http://www.nefe.org)  
[www.smartaboutmoney.org](http://www.smartaboutmoney.org)

### Native Financial Education Coalition

(605) 342-3770  
[www.nfec.info](http://www.nfec.info)

## DIRECT DEPOSIT & YOU

Many people who receive federal benefits checks, such as Social Security, Supplemental Security Income, Veterans Affairs or other government checks, enroll in direct deposit. Not only is it safer (no direct deposit has ever been stolen), it is far more convenient, and it gives you more control over your money than a mailed check. Call the toll-free Go Direct helpline at (800) 333-1795 or (800) 333-1792 en Español, or go to [www.GoDirect.org](http://www.GoDirect.org) for more information and other sign-up options.

## ELECTRONIC TRANSFER ACCOUNT

For a low-cost option for direct deposit, consider an ETA account. The Electronic Transfer Account, or ETA<sup>SM</sup>, allows you to have your federal benefit, wage, salary and retirement payments deposited directly into your bank account—automatically, electronically and safely. Open a low-cost ETA at a federally insured bank, credit union, or savings and loan. Financial institutions offering the ETA have decals in their windows or lobbies identifying them as certified ETA providers. To find an ETA provider in your area, visit the ETA web site, [www.eta-find.gov](http://www.eta-find.gov), or call toll-free, (888) 382-3311.

**New Mexico Regulating and Licensing Department  
Financial Institutions Division**  
(505) 476-4885  
[www.rld.state.nm.us/FID](http://www.rld.state.nm.us/FID)

**New Mexico State University  
Cooperative Extension Service**  
(505) 646-2198  
<http://cahe.nmsu.edu/ces/families/families.html>

**Texas Cooperative Extension**  
(979) 845-7907  
<http://texasextension.tamu.edu>

**Texas Department of Banking**  
(512) 475-1337  
[www.banking.state.tx.us/dss/fe.htm](http://www.banking.state.tx.us/dss/fe.htm)

**Texas Saves**  
(877) 897-2830  
[www.txsave.org](http://www.txsave.org)

**Texas Society of CPAs**  
(800) 428-0272  
[www.valueyourmoney.org](http://www.valueyourmoney.org)

**U.S. Department of Agriculture  
Cooperative State Research,  
Education and Extension Service**  
(202) 690-2674  
[www.csrees.usda.gov](http://www.csrees.usda.gov)

**U.S. Department of Labor  
Women's Bureau**  
(800) 827-5335  
[www.wiseupwomen.org](http://www.wiseupwomen.org)

**U.S. Department of the Treasury**  
(800) 722-2678  
[www.treasurydirect.gov](http://www.treasurydirect.gov)

**U.S. Financial Literacy and  
Education Commission**  
(888) 696-6639  
[www.mymoney.gov](http://www.mymoney.gov)

**U.S. Social Security Administration**  
(800) 772-1213  
[www.ssa.gov](http://www.ssa.gov)

**Women's Institute for Financial  
Education**  
(760) 736-1660  
[www.wife.org](http://www.wife.org)

**Women's Institute for Secure  
Retirement**  
(202) 393-5452  
[www.wiserwomen.org](http://www.wiserwomen.org)

## FINANCIAL EDUCATION – YOUTH

**American Financial Services  
Association**  
(888) 400-7577  
[www.moneyskill.org](http://www.moneyskill.org)

**Banking on Our Future**  
(877) 592-4673  
[www.bankingonourfuture.org](http://www.bankingonourfuture.org)

**Federal Reserve Board**  
(212) 720-6134  
[www.federalreserveeducation.org](http://www.federalreserveeducation.org)  
[www.federalreserve.gov/kids](http://www.federalreserve.gov/kids)

**Jump\$tart Coalition for Personal  
Financial Literacy**  
(888) 453-3822  
[www.jumpstart.org](http://www.jumpstart.org)

**Junior Achievement**  
(719) 540-8000  
[www.ja.org](http://www.ja.org)

**National Council on Economic  
Education**  
(800) 338-1192  
[www.ncee.net](http://www.ncee.net)

**National Endowment for Financial  
Education**  
(303) 741-6333  
[www.nefe.org](http://www.nefe.org)

**North American Securities  
Administrators Association**  
(202) 737-0900  
[www.nasaa.org](http://www.nasaa.org)

**Sallie Mae**  
(888) 272-5543  
[www.salliemae.com](http://www.salliemae.com)

**U.S. Department of the Treasury  
Money Math**  
(800) 722-2678  
[www.savingsbond.gov/mar/marmoneymath.htm](http://www.savingsbond.gov/mar/marmoneymath.htm)

## **BUDGET AND DEBT MANAGEMENT**

**Consumer Credit Counseling  
Services of Greater Dallas, Inc.**  
Colorado, New Mexico, Oklahoma  
and Texas  
(800) 249-2227  
www.cccs.net

**Consumer Credit Counseling  
Services of the Gulf Coast Area,  
Inc.**  
(713) 923-2227  
www.cccsintl.org

**Credit Coalition  
Houston Area**  
(713) 224-8100  
www.creditcoalition.org

**CCCS of Greater San Antonio  
Austin, Laredo and San Antonio**  
(800) 410-2227  
www.cccssa.org

**Get Checking**  
(480) 629-7683  
www.getchecking.org

**Homeownership Preservation  
Foundation**  
(888) 995-HOPE  
www.995hope.org

**Money Management International  
Various locations across U.S.,  
including Texas, Louisiana and  
New Mexico**  
(800) 873-2227  
www.moneymanagement.org

**National Foundation for Credit  
Counseling**  
Various locations across U.S.,  
including Texas, Louisiana and  
New Mexico  
(800) 388-2227  
www.debtadvice.org  
www.nfcc.org

**Operation HOPE, Inc.**  
(888) 388-HOPE  
www.operationhope.org

## **CONSUMER PROTECTION**

**Federal Deposit Insurance  
Corporation**  
(415) 808-8049  
www.fdic.gov/consumers/  
index.html

**Federal Trade Commission**  
(202) 326-2222  
www.ftc.gov

**First Gov for Consumers**  
(800) 333-4636  
www.consumer.gov/yourmoney.  
htm

**Investor Protection Trust**  
(202) 775-2113  
www.investorprotection.org

**Louisiana Department of  
Insurance**  
(800) 259-5300  
www.ldi.state.la.us

**Louisiana – Office of the Attor-  
ney General**  
(800) 351-4889  
www.ag.state.la.us

**National Association of Insur-  
ance Commissioners**  
(816) 842-3600  
www.insureuonline.org

**New Mexico Insurance Division**  
(800) 947-4722  
www.nmprc.state.nm.us/id.htm

**New Mexico – Office of the  
Attorney General**  
(800) 678-1508  
www.nmag.gov/default.aspx

**Securities and Exchange  
Commission**  
(800) 732-0330  
www.sec.gov

**Texas Department of Insurance**  
(800) 252-3439  
www.tdi.state.tx.us

**Texas – Office of the Attorney  
General**  
(800) 252-8011  
www.oag.state.tx.us

**Texas State Securities Board**  
(888) 663-0009  
www.texasinvestored.org

## **BOOKS QUOTED IN PUBLICATION**

*Getting Rich in America:  
8 Simple Rules for Building a  
Fortune and a Satisfying Life*  
Dwight R. Lee and  
Richard B. McKenzie  
1999, Harper Business

*It's About the Money!  
The Fourth Movement of the  
Freedom Symphony: How to Build  
Wealth, Get Access to Capital,  
and Achieve Your Financial  
Dreams*  
Reverend Jesse L. Jackson, Sr.  
and Jesse L. Jackson, Jr.  
with Mary Gotschall  
1999, Times Business/Random  
House

*The Millionaire Next Door:  
The Surprising Secrets of  
America's Wealthy*  
Thomas J. Stanley  
and William D. Danko  
1996, Longstreet

*We hope that you have found Building Wealth to be a useful tool. We invite you to visit our web site and send us your Building Wealth success stories.*



Richard W. Fisher, President and CEO  
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[www.dallasfed.org](http://www.dallasfed.org)



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