

Budgeting Basics for Everyone

Learning How to Manage Your Income

Money and the college student

You're in college, so it's too early to be thinking of having a personal financial plan. That's for after you graduate and you're making the big bucks, right? Unfortunately, many college graduates who believe this start their new lives after graduation weighed down with debt that often follows them for the rest of their lives. You don't need to be one of them, but now is the time to make sure that you don't start down that road.

You have to juggle all of your own finances. You may have what seems like a large amount of money from student loans, financial aid, your hard-earned savings, and financial support from your family. And then there's the credit card, or cards, that are suddenly coming your way. You buy clothes, gas, beer, and concert tickets. You party. Before you know it, you find yourself unable to pay your credit card bills, or you have no money left to buy books for your classes

According to an advisor at a major university, more students drop out of college due to credit card debt than to academic failure. The best way to prevent this is to adopt a spending plan early in your first semester, and stick to it.

Like anybody else, college students are usually surprised at how much the little expenses add up to. A cup of coffee at the local coffee shop before classes each morning can total \$46 a month, or nearly \$200 a semester. Smoking is one of the most costly habits. At \$3.50 a pack, a pack-a-day habit can total well over \$400 a semester. It doesn't take much to reach thousands of dollars a semester on incidentals. Students who get a handle on their spending and their available funds early can avoid the stress of being unable to pay off their bills and having to work more and more hours during college in order to juggle their finances.

The basics of budgeting are the same for students as they are for anybody else: list the sources of your income, such as savings from your summer jobs, financial support from your parents, financial aid from the school, scholarships, and income from your job if you have one. Then list your expenses, such as tuition, books, groceries, gas, entertainment, etc., in as much detail as possible.

If your expenses are less than your income, you're in good shape as long as you stick to your spending plan. If your expenses are **MORE** than your income, you need to find ways to cut spending or increase your income. A college degree is no guarantee of an ability to manage your money wisely. It takes effort and discipline, and the time to start is now.

The Budgeting Process

Budgeting, a management process follows these steps:

1. Communicating among family members.
2. Considering personal or family situation.
3. Setting goals.
4. Estimating income.
5. Estimating expenses.
6. Balancing the budget.
7. Putting budget into action.
8. Adjusting budget as necessary.
9. Use for future planning.

Communication

The first step is communication with all family members. If single, this involves honest thinking and communicating with yourself. Studies have shown there is considerably less argument in marriages where both spouses share in making financial decisions and where they openly communicate with the children about the financial situation. Money is a common problem for people. When family members have different values and attitudes about spending and saving money, or when people strive for unrealistic goals, there is potential conflict. When people don't "talk things out," even the most workable spending plan may not work.

Communication isn't always easy, but it is important. Generally, the more open the communication about finances, the better the quality of the financial decisions.

Overcoming money problems takes honest and candid communication, time and effort. Arrange a time when all people involved can talk about money. Meet on a regular basis. Choose a location where you won't be interrupted. Recognize that whoever earns the money doesn't also earn the right to dictate how it should be spent. Family members, including children old enough to understand, need to make decisions about money as a team. They'll be more satisfied with the decisions if they helped make them. Clearly identify the issue at hand; stick to the subject. Let each person freely state his or her wants, needs, and personal feelings. Avoid judging or criticizing others. Encourage statements beginning "I think" or "I feel," avoid "You always" and "You never." Listen carefully. Finally, be willing to negotiate--compromise is the key to successful communication about money.

Your Situation

Situations differ from person to person and from family to family. No two people or families are exactly alike in size, ages, tastes, talents, occupations, lifestyles, expenses, income, and past history. These characteristics make a difference in the way a particular person views money and makes money decisions. Family economics experts favor tailoring each plan for the particular situation involved.

Family size. Whether single or married makes a difference in your budgeting plan. And whether you're married or single, you may have one or more children or other dependents. Not even all married families with children are similar. You may have a family where it is the first marriage for each spouse and all of the children belong to both of you, or you may have a stepfamily where one or both spouses were married previously and have a child or children from

that previous marriage. The exact number of people in the family will make a difference.

Ages. As a young single person, your expenses and income will be different from those of a retired, single person. Likewise, a family with younger children will have different financial circumstances than a family with children near college age. People need to provide for various expenses, including savings and investments, depending on their ages. You can't begin to plan for retirement income, for example, when you reach age 60.

Lifestyles. Each person's tastes, talents, values and attitudes will also make a difference in the total financial budget. Whether you have a taste for prime rib or hot dogs, or whether you consider it important to set aside money for retirement or believe in spending it to day while you have it will make your particular budget very special for you. Each person's occupation and talents will affect the budget. By using a certain talent you may be able to cut expenses for home decorating, but you may also find you have a larger cash outlay for tools and supplies so that person can practice his or her talent.

Income and expenses. Whether income is regular, such as a paycheck every two weeks, or irregular, such as that received by a farmer or other person in business for him or herself, will determine how a budget is set up and followed. Whether expenses are regular or irregular also makes a difference in the budget.

Potential changes. Are you planning a major change during the coming year such as a move, changing jobs, buying a house, getting married, having a child, entering the job market or buying a new roomful of furniture? Every major change will affect the budget. A workable budget will not tell what is a good way to spend your money, since what is good for one person or family may not necessarily be good for the next person. But a budget can help you be sure you are spending your financial resources in ways that are the most beneficial and satisfying to you.

Setting Goals

Short-term goals are what you want to have or do within one year, while long-term goals are to be achieved during the years to follow. People who set goals for themselves are often more successful than those who don't--they know where they're going and what they want to achieve.

Write down your goals. Then, estimate how much the goal will cost. Determine when you want to achieve your goal. Finally, estimate how much money you need to set aside each year, or even each month, to reach your goal. Then, set aside that amount before you begin to use your income to meet current expenses.

Examples of long-term goals include saving for a down payment for a house, providing for retirement income, and developing an investment plan. Short-term goals include braces for children's teeth, replacing a living room sofa, turning the basement into a family room, or taking a family vacation.

Income

Add together all sources of income including take home pay, interest, dividends, bonuses, etc. If you're self-employed, determine just how much you have available for living expenses by

examining personal and family goals, business goals, and living and business expenses. If your income fluctuates, underestimate your income and overestimate expenses. Avoid relying heavily on bonuses or overtime pay.

If you don't have a regular income, you may find it beneficial to set up a budget, conservatively estimating your income and overestimating your anticipated expenses. Plan your spending for minimum living expenses each month. Then, when income does arrive, put it into the bank and draw it out following your plan. If you get a large check, resist the temptation to buy something extra; that money might have to last for more weeks or months than you think. If, as the year goes on, you realize your earnings are falling short of covering your minimum living expenses, immediately adjust your budget downward. If there's extra money beyond living expenses, put it in the bank or savings and loan or credit union. Then, the following year, use this surplus for those "extras" such as a vacation, new refrigerator, or special investment. By taking special purchases out of your accumulated surplus from the previous year, you'll find it easier to keep your living expenses within the limits you expected for the year.

If you can predict when your smallest income month or months are, a second way to handle irregular income is to develop a budget using that smallest income amount as the basic monthly income. Plan your expenses to fall under that amount. Then, develop a supplemental plan for using income above the minimum amount. That supplemental plan should also include a priority listing which will help you know which item will be bought first, which second, etc. It would also be to your advantage to work with insurance companies and the others to schedule as many of the irregular expenses as possible to fall during the higher income months.

A third way to handle irregular income would be to figure basic expenses for the months you expect to receive little or no income. For example, suppose you expect no income for three months, and your basic living expenses are \$2,250 for those three months. During the rest of the year a proportionate share of the amount needs to be set aside. That is, one ninth of \$2,250, or \$250, needs to be set aside each of the nine months for using during the three-month period when you expect no income.

Fixed Expenses

The next step is to decide how income will be spent during the year. First, figure fixed expenses. Examples include rent or mortgage payment, utilities, installment loans, credit card minimums, and babysitting while both parents are employed. Savings, including savings for goals and savings for an emergency fund, should be considered as fixed expenses.

Credit debt payments. An important part of fixed expenses are those that go for credit debt repayment, ranging from the mortgage payment for your home to various charge accounts and credit card bills. A guideline to remember is that credit debt payments, excluding mortgage, should take no more than 15-20 percent of your take-home pay monthly. That limit could be higher (if you are a two-income family with no children and no home mortgage) or lower (if you have a fairly new mortgage with interest rates at 11 percent or more, have just one income, and several young children).

Savings for goals. If you don't make goal savings a fixed expense and pay yourself first, as the saying goes, you'll probably find it difficult, if not impossible, to accumulate savings to reach your goals. It just doesn't work for most of us to say we'll put what's left at the end of the month

into the savings account.

Emergency fund savings. You need to put aside an amount each month to help cover emergencies, both expected and unexpected. Expected emergencies are expenses such as paying the insurance deductible when you have an accident or paying the insurance premium or replacing the refrigerator. Some you can predict and others you can't. Experts now recommend keeping two months' living expenses in a fairly liquid, interest-bearing account that is readily available. An additional one to four months' living expenses might also be kept in slightly less readily available places such as certificates of deposit, money market funds or mutual fund shares. The exact amount you need in emergency fund reserve will depend on what insurance coverage and other assets you have, how stable your income is, family size, and earning potential of all family members.

Flexible Expenses

These are the day-to-day expenses that change frequently and are often the hardest to account for. Examples include food, clothing, household expenses, medical care, a part of your utilities bills, and entertainment. This is the part of the budget where the greatest adjustments can be made when necessary. If you have no records to help you estimate what your various monthly expenses are for flexible items, keep track of your expenses for two or three months to help you get a better idea.

Irregular Expenses

Some major fixed expenses come up periodically throughout the year. Insurance premiums and taxes are good examples. So are organization dues, magazine subscriptions, and holiday gifts. These and other irregular expenses will be flexible in both amount and/or timing. You'll never be sure just when you have to pay that insurance deductible because of an accident or just what amount you'll need for back-to-school expenses or for replacing the furnace. Look over your past records and make "educated guesses" as to when irregular expenses are likely to occur. Total up the amount you'll likely need during the year. By dividing that figure by 12, you'll have the amount to set aside each month in your emergency fund for irregular expenses.

Balance the Budget

Subtract fixed expenses, including an amount for both types of savings, from your expected income. Then, subtract the total amount of flexible expenses from what is left of income. If you need to cut back on your expenses, start first with the flexible expenses, then move to irregular expenses, and finally, to fixed expenses. If you have a surplus after subtracting expenses from income, consider adding more to your goal-related savings.

Put Your Plan Into Action

This is probably the hardest step in using a budget. Keep records of actual spending and compare them with your budget plan at the end of the month.

Adjust Budget Plan

Adjust budget plan figures if necessary. It may take several months of adjusting and re-adjusting before your plan works smoothly.

Use for Future Planning

The real payoff of working with a budget plan and keeping records comes when you use your past year's budget and records to plan for the future. Budget records can help you pinpoint spending leaks or spot potential trouble before it occurs.

Budgeting Systems

If you are single, it will be relatively easy to find and use a system. Budgeting, to be effective, needs some record keeping. Whether you choose to use a checking account system, a ledger system, or a combination of the two, you'll probably also need to have a savings account for your emergency fund. Keep the system as simple as possible, yet with enough detail to satisfy you.

In a family situation, things get more complicated. You may want to consider separate checking accounts, either "yours and mine" or "yours, mine and ours." Separating checking accounts, at least for personal expenses, will be beneficial in case of divorce or death, since ownership will be established. With this system you can divide expenses so that each partner is responsible for paying certain ones. You'll also need to decide who handles the bookkeeping. In some marriages, one partner controls the money and doles out funds to both the spouse and children. Such a system can cause problems, particularly if the controller dies without other family members understanding the system. Whatever system you choose to use, remember it is best when worked out with all family members.

Why Keep Records

- You need them at tax time. Complete records make filling out income tax forms easier and quicker.
- You need to maintain control of your expenses. Records can help you keep track of where the money is going.
- Records can help pinpoint potential trouble spots before they occur.
- Records will help you make decisions and plan future spending.

Records are valuable only to the extent you use them to help plan your financial future.

Why People Don't Keep Records

Some reasons people fail to keep records or quit once they've started:

- Failing to review their plan and records so adjustments can be made when necessary.

- Failing to find a budgeting system that fits their situation.
 - Trying to plan for too long a time period. For most actual budgeting, plan for six or even three months at a time.
 - Failing to have the cooperation and support of all people involved.
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Budgeting Tips

Keep it simple. Don't detail your plan to the penny. Keep track to the nearest dollar or even the nearest five dollars. This works only if you set your "breaking point" and stick to it. For example, if you prefer to keep track to the nearest dollar, set \$.50 as your "breaking point." If the amount to be recorded is \$21.49, you drop the cents and write down 21 dollars. But, if the amount is \$21.50, you write 22 dollars in your records. Such a system keeps some of the drudgery out of record keeping.

Be realistic. Consider all expenses, including vacations, spending money, alcohol, tobacco and hobbies. To build in a margin of safety in your plan, overestimate your expenses and underestimate your income. Keep trying until you find a system that works for you.

Provide for personal allowances for everyone in your plan. Then, give each person total control of his or her allowance. By providing everyone with an allowance, no matter how small, you are giving everyone money to "blow" when the urge comes.

Don't try to use someone else's budget and expect it to work for you. When you see a budget in the newspaper or magazine, realize it is for a particular situation or for an "average" or "typical" family. We have to tailor-make a spending plan to fit us.

Distinguish between wants and needs. Buy what you need first. The wants belong in the "what's left over" category.

Borrow with care. Remember, you create a fixed expense each time you charge something or pay "on time."

Plan for and develop an emergency fund.

How to Set Up a Successful Budget

Setting up a budget that will work for you is the first step in Financial Planning. Here's how to do it right.

Difficulty Level: **Average**

Time required: **1 to 3 hours**

Here's How:

1. Start with a budget worksheet (see attached document).
2. Go through your checkbook or bills for the last two to three months and add and delete categories from the worksheet to fit your expenditures.
3. Think about your hobbies and your habits and be sure to add categories for these expenses.
4. Go through your pay stubs and calculate your average monthly gross pay.
5. Do the same for any interest income, dividends, bonuses, or other miscellaneous income.
6. For each expense category, try to determine a budget amount that realistically reflects your actual expenses while setting targeted spending levels that will enable you to save money.
7. Once you're comfortable with your expense categories and budgeted amounts, enter expenditures from your checkbook from the last month.
8. Keep track of cash expenditures throughout the month and total and categorize these at the end of each month.
9. Subtotal the income and expense categories.
10. Subtract the total expenses from the total income to arrive at your net income.
11. If the number is negative, your expenses are greater than your income. Your situation can probably be greatly improved by changing your spending habits.
12. If you have a positive net income, transfer most of it to a savings or investment account at the end of each month. Extra cash left in a regular checking account has a way of getting spent.
13. After you've tracked your actual spending for a month or two, analyze your spending to identify where you can comfortably make cuts.
14. Once you've got the budgeting process in place, take an in-depth look at your largest spending categories, brainstorm about ways to reduce spending in specific categories, and set realistic goals

Update your budget and expenses monthly.

The following is an example of a basic budgeting sheet used to figure Net Income

Income:	
Wages Paid	
Bonuses	
Miscellaneous Income	
Income Subtotal:	
Expenses:	
Mortgage/Rent	
Home Owners/Renters Insurance	
Home Owners Property taxes	
Utilities:	
Electric	

Gas	
Water	
Cable	
Telephone	
Hom Repairs/Maintenance	
Car Payments	
Gasoline/Oil	
Auto Repairs/Maintenance	
Car Taxes/Tags	
Auto Insurance	
Child Care	
Computer Expense	
Entertainment/Recreation	
Groceries	
Toiletries/Household Products (Soap, Cleaning Supplies, etc...)	
Clothing	
Eating Out	
Gifts/Donations (Such as Church tithing)	
Healthcare (Medical/Dental/Vision/Including Insurance)	
Hobbies	
Credit Cards/Interest Fees	
Magazines/Newspapers	
Federal Income Tax (amount taken out of check)	
State Income Tx (amount taken out of check)	
Social Security/Medicare Tax (Taken out of check)	
Pets	
Miscellaneous Expense	
Expenses Subtotal:	
Net Income (Income less(-) Expenses)	

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