

Setting Your Goals: Financial Security May be a Place to Start

Why is it that some families take in stride many of life's financial challenges (from car repairs and medical bills to a job layoff or death), while other families, of similar income, take years to recover? Much of the answer is in their **financial security**: the family's protection against financial risk.

At the core of our efforts to maintain financial security is our desire to continually improve or at least maintain our lifestyle. **Being financially secure means that it is unlikely we'll have to do without something that is important to us, even if we're faced with events that significantly increase our expenses or reduce our income.**

While there is no way to guarantee that we won't face financially challenging events, there are several ways we CAN increase the resources we would have available if they should occur.



Savings

An **emergency savings fund** may be used for minor emergencies like car repair or medical bills, but **its main purpose is to protect against the ultimate emergency: loss of income.** The ideal emergency fund provides enough money to cover household expenses for **three to six months**. If you're starting from scratch this may take years to build up, but it still pays to start. Every dollar saved is a dollar that keeps you more than "a paycheck away" from financial disaster.

B. Wollan, Draft, 4/99

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Getting started:

How much money does your family spend in a month? Multiply that amount by 3. The result might be your *eventual* goal for your emergency fund. **Start with a moderate goal** you can reach in the short term -- perhaps you'll aim for \$200 first. Set that aside, try not to touch it, and keep saving. When you get to \$500, give yourself a hand and have a little party. And keep saving.

Where to put emergency funds:

Emergency funds need to be safe and accessible. Part of your fund may be in a traditional savings account. To earn a higher return, you may choose to put part of your emergency fund in a money market fund or another safe and accessible account.

Insurance

Adequate insurance coverage forms a second essential component of financial security. *Health, auto, and homeowner's/renter's insurance protect you against direct financial losses* -- personal expenses you may incur due to illness, property damage or loss. In evaluating insurance policies, consider a worst-case scenario -- how large might medical expenses be, what would it cost to replace lost/damaged property? In addition, consider other resources you have available to cover lower-cost expenses; you may find that lower premiums make it worthwhile to purchase a policy with a higher deductible, even though your out-of-pocket expense would be larger if you experience a loss.

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Auto and homeowner's/renter's insurance also provide protection against liability losses -- costs that may be charged to you if you were responsible for causing injury or property damage to someone else. Another product, *umbrella liability insurance*, pays for personal (not professional) liability expenses that exceed the limits of your other liability policies. When considering how much liability insurance you need, consider:

- 1) the potential magnitude of expenses for which you could be held responsible (medical treatment costs, property damage costs); and
- 2) the value of the assets you could lose if you did not have adequate liability coverage.

An often-neglected insurance product that is critical to wage-earners is ***disability insurance***. If a disability made you unable to work, either temporarily or permanently, disability insurance would replace part of your income. Find out about disability policies available through your employer, or explore other options. When examining disability policies, look at: the definition of disability; the level of benefits provided; the waiting period (30 - 180 days) before benefits begin; and the number of years benefits will be paid.

Life insurance protects surviving family members after a death. The primary purposes of life insurance are to replace some (or all) of the income which would have been provided by the decedent, and/or to pay for some of the tasks (child care, transportation...) which the decedent had carried out. In general, life insurance is most important for wage earners and homemakers with dependents. When purchasing life insurance, first decide how much is needed and what type of policy to purchase.

For more information about meeting your insurance needs, see ISU Extension's Money Mechanics fact sheet series.

Credit

Decisions about **credit** also affect your financial security. **Credit is a valuable resource; it is wise to make sure you can obtain credit if you need it.** In addition, a low debt load reduces the financial strain you might experience at a time of financial difficulty or crisis.

Some ways to ensure your access to credit:

- ⇒ have credit in your own name;
- ⇒ pay your bills on time; and
- ⇒ avoid taking on more debt than you can reasonably handle.

When you have a low debt load and a good credit history, you also put yourself in a position to be able to shop around for favorable credit terms, thus reducing the cost of the credit you use.

Financial security elements interact

Decisions about insurance, savings, and credit use must be viewed in relationship to each other.

- ◆ If you have little or no savings, can you afford a high deductible on your insurance policies?
- ◆ If you have a 180-day waiting period on your disability insurance policy, what does that mean for the amount of emergency savings you need?
- ◆ If your emergency fund is low, can you afford to take on much debt -- would you be able to pay the debt off if your income was reduced?

A fourth element also plays a role in financial security decisions. **Income security** varies from family to family. Families with only one wage earner need greater financial security than families with two wage earners whose income comes from separate sources. Families with irregular income have greater need for strong savings and low debt load than families whose income is stable from month to month.

The First Step to Security

Living beneath your means is a prerequisite to financial security. You cannot be financially secure if your expenses exceed your income. In that negative cash flow situation, you are increasing your debt and/or decreasing your savings, *and* you are becoming accustomed to a lifestyle which you cannot afford to maintain.

Creating a positive cash flow is always the first step to security, and puts you in a position build your savings and/or pay off debt. Gradually increasing your overall security by building savings, reducing debt, and purchasing insurance that meets your needs is the best way to ensure that you'll be able to take in stride any financial emergencies that come your way.