

WISE FINANCIAL LITERACY CERTIFICATION TEST

Topic Check List

Topics that are often problematic for students

Money

- ✓ **Sources of income:** wages, rentals, interest, capital, profits, investments, entrepreneurship
- ✓ **Exemption (aka an allowance) and how does it work:** allowance is used to reduce amount of taxed income
- ✓ **Liquidity—what does it mean; what products are liquid:** the degree of ease in which assets can be sold
- ✓ **Gift cards and how they work (a monthly inactivity fee may begin after 12 months):** closed loop system and open loop system
- ✓ **Discretionary income or budget surplus:** not allocated for food or shelter
- ✓ **Money orders (high rate of counterfeits):** A **money order** is a payment order for a pre-specified amount of money and is purchased at different types of stores – it is used like a check. They are usually limited in maximum face value to some specified figure (for example, the United States Postal Service limits domestic postal money orders to US \$1,000.00. US Postal money orders are hard to counterfeit.
- ✓ **Why does the U.S. currency have value even though it is not tied to a commodity** – there is a belief that money has value and therefore is accepted
- ✓ **Opportunity cost:** next best alternative – it is what is given up when a choice is made.
- ✓ **Who is hurt the most and the least with inflation** – most hurt are lenders (banks) and people living on a fixed income. Least hurt are those who owe large amounts of money.
- ✓ **Role of the Treasury Department:** collects taxes, prints money, issues treasury bonds

Banks

- ✓ **Pay Yourself First:** automatically route money from paycheck to savings (before paying bills).
- ✓ **CD: What is it and what happens if you cash it before maturity:** it is a time deposit offered at financial institutions – penalty if cashed before maturity.
- ✓ **Institutions that give loans:** banks, credit unions, pawnshops, finance companies, payday lenders, tax preparers
- ✓ **Which institution(s) charge the highest interest rates on loans:** pawnshops, payday lenders, tax refund lenders, finance companies
- ✓ **What is a credit union and the advantage of using a credit union:** member owned co-operative financial institution – advantage is lower interest rates on loans
- ✓ **Overdraft protection (opt in regulation) and how it works:** Overdraft protection is a feature offered by banks to keep your checking account from over-drafting when you write a check or swipe your debit card but don't have enough money in your account. It is a loan that is paid back.

Banks (Continued)

- ✓ **Compound Interest:** interest added to principal – interest earned on interest
- ✓ **Time value of money:** is calculated by value of money with given amount of interest earned over a period of time; the longer the time you keep your money invested, the more interest you will earn.
- ✓ **Liquid financial products vs. products that are less liquid:** savings and checking accounts are most liquid, certificate of deposit and money market accounts are less liquid
- ✓ **Rule of 72:** how long (many years) will it take to double an investment? Divide 72 by the interest rate to be earned: 72 divided by 3% interest = 24 years (if you are given the number of years and need to determine the interest rate needed to double your money, then divide 72 by the given number of years: 72 divided by 24 years = 3% interest).
- ✓ **Reconciling a Checking account-- why and when:** to view what activity has occurred in your account. Keep current with your check register to know what your current balance is at all times. When you receive your bank statement, you reconcile your check register against the statement to be sure no errors have been made and to record any bank fees and/or interest earned in your register.
- ✓ **Repayment of student loans:** 6 month grace period (after leaving school) before you start making payments.
- ✓ **Tax anticipation loans:** A refund **anticipation loan** (RAL) is a short-term consumer loan secured by a taxpayer's expected **tax refund**

Credit

- ✓ **Credit card cash advances:** provided by credit card companies – withdraw cash with credit card – you pay a higher interest rate
- ✓ **Truth in Lending Act:** – Also called the Consumer Credit Protection Act, legislation enacted in 1968 requiring money lenders to be explicit about the true costs of credit transactions. The Truth-in-Lending Act also outlaws the use of threatened or actual violence to collect debts
- ✓ **Consequence of paying the minimum payment due on a credit card bill or paying a bill late:** impacts credit score if paid late. If you are only paying minimum payment each month you will take a much longer time to pay off balance – you will greatly increasing the total amount paid back due to APR charged per month.
- ✓ **How does the degree of risk influence the interest rate charged for credit:** if you have a low credit score, it demonstrates you are a poor credit risk, and you will pay a much higher interest rate on loans
- ✓ **Debt to Credit Ratio:** A credit-to-debt ratio is the amount of available credit you have relative to the amount of debt you carry.
- ✓ **Credit Reports:** is a number representing the creditworthiness of a person, and the likelihood that person will pay his or her debts. Lenders, such as banks and credit card companies, use credit scores to evaluate the potential risk posed by lending money to consumers.

Credit (Continued)

- ✓ **Three leading credit reporting agencies** - Equifax, TransUnion, Experian
- ✓ **Consequence of a lost or stolen credit card:** if unauthorized charges are made with your credit card before you report it lost or stolen, the maximum amount you can be liable for is \$50. If the charges are made after you report the card lost or stolen, you have no liability. If you don't report card after it is lost or stolen, you have full liability to pay back charges.
- ✓ **The length of debt repayment and impact on cost:** the longer you take to pay back a loan, the more you will pay in interest and principal overall.
- ✓ **What to do if a person thinks he/she is a victim of identity theft:** contact banks and cancel all credit card/debit cards, review bank accounts to see if there are recent charges/purchases on accounts, contact all 3 credit bureaus to report identity stolen, apply for new social security card
- ✓ **Characteristics of predatory loans:** making loans to customers who are poor credit risk (low credit scores) and making those customers pay extremely high interest rates.
- ✓ **Collateral (secured vs. unsecured loans):** collateralized/secured loans use an item (house, car, appliances, etc...) to guarantee the loan. An unsecured/uncollateralized loan is a personal loan – secured only by someone's good credit score.
- ✓ **Pawnshops:** Collateralized loans – the loan is collateralized/secured by the item (musical instruments, jewelry, etc...) you bring in order to get a loan from the pawnshop. You pay interest on the loan and a type of fee.

Insurance

- ✓ **How insurance works—Transfer of Risk**

Insurance policies transfers all or some of the financial impact of unexpected events. Insurance exists to help individuals recover from the financial consequences of these events by pooling the resources of a large group to pay for the losses of a small group.
- ✓ **Insurance deductible:** A deductible is the amount that the insured has agreed to pay before the insurer is obliged to pay anything on a covered claim. The higher the deductible the lower the monthly premium (payment) – the lower the deductible the higher the monthly premium (payment).
- ✓ **Collision coverage—when do consumers normally terminate this coverage:** Collision coverage on your car insurance policy that will repair damages to your vehicle when something collides with your vehicle. Consumers terminate/cancel the policy when the value of the car is less than the replacement pay out by insurance company.
- ✓ **Term life insurance:** Term life insurance is an insurance policy that will pay a lump-sum benefit to your family or another beneficiary of your choice, if you die while the policy is in effect. Is not a permanent life insurance policy.

Insurance (Continued)

- ✓ **Renters Insurance:** is insurance you buy to protect your furniture, belongings, etc. in case of a burglary, fire, or some natural disaster. Also covers liability/injury to others.
- ✓ **Whole life insurance:** Whole life insurance is a policy that is also a way to invest money. It is referred to as a permanent life insurance policy because, as long as you pay your premiums, the policy is yours for life, providing your loved ones with a guaranteed benefit upon your death.
- ✓ **Health insurance and co-pay: health insurance** is insurance against the risk of incurring medical expenses among individuals. By estimating the overall risk of health care and health system expenses, among a targeted group, an insurer can develop monthly premium to ensure that money is available to pay for the health care benefits specified in the insurance agreement. A **co-pay** is the amount of money you pay out-of-pocket for a covered medical service. Co-pays are typically a flat dollar amount for a doctor's office visit, prescriptions or lab tests.
- ✓ **Disability Insurance:** Disability insurance will cover your bills while you are disabled or cannot work, with an injury or illness for a certain amount of time. Doesn't replace income.
- ✓ **How to reduce the cost of auto insurance:** get good grades, no accidents, good credit, and drive a certain type of car.

Investing

- ✓ **Securities/equities:** capital gains or loss from investments; dividends paid on investments; historical performance of stocks or the advantages of owning securities (high risks comes with high returns); primary markets (underwriting) vs. secondary markets (New York Stock Exchange; NASDAQ). For example, Twitter recently had an IPO (initial public offering) where their stock was first sold to the primary market (consisting primarily of institutional investors that arrange to purchase the stock through the underwriter; it is very difficult for an individual investor to buy stock in the primary market), the stock was then made available to the secondary market through the New York Stock Exchange. The initial price to the secondary market of the Twitter stock was much higher than the initial price paid in the primary market. You can think of the primary market as the market where the stocks are "created" and the secondary market as the market where they are traded.
- ✓ **bull market (remember u in bull --- market goes UP):** bull market refers to a financial market that experiences an extended period of growth above the historical averages.
- ✓ **bear market:** A bear market refers to financial markets that are experiencing a prolonged period of contraction or loss.
- ✓ **Diversification:** is when an investor has different types of investments (stocks, bonds, mutual funds, Treasury Bills, etc..) it reduces risk of investing – not putting "all your eggs in one basket"

Investing (Continued)

- ✓ **Dividends:** Dividends are the earnings given to the people who are shareholders of the company stock.
- ✓ **Bonds—purpose; how they work; interest feature; tax free feature of municipal bonds:** a bond is a financial instrument that gives its holder/owner the right to collect interest payments from the company or organization that has borrowed money. A municipal bond is a bond that is issued by a city or some type of governmental agency. Government bodies usually issue tax-free municipal bonds to fund large capital expenses and improvements, like parks, downtown restorations, schools or airports.
- ✓ **Mutual Funds—what they are, how they work and who manages the fund:** A mutual fund is defined as a professionally managed investment vehicle that is made up of pool of funds collected from many investors and invested in stocks, bonds, money markets and securities. Managed by fund manager. Mutual fund provide an easy way for small investors to diversify the investment.
- ✓ **Investment portfolio:** A portfolio is a diversified (hopefully) set of investments held by an individual or institutional investor
- ✓ **Treasury Bills:** Treasury bills are short-term loans sold to operate the U.S. government. Amounts invested range from \$1,000 to \$5 million per investor. (Also known as T-Bills.)

Financial Planning

- ✓ **Determine Net Worth:** Total Assets minus Total Liability = Net Worth (what I own minus what I owe)
- ✓ **examples of assets** (equity in a house, investments,savings, etc..) , **liabilities** (mortgage, auto loan, student loans, credit cards, etc...) **and net worth** (total assets – total liability = net worth)
- ✓ **Retirement: How different plans/accounts work and when taxes are paid on funds**
- ✓ **Pensions:** A pension plan is a retirement plan which is sponsored by an employer.
- ✓ **401k plans:** an account that an employee uses to save for retirement. This account allows the worker to defer current income taxes on the saved money and interest earnings until he or she withdraws the money.
- ✓ **Traditional Individual Retirement Accounts (Traditional IRA)** An IRA is an individual retirement account. A traditional IRA is tax deductible, and you can contribute \$5000 a year to it. You will pay taxes on the money when you withdraw it in retirement.
- ✓ **Roth Individual Retirement Account (Roth IRA)** is a type of IRA that does not give you a tax benefit for contributing like a traditional IRA does. Instead the money in the account grows tax free and can be withdrawn at retirement without paying any taxes.
- ✓ **Inflation is the general rise of price levels:** who suffers in inflation: creditors, people living on fixed income, and people trying to save. Who benefits from inflation: people who owe significant debt.

Financial Planning (Continued)

- ✓ **Deflation:** is when the cost of consumer goods is actually declining. This may seem like a good thing, but if there is a prolonged period of deflation, companies will begin to suffer as will the overall economy. Consumers benefit from deflation.
- ✓ **Depression:** An economic depression is a period of time in which the economy has reached the lowest point possible. Production and consumption decreases drastically, and unemployment rises.
- ✓ **Taxes—graduated income taxes:** Graduated income tax is considered a progressive tax. Progressive tax is a rate that increases as the amount of taxable income or funds go up.

Regulatory Agencies:

- ✓ **The SEC:** The SEC is the Securities and Exchange Commission. It is a board with five members. They regulate the offer of and sale of securities among the public (stock shares from corporations).
- ✓ **Federal Reserve (Fed);** The **Federal Reserve System** (also known as the **Federal Reserve**, and informally as the **Fed**) is the [central banking](#) system of the United States. The fed uses monetary policies to regulate the money supply. The 3 traditional policies include:
 - 1) **Discount Rate** (the interest rate the Fed charges commercial banks for short-term overnight loans). By decreasing the Discount Rate, banks lend more, which increases the money supply. By increasing the discount rate, banks lend less, which decreases the money supply.
 - 2) **Reserve Requirement Ratio** (percentage of deposits a bank is required to have in reserves-or "on hand"). By decreasing the reserve ratio, banks lend more, which increases the money supply. By increasing the reserve ratio, banks lend less in order to meet the requirement, thus the money supply decreases.
 - 3) **Open market operations** (MOST POPULAR POLICY TODAY): This is when the Fed buys and sells [treasury bonds](#). If the Federal Reserve buys treasury bonds, it "free-ups" the bonds a bank must have on hand, thus they are able to lend out more reserves and it increases the money supply. If the Fed sell treasury bonds, they decrease the money supply.
- ✓ **FDIC (Federal Deposit Insurance Corporation):** FDIC insurance covers all deposit accounts, including checking and savings accounts, money market deposit accounts and certificates of deposit. The standard insurance amount is \$250,000 per depositor, per insured bank, for each account ownership category. (Note: FDIC does not insure accounts held in a credit union.)
- ✓ **CFPB: The Consumer Financial Protection Bureau (CFPB)** is an independent federal agency that holds primary responsibility for regulating consumer protection with regard to financial products and services in the United States.