Intro to BUSINESS

> Finance
> Marketing
> Operations
> Management

Dlabay

Burrow

Eggland
Explore the Real World of Business Ed

**Entrepreneurship: Ideas in Action 3E**
Take students step-by-step through the entire process of owning and managing a business. Focus their attention on the real skills required of entrepreneurs – start with meeting a market need and work through planning, financing, incorporating technology, hiring, managing, and avoiding legal problems. Students learn by doing using the innovative, activity-based *Build a Business Plan* in every chapter. *Winning Edge* gets students prepared for BPA, DECA, and FBLA competition.

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Start students on the path to dollars and sense. Use NAIC’s respected Stock Selection Guide process to teach smart saving, investing, and planning. Students learn how to analyze the value of stocks and mutual funds. Company Profiles introduce every chapter and the lesson-plan approach makes material easy to comprehend.

**Instructor Support and Other Materials Available**

Join us on the Internet at www.swlearning.com
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“Using credit to buy that home theater system resulted in a much higher cost.”
“The interviewer asked me some questions I didn’t expect.”
“Higher taxes in our community may be necessary to maintain quality police and fire protection.

These comments represent your economic roles as a consumer, worker, and citizen. Each day, you encounter many situations that require knowledge and experience to plan and make decisions. That’s what we offer you.

Intro to Business will introduce you to the exciting and challenging world of business. Through the information and activities in the book you will increase your preparation to be a knowledgeable consumer, well-prepared employee, and effective citizen in our economy. This course will serve as a background for other business courses you will take in high school and in college, prepare you for future employment or business ownership, and make you a better informed citizen for an expanding international economy.

This book, along with the supplementary instructional resources, will make it possible for you to learn about many topics you will encounter throughout your life as a consumer, worker, and citizen.

GETTING STARTED

The text is carefully designed and written to present an interesting discussion of business and to help you learn important business principles. It is organized into 20 chapters with each chapter divided into several lessons. Lessons are organized around short Goals that identify the important ideas you will learn. You are also given a list of Key Terms at the beginning of every lesson that introduces the vocabulary of business. You will find a variety of figures, illustrations and photographs that offer additional insights and interesting ideas.

BUSINESS OUTSIDE THE BOX

These actual stories start each unit and will help you think about business in a different way. The company situations represent some unusual and innovative business enterprises. These articles are just the start of many real-world examples you will encounter throughout the book.

PLANNING A CAREER IN ...

What would you like to do in the future? Each chapter starts with information about a career field. These features will help you think about the many career opportunities from which you might choose.

FOCUS ON REAL LIFE

Daily situations provide the basis for learning. These situations at the start of each lesson can get you thinking about the topic to be covered. Put yourself in the situation and decide what you might do.

WELCOME TO STUDENTS
HELPING YOU LEARN

Many features are included especially to assist you in your learning by providing enhancements to your textbook.

FYI
Did you know that...? These short items provide solid information that can make a difference in your life. Provided are information about effective business management, wise consumer decisions, and career planning suggestions.

NET BOOKMARK
No greater research source is available to enhance your learning than the Internet. These features refer you to www.businessxtra.swlearning.com to gain additional information on various business topics.

WORK AS A GROUP
If you are alive, you will work on a team at some time. These exercises will allow you to experience dynamics that enhance the learning process. You will also learn about the benefits and concerns of shared decision making.

THINK CRITICALLY THROUGH VISUALS
“A picture is worth a thousand words.” A picture is also the basis for expanded knowledge. Throughout the chapter, you will view various photos. Then, a question will challenge you to apply your learning to these visual situations.

ALSO OF INTEREST TO YOU

Many special features have been developed and placed within the chapters and lessons to encourage you to think about business in new ways and to study innovative examples of business practices.

A QUESTION OF ETHICS
Each day, decisions are made that may not seem fair for some in our society. You will consider many ethical issues in your life. This feature can help you better prepare for those situations.

BUSINESS IMPROVING SOCIETY
While businesses must earn a profit to survive, most companies also have other goals. These essays provide examples of organizations that are attempting to enhance economic development and improve the quality of life in the United States and around the world.

DOING BUSINESS IN...
Every organization is affected by international business activities. A basic knowledge of doing business in other countries is vital for living and working in the global economy.

E-COMMERCE IN ACTION
Today, doing business around the world can be as easy as doing business around the block. E-commerce makes use of the Internet and other technology to buy, sell, promote, and communicate information about goods and services.
TECHNOLOGY TOPICS
What types of companies do not use computers in some way? There are very few. Your computer skills and technology knowledge are necessary for every work situation as well as for many consumer activities.

SHARPM ON YOUR LIFE SKILLS
Certain skills are vital in every school and work setting. For example, researching, working in teams, and making effective presentations are abilities that will serve you today and in the future.

MEASURING YOUR PROGRESS
Intro to Business provides you with various kinds of assessment. After each main topic in the lesson, a **Checkpoint** is provided that asks you a questions about the topic. At the end of each lesson there is a **Lesson Assessment** that provides exercises to help you master the concepts in the lesson. At the end of each chapter is an extensive **Chapter Assessment** that provides a number of ways for you to test and apply what you have learned in the chapter’s lessons.

CHECKPOINT
After every section of reading, you will encounter a review question. These will help you to know if you have learned the main idea for this material.

LESSON ASSESSMENT
At the end of each lesson, you will have a few **Key Concept** questions to help you test your knowledge of the material. In addition, **Make Academic Connections** are exercises that will enhance your learning by showing you the relationship of business to other courses in your school.

CHAPTER ASSESSMENT
When you arrive at the end of a chapter, a variety of exercises and activities will give you the opportunity to check your progress. Study questions, vocabulary exercises, decision-making cases, and field research projects are offered to measure and expand your learning. The chapter assessment begins with **Business Notes** that summarize each lesson. The next section is **Communicate Business Concepts** that ask you to think about ideas from the chapter as you solve a problem or gather information. In **Develop Your Business Language** you match the key terms from the chapter with the correct definitions. A short case problem is presented in **Decision-Making Strategies** with challenging questions to demonstrate your problem-solving and critical thinking skills. **Make Academic Connections** are activities that show the relationship of business to other courses in your school’s curriculum. **Linking School and Home** offer an opportunity to see how what you are learning in Intro to Business can be applied in your neighborhood and your community. In **Portfolio Activity** you select an activity completed in the chapter to put into a portfolio.
THERE'S STILL MORE

WINNING EDGE
Your ability to work under pressure is a vital skill for business. At the end of each chapter, these activities are based on competitive events for the FBLA (www.fbla-pbl.org) and the BPA (www.bpa.org).

GLOBAL BUSINESS PROJECT
How might you do business in Asia or Africa? This end-of-unit project provides an opportunity to plan, organize, and implement global business activities.

LIFE-SPAN PLAN PROJECT
Several decision areas must be considered throughout your life. The Life Span activities will guide you when making choices related to your education, career, family, personal finances, and community involvement.

Now it's time get started on your educational journey using Intro to Business. We wish you a life of great success and personal satisfaction.

Les Dlabay
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Les R. Dlabay, Ed.D., is a Professor of Business in the Department of Economics and Business at Lake Forest College in Illinois. The courses he teaches include Marketing Research, Financial Accounting, Cultural Perspectives of International Business, Global Marketing, Latin American Global Business, and Asia Business Culture and Trade Relations. Dr. Dlabay has presented over 250 teacher workshops and seminars, and has taught more than 30 different courses in high school, community college, university, teacher preparation, and adult education programs. He has also served as International Business editor for Business Education Forum, published by the National Business Education Association, and helped develop the National Curriculum Standards for International Business. Dr. Dlabay’s “hobbies” include a cereal package collection (from over 100 countries) and paper currency from 200 countries, which are used to teach about economic, cultural, and political aspects of foreign business environments.

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Steven A. Eggland, Ph.D., is the Executive Director of the Accrediting Council for Independent Colleges and Schools (ACICS) in Washington, DC. ACICS is the largest accrediter in the world of business colleges and schools, accrediting over 600 institutions of higher education. Dr. Eggland is also Emeritus Professor of Vocational and Adult Education in Teachers College at the University of Nebraska. He has taught a wide variety of business courses and has a special interest in marketing education.
The fact that you are reading a copy of *Intro to Business* shows a number of things about you. It probably means you have chosen to sign up for a course that will teach you about businesses and how they operate in the United States. Studying the role businesses play in the nation’s society, politics, or economy may interest you. Questions such as, “What causes some businesses to prosper while others fail?” or “What types of people become successful business leaders?” are ones that you may have asked yourself. You may have wondered whether a career in business is right for you. Becoming a success in business, either as an employee or owner, may already be a basic goal you have set for yourself. Whether or not this is true of you, this book will provide you with knowledge and skills you may use to make better decisions throughout your life.

### YOUR PERSONAL GOALS

Goals are the things that people want most to achieve in their lives. They are the things that hold the greatest value to them. Most people have set a wide range of goals for themselves. Some are short-term goals that they hope to achieve within a year. Others are long-term goals that will require many years to attain. Individuals’ goals are likely to involve family, living conditions, education, careers, community, and many other aspects of their lives. The goals you set for yourself are based on your personal values, your hopes, and your dreams. Although many people share common goals, most people also have unique goals that set them apart from others.

There is no way to judge most goals as right or wrong, or better or worse. Your most important goal may be to study law and become a judge while your best friend might want to own a farm and grow tomatoes. Your brother may want to start a family at a young age while you prefer to put off marriage and family responsibilities until well into the future. As long as a person’s goals are based on what she or he really wants from life, there is no reason for them to be the same as other people’s goals.

Almost every important goal you could set for yourself involves topics you will learn about while studying this textbook. Suppose, for example, your most important personal goal is to have a happy and secure family life. You
might think that this goal has little to do with what you will learn about businesses this year. But, if what you learn about businesses helps you make a better career choice, then you may be able to earn a greater income and be more satisfied with your life. This will also allow you to provide a better standard of living for a family. The same is true for almost any other personal goal you might set.

**A LIFE-SPAN PLAN**

As you grow older you should expect the things you want most in your life to change. Today you might believe that owning a nice car is your most important goal. In ten years you may be more concerned with having a rewarding career, buying a home, or saving for your children’s education. Even later you will want to have a satisfying retirement. Important events in your life, such as preparing for a career, raising a family or enjoying retirement are parts of your *life cycle*.

Your *life span* is the time from your birth to your death. It includes the events that make up your life cycle. When you are young, you will set long-term goals that you want to achieve over a period of years during your life span. You may think of your life span as a straight line that contains the events of your life cycle.

The *life-span timeline* above can help you understand the relationship between a life span and events in a person’s life cycle. It shows a life span as a straight line along the top of the figure. Events in the life cycle appear beneath the time in a person’s life when they might happen. If you construct a figure like this for yourself, it is likely to have different events taking place at different times because your life will not be exactly the same as anyone else’s.
Life-span goals are long-term goals that you want most to reach during your life. They shape many of the most important decisions you will make. Examples of life-span goals include earning a college degree, owning a business, raising a family, or achieving financial security. For most people, life-span goals don’t just happen. Successful people create long-term plans for how they can achieve their life-span goals. These plans are called life-span plans. You will be asked to choose life-span goals that you will use to create a life-span plan of your own. This text is specially designed to help you complete this assignment. You will see Life-Span Plan icons, like the one at the right, placed near parts of the text that can be helpful in setting your life-span goals and preparing a life-span plan for yourself. For each icon, an assignment or activity is listed at the end of this introduction by page number. By completing these assignments and saving them to use later, you may prepare to construct your life-span plan.

A LIFE-SPAN PLAN FOR KELLY
To help you prepare your own life-span plan, consider the example of Kelly.

Kelly is fifteen years old and a high school sophomore. Roy, a senior at her school, is her steady boyfriend. They have talked about their future and getting married someday, but have agreed to wait until they both finish their educations, get jobs and save some money.

Kelly’s favorite subject in school is art. She has signed up for every art class that she could fit into her schedule. Although she loves art, she has learned that she is not an exceptionally talented artist herself. Experience has convinced Kelly that she will never be good enough to earn a living creating works of art. But, she still wants to earn her living in the art world. Kelly has decided that her best alternative is to work in, and perhaps eventually own, a studio that sells pieces of fine art. One of the reasons she chose to take a class titled Intro to Business was to learn more about businesses and decide whether this might be a good choice for her future. Over the months of her class, Kelly completed assignments that helped her learn many things about
herself. She saved these assignments in a file and used them to help her complete her life-span plan by taking these steps.

**FIRST THINGS FIRST**

To begin her life-span plan, Kelly identified six central life-span goals that she most wants to achieve over the next 50 years. These goals fit in well with her values, interests, and personality. They are to:

1. Gain training and education needed to work in a successful retail art studio.
2. Own and operate a successful retail art studio.
3. Get married, have several children, and own a house in a nice neighborhood.
4. Become financially secure.
5. Be active in my community, church, and local government.
6. Be able to retire and take up other interests by the age of 65.

Kelly realizes that achieving these life-span goals will involve careful planning and many trade-offs. Almost all life-span goals people set require money. To pay for her education, a business of her own, a home, and a secure retirement she will need to save and invest part of the income she receives during her working life. At times, she may need to borrow funds from others. She will need to construct and follow a budget that allows her to do this. At the present, Kelly may decide not to spend as much of her income on new clothes so she can save more to pay for college tuition later. Kelly will also need to identify related short-term goals that can help her achieve her more-important life-span goals in the future.

**RELATED GOALS**

Kelly’s central life-span goals are related to each other. Saving and investing to achieve financial security, for example, will help her pay for training and later to start a business. If her business is successful, she will be able to afford the house she wants to own. Financial security will also allow Kelly to enjoy a few luxuries. About 160 years ago Kelly’s ancestors immigrated to the United States from Ireland. Some day Kelly would like to visit Ireland and see where they lived. If her business is a success, she will be able to take this trip.

Kelly wants to achieve many short- and long-term goals that are not central goals in her life. These include buying cars, furniture, and owning a sailboat. Although these goals are important, they aren’t among the things Kelly cares most about in life, and so they are not listed in her life-span plan. In preparing her life-span plan, Kelly listed and evaluated her goals to decide what was most important to her and what was only something that would be nice to have.
Kelly organized her life-span goals in a table as shown below. Across the top she placed six categories to represent her six central life-span goals. On the left side she placed periods of time. These started with the next two years at the top and went fifty years into the future at the bottom. She then placed her goals according to when she would like to achieve them and how they contribute to her central life-span goals. In this way, she created a life-span plan that she believes will help her accomplish what she wants most in life.

Kelly feels a sense of satisfaction with her work. She knows that she will almost surely revise her plan in the future, but she has a foundation on which to build. She can use her plan to help make decisions now. When she makes her class schedule for next year she will sign up for accounting, business management, and more art classes. She knows what type of work to look for and how to spend and save her income. Because she has definite goals, she is better able to choose not to spend money for things she doesn’t really need.

**KELLY’S LIFE-SPAN PLAN**

<table>
<thead>
<tr>
<th>Time</th>
<th>Education</th>
<th>Career</th>
<th>Family</th>
<th>Financial</th>
<th>Community</th>
<th>Retirement</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Next 2 years</strong></td>
<td>Complete high school. Apply to art school.</td>
<td>Find a part-time job in an art studio.</td>
<td>Help parents with younger children.</td>
<td>Save $2,500 each year to help pay tuition</td>
<td>Be an active member of my church.</td>
<td>Nothing yet</td>
</tr>
<tr>
<td><strong>5 years from now</strong></td>
<td>Graduate from art school.</td>
<td>Work full-time in an art studio or art museum.</td>
<td>Find a nice apartment in a good location.</td>
<td>Save and invest income to buy a home.</td>
<td>Teach art classes to children at my church.</td>
<td>Buy life insurance.</td>
</tr>
<tr>
<td><strong>10 years from now</strong></td>
<td>Take classes in small business management.</td>
<td>Accept a managerial position at an art studio.</td>
<td>Get married and buy a small home. Have one child.</td>
<td>Save and invest to buy an art studio.</td>
<td>Teach art classes at a local community college.</td>
<td>Open a retirement account.</td>
</tr>
<tr>
<td><strong>20 years from now</strong></td>
<td>Travel to Ireland to see local artist’s work.</td>
<td>Buy or start an art studio.</td>
<td>Buy a larger house. Have another child.</td>
<td>Start a fund for children’s education.</td>
<td>Continue teaching art classes.</td>
<td>Continue saving in retirement account.</td>
</tr>
<tr>
<td><strong>35 years from now</strong></td>
<td>Teach art store management classes at a community college.</td>
<td>Build a successful business and look for a person to help run it.</td>
<td>See children graduate from college. Buy a vacation home at the beach.</td>
<td>Increase saving and investments now that children have moved out.</td>
<td>Run for town council or participate in government in some other way.</td>
<td>Investigate volunteer work I might enjoy.</td>
</tr>
<tr>
<td><strong>50 years from now</strong></td>
<td>Take classes in Irish cooking and history.</td>
<td>Sell business. Take part-time job in art store.</td>
<td>Buy a retirement home in a place where it’s warm.</td>
<td>Manage investments carefully.</td>
<td>Volunteer to advise people who have small businesses.</td>
<td>Take at least one long trip each year and visit grandchildren.</td>
</tr>
</tbody>
</table>
Kelly’s life-span plan is right for her. It fits her values, personality and family situation. Her plan, however, would not be right for most students, including you. You aren’t Kelly. You have other values, abilities, and interests. Her personality is not your personality. Her family is not your family. You need to make your own life-span plan.

YOUR OWN LIFE-SPAN PLAN

Near the end of this class you will be asked to prepare a life-span plan for yourself. To do this, you should reflect on what you’ve learned throughout this course. You will study numerous topics and finish many activities that you can use to help you complete this assignment. You will also want to consider things about yourself that were not directly covered in this course. The type and size of family you want to have is important, but will not be discussed in this course. The same is true of where you want to live and the role you wish to play in your community. Preparing your life-span plan will require you to consider all of your values and goals, not just those that are related to businesses and your career choice.

After you accumulate as many useful resources as you can, use these materials to help you write a list of your goals. Base them on what you want from life for yourself, your family, and your community. Sort them according to whether they are short- or long-term goals, and then classify them into overall life-span goals. Place your goals on a grid similar to Kelly’s to construct your life-span plan.

When you have finished your life-span plan, it would be helpful to ask an experienced person to review your plan with you. A teacher, guidance counselor, or other adult you respect would be a good choice. Discuss your choices and the feasibility of your plan. This person can offer advice and encouragement for achieving your goals.

Making a life-span plan is an important first step. But, it is only a first step. Putting your life-span plan into action can make the difference between just thinking about your future and actually achieving the life-span goals that are most important to you. If you fail to act on your life-span plan, it will only be a piece of paper.

Following is a listing of the locations of Life-Span Plan icons and activities you may complete to help you create your own life-span plan.
### LIFE-SPAN PLAN ACTIVITIES

<table>
<thead>
<tr>
<th>Page</th>
<th>Activity</th>
</tr>
</thead>
<tbody>
<tr>
<td>14</td>
<td>Write an essay that describes how you could use the decision-making process to choose classes for next year that will help you achieve your life-span goals. In what other ways will the decision-making process benefit you in the future?</td>
</tr>
<tr>
<td>44</td>
<td>Calculate your savings rate (percent of your current income that you save). Do you believe you save enough of your income? Explain how saving is related to people achieving their life-span goals. Set a short-term saving goal that you could achieve now to help you eventually reach future life-span goals.</td>
</tr>
<tr>
<td>55</td>
<td>Identify your special aptitudes or abilities that you believe could help you achieve your life-span goals. Explain how these aptitudes or abilities are similar to nations that have an absolute or comparative advantage in production and trade.</td>
</tr>
<tr>
<td>76</td>
<td>Explain how environmental issues might affect the life-span goals you set for yourself.</td>
</tr>
<tr>
<td>79</td>
<td>Do you have a personal code of ethics? Explain how your ethics might affect the life-span goals you set for yourself.</td>
</tr>
<tr>
<td>91</td>
<td>Explain how government taxing and spending could affect the life-span goals you set for yourself as well as your ability to achieve these goals.</td>
</tr>
<tr>
<td>108</td>
<td>Is owning a business a life-span goal you have set for yourself? Describe steps you would need to take to achieve this life-span goal.</td>
</tr>
<tr>
<td>128</td>
<td>What personal characteristics do you have that could help you become a successful entrepreneur? Describe how these characteristics may affect the life-span goals you set for your future.</td>
</tr>
<tr>
<td>138</td>
<td>What hobbies, interest, and experiences do you have that could help you achieve your life-span goals? Describe steps you could take now that would expand your experiences and opportunities for achieving your life-span goals.</td>
</tr>
<tr>
<td>157</td>
<td>List and evaluate your own leadership abilities. Explain how your leadership skills may affect the life-span goals you set for yourself.</td>
</tr>
<tr>
<td>176</td>
<td>Why might it not make sense to set a life-span goal of becoming a telephone switchboard operator? Explain why it is necessary to understand changes that are taking place in the workplace when you set your life-span goals.</td>
</tr>
<tr>
<td>189</td>
<td>How important do you believe family leave policies, flextime, or job sharing would be to you in choosing a career? Explain why work-life relationships are important when people set their life-span goals.</td>
</tr>
<tr>
<td>203</td>
<td>Describe a career planning process you might complete that would help you achieve your life-span goals.</td>
</tr>
<tr>
<td>209</td>
<td>Complete a personal assessment of yourself. It should include listings of your interests, values, talents and abilities. Explain how these lists may help you create your own life-span plan.</td>
</tr>
<tr>
<td>217</td>
<td>Complete a resume for yourself similar to the one in Figure 9-4 in your text. Identify steps you could take over the next year that would improve your resume and increase your chances of being hired. Explain how these short-term steps might help you achieve your life-span goals.</td>
</tr>
<tr>
<td>240</td>
<td>How easily are you able to communicate with other people? Explain how an ability to communicate with other people can affect the life-span goals you set and your ability to achieve them.</td>
</tr>
<tr>
<td>266</td>
<td>Do you believe that you are computer literate (able to understand and use computers efficiently)? Are you comfortable using computers? Describe how the computerization of our society and economy may affect your ability to achieve your life-span goals.</td>
</tr>
<tr>
<td>278</td>
<td>Explain whether you believe the growth of e-commerce will affect the life-span goals you set or your ability to achieve them.</td>
</tr>
<tr>
<td>302</td>
<td>Describe ways in which the financial planning functions of a business are similar to the financial planning that must be done by people to achieve their life-span goals. Evaluate the status of your own financial planning. Will you be financially able to achieve your life-span goals?</td>
</tr>
<tr>
<td>310</td>
<td>Explain why making good financial decisions is no less important to individuals than it is to businesses. How do you make your financial decisions? Will this process help you achieve your life-span goals?</td>
</tr>
<tr>
<td>324</td>
<td>Identify and describe similarities between production planning and life-span planning. Describe steps you could take to produce success in achieving your life-span goals.</td>
</tr>
<tr>
<td>351</td>
<td>Describe several examples of losses you might suffer that would prevent you from achieving your life-span goals. Explain why buying adequate insurance is an important part of every person’s life-span plan.</td>
</tr>
<tr>
<td>377</td>
<td>Explain why an ability to make wise buying decisions is important for achieving your life-span goals. Do you believe buying skills contribute to your ability to reach your life-span goals? What could you do to improve your buying skills?</td>
</tr>
<tr>
<td>404</td>
<td>Explain why it is important for people to create and use a budget process when they are young even if they have only small amounts of income and make few expenditures. Do you have a budget process that you use? How can a budget process help you achieve your life-span goals?</td>
</tr>
<tr>
<td>410</td>
<td>Describe the role of financial planning in the creation of a person’s life-span plan. Do you have a financial plan? Explain why people who fail to create and follow a financial plan often fail to achieve their life-span goals.</td>
</tr>
<tr>
<td>424</td>
<td>Do you believe that people need a safe and reliable banking system to achieve their life-span goals? Describe how you expect to use banks and other financial institutions to reach the goals you set in your life-span plan.</td>
</tr>
<tr>
<td>451</td>
<td>What life-span goals might you set that would require you to use credit? Describe steps you can take in the next few years to create a credit history that will help you borrow funds in the future.</td>
</tr>
<tr>
<td>460</td>
<td>Describe why the excessive use of credit can prevent people from achieving their life-span goals. How would you decide when, or when not, to borrow funds?</td>
</tr>
<tr>
<td>481</td>
<td>Explain why people who have created life-span plans are often more successful in saving than those who have not. How might your life-span plan help you save?</td>
</tr>
<tr>
<td>489</td>
<td>Describe how a life-span plan can influence the types of investment choices a person makes. How much risk are you willing to take? How may your willingness to accept risk affect the life-span goals you set for yourself?</td>
</tr>
<tr>
<td>498</td>
<td>Will home ownership be one of your life-span goals? Explain how buying a home is different from other types of investments you may make.</td>
</tr>
<tr>
<td>517</td>
<td>Why is the purchase of property and liability insurance important to all life-span plans? What amounts and types of insurance should you plan to buy in the next few years?</td>
</tr>
<tr>
<td>524</td>
<td>Most life-span plans are created to serve a family. Explain why these plans should include life insurance for all adult members. When do you expect to purchase life insurance? How much and what type will you buy?</td>
</tr>
</tbody>
</table>
Unit 1

Business in the Global Economic Environment

1. Economic Decisions and Systems
2. Economic Activity
3. Business in the Global Economy
4. Social Responsibility of Business and Government
Drinks for Developing Countries

Vitango, an orange-flavored drink, not only provides refreshment but also could save lives. The Coca-Cola Company offers the product in Botswana and other countries. This juice drink contains 12 vitamins and minerals to help reduce anemia, blindness, and other health problems among children in developing economies. Another major company, Procter & Gamble, was already offering a similar drink.

The drink originally sold for about 20 cents for an 8-ounce liquid serving. Even at that price, few could afford it in these very poor nations. A revised formula of the drink reduced costs—and the price—making Vitango more affordable to those who need it most. This effort is a part of Coca-Cola’s strategy to increase sales of its major products. In addition, the company is contributing to the health and well-being of people living in very difficult situations.

Think Critically
What are some products and services that companies could offer to improve quality of life around the world?

Competing with the Big Guys

How does a small local supplier of lighting fixtures compete with Home Depot, Lowe’s, and Menards? In the case of Bronson Electric, they took a close look at the needs of their customers.

First, since Bronson mainly served small contractors, many of them needed a place to park their trucks. Family members and neighbors were not pleased to have the vehicles in home driveways. Next, most small contractors did not have time to maintain accounting records and send bills to customers. Finally, ordering items for the next day’s work could be time consuming and was sometimes overlooked.

These three concerns resulted in Bronson Electric building a series of small garages near its warehouse for use by contractors. These facilities provided a place for contractors to park their trucks. A small office space in each garage gave contractors an area for preparing invoices. A software system allowed the contractor to key in the needs for the next day’s work. Overnight, Bronson employees loaded the lighting fixtures on the trucks of the contractors. These additional services helped Bronson serve the needs of customers in ways large companies could not address.

Think Critically
Create a list of ideas that might be used by small businesses in your community to help them better compete against larger companies.
Chapter 1

Economic Decisions and Systems

1-1 Satisfying Needs and Wants
1-2 Economic Choices
1-3 Economic Systems
1-4 Supply and Demand
Planning a Career in...

Corporate Economics

Economists play an important role in the business world. They are often asked to be fortunetellers. They try to predict what economic changes are coming. This is a very important task, as businesses and government officials use these predictions to make decisions that affect the economic future. Most economists work in government positions, for businesses and business associations, or as teachers and professors in colleges and universities.

Economists working for corporations forecast the size of markets, changes in consumer demand, and changes in sales and costs. They analyze competitors’ growth and market share and advise their company on how to plan. Today economists pay attention to the international economy and the economic conditions in countries where the company currently operates or plans to expand.

Employment Outlook

- More than half of all economists work for corporations or industry associations that provide research and information to businesses.
- Opportunities for corporate economists should be good in the future. The need for economists results from increased competition and the importance of the global economy. Businesses increasingly rely on statistical analysis to support decisions.
- Economists need at least a master’s degree and many obtain a PhD as they move into senior-level positions.
- Specialized opportunities are available in banking, finance, insurance, and the securities industry.

Job Titles

- Senior Economist
- Quantitative Analyst
- Forecaster
- Research Assistant

Needed Skills

- Mathematics, statistics, econometrics, research design, and computer science
- Attention to detail to ensure accuracy of data analysis
- Work independently and for long hours gathering and analyzing information
- Present findings, both orally and in writing, in a clear, concise manner

What’s it like to work in...

Corporate Economics

Pierre Latrobe is dressed and on his way to the office at 4 a.m. each morning. As an Associate Analyst, he helps prepare the morning briefing. He is responsible for tracking changes in the European economy. Each morning at 9 a.m., the Senior Economist participates in a videoconference connecting eight international offices. She uses the information prepared by her team to review daily changes in financial markets, preview trends in interest rates and costs of commodities, and identify any important government actions. A summary report is e-mailed to the executives and team members are available after the conference to further interpret the information.

On the commuter train, Pierre uses his PDA to get the latest information from the major stock markets. Then he checks the international news services for important stories that might affect the European economy. He updates forecast charts and enters notes.

What about you? What do you like and dislike about Pierre Latrobe’s work schedule and activities? What do you think happens in the daily team meetings as they prepare the morning briefing?
NEEDS AND WANTS

Hardly a day goes by that you don’t see a product or service that you would like to have. You see them in the shopping mall, the grocery store, or while surfing the Web. Advertisements on television, radio, or the Internet attempt to convince you that you need whatever is new. How do you decide what to buy or even if you need to buy at all?

Needs Are Essential

You want many things, but do you really need them? Determining what is a need and what is a want is an important part of making good decisions.

Things that are required in order to live are known as needs. Everyone needs food, water, clean air, clothing, and shelter. Other needs in today’s economy are a good education, employment, and safety. Most people need transportation to get to and from school and work. People who have health problems need medical care and medicines.
Wants Add to the Quality of Life

Things that add comfort and pleasure to your life are **wants**. You may believe you can’t live without the latest fashion, CD, or movie, but you can and many people do. A small apartment meets the need for shelter, but many people want a large house or a vacation home at the beach. It is possible to use public transportation to get around in the city, but driving a new car with luxury options adds convenience and an image of success.

It is not always easy to determine products and services that are needs and those that are wants. The country in which you live, the economic status and lifestyle of your family, and the work you do help determine whether something is really necessary or not. Most products and services you purchase do more than meet your needs. They make your life easier and more comfortable.

Needs and Wants Are Unlimited

Your needs and wants never end. You are limited only by your imagination and by what businesses make available for sale. A new style convinces you your current jacket is no longer adequate. One purchase leads to another. You purchase the latest model video game player and now you need a new set of game cartridges. A new pair of shoes may require a matching purse.

Your wants can go on and on. They change from day to day. Something you thought you couldn’t live without two days ago now doesn’t seem as important and is replaced by a new want. Everyone has unlimited wants. Those wants are not the same for each person.

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**Check Point**

What is the difference between a need and a want?

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Work as a Group

Do you believe your needs are very similar to or quite different from those that your parents had when they were your age? As a group, prepare a list of five needs that you agree would be similar to those of your parents when they were young and a list of five needs that you agree would likely be different. Justify why those listed are needs and not wants.

---

Goods and Services

You satisfy your needs and wants by purchasing and consuming goods and services. **Goods** are things that you can see and touch. They are the products you can purchase to meet your wants and needs. **Services** are activities that are consumed at the same time they are produced. Services are intangible, meaning they have no physical characteristics. You use services as well as goods to satisfy your wants and needs, but they must be provided to you at the time you want to consume them.

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Does the service industry supply more needs or more wants?
CHAPTER 1  Economic Decisions and Systems

Goods and Services for Businesses and Consumers
Goods and services are purchased by businesses as well as by consumers. Some goods and services are unique for business or consumer use. Others are similar but meet different needs.

A business needs steel, plastic, gasoline, and computers in order to operate. It must have a constant supply of electricity, security for buildings and equipment, and accountants who maintain records and file tax returns.

Consumers buy watches, televisions, automobiles, cell phones, and books. They eat at restaurants, go on vacations, and take their car to the auto dealer for service and repairs. Businesses supply the goods and services that meet business and consumer needs and wants.

The U.S. Economy
The United States is the largest producer of goods and services in the world. Americans consume more than any other country. In fact, America has twice as many shopping malls as it does high schools! America’s lead in consuming goods and services began around the turn of the 20th century. In 1950, American families usually owned only one car. In 2000, nearly one in five families owned three or more cars. Because of this consumption, Americans produce more pounds of garbage per person per year than any other country.

Americans often incur debt through obtaining loans and using credit cards. Not all consumption is excessive and not all Americans purchase beyond their means to pay. In fact, many demonstrate financial responsibility through saving and investing their money rather than spending. This enables them to accumulate enough money to finance a car, pay for additional education, or even save for retirement.

Some believe the high level of U.S. consumer demand stems from the sheer quantity of goods and services available and the amount of money businesses spend to advertise their offerings. Spending opportunities occur daily and require careful decisions to make sure important needs and wants are satisfied in the future as well as today.

ECONOMIC RESOURCES
How do you get the goods and services you need and want? Few are free. Individuals no longer create most of the products and services they consume as they did many years ago. Economic resources are needed. Economic resources are the means through which goods and services are produced. Economic resources are called factors of production. The three kinds of economic resources are natural resources, human resources, and capital resources. Businesses and individuals use resources to produce goods and services.
Natural Resources
Raw materials supplied by nature are natural resources. The earth contains oil, minerals, and the nutrients needed to grow crops and timber and to feed animals. Rivers, lakes, and oceans are the sources of both food and water. The air you breathe comes from the atmosphere that surrounds you. All products you consume begin with one or more natural resources.

Consider something as simple as a can of chicken noodle soup. What natural resources were used in its production? The chickens, vegetables, and spices are the result of crops and livestock grown on rich farmland. The water is extracted from wells that were filled by rain. Aluminum was extracted from the ground and used to produce the container.

The earth contains a variety of minerals, plants, fish, and animals. The supply of many natural resources is limited. Increased consumption as well as damage to the environment threatens the natural resources of many regions of the world. Conservation practices as well as the production of more efficient products help to preserve resources.

Human Resources
People producing goods and services are known as human resources. In the example of the chicken noodle soup, many people are needed to complete the work required to produce that product. Farmers raise the livestock and crops. Factory workers and managers use equipment designed by engineers and manufactured by other businesses to process the food. Truck drivers, salespeople, advertisers, and grocery store employees are also involved in producing the product and making it available to consumers for purchase.

One type of human resource is an entrepreneur. An entrepreneur is the risk taker who uses resources in an entirely new way to create a new product or service. Without the creative ideas of entrepreneurs and their belief that they can develop a successful business, there would be fewer choices of goods and services and fewer employment opportunities.

FYI
Even water, one of the most common substances on the planet, is a scarce natural resource, especially in the western United States. Disputes among southwestern states over water rights and access to the major riverways result in frequent political debate and court actions. Water will likely become a more important natural resource in the future.
Capital Resources

People must have access to tools and equipment in order to convert natural resources into products. The products and money used in the production of goods and services are capital resources. Capital resources include buildings, equipment, and supplies. They also include the money needed to build a factory, buy a truck, pay employees, or purchase services needed to manufacture and distribute goods and services.

Some people invest money in businesses so the business will have the capital needed to operate. Those people expect they will make money when the business is successful. Other people receive income by selling their knowledge and skills to businesses in the form of labor. Those with special skills or knowledge of important business processes often command higher incomes than those with knowledge and skills that are more common.

Technology Topics

Mobile Video Gaming

People have always participated in some type of entertainment. Most of the entertainment products and services you purchase and use satisfy your wants. Computer technology has introduced an exciting form of entertainment—video games. To satisfy the ever-increasing desire to play video games, companies are now producing portable versions of their products for gamers-on-the-go.

Numerous mobile game platforms compete for customer attention and sales. Nintendo’s Game Boy Advanced is the current king of these mobile entertainment devices and was revolutionary with its introduction of color to the handheld platforms. Smaller and faster video processors promise to advance the gaming industry even further. Sony is creating a mobile technology platform called the PSP, which will combine gaming, DVDs, and music in one convenient portable device. Nintendo is also generating a new platform, named the Dual Screen. In addition, the currently existing N-Gage device, from Nokia, is continually gaining support among certain segments of the gaming population. Wireless technology allows gamers to compete with each other via the Internet no matter where they are located.

The demand for mobile gaming is so strong that other mobile devices are increasingly being equipped with gaming technology. For instance, graphing calculators have a large number of downloadable games available. Companies are even developing advanced games that can be played on cell phones!

Think Critically

1. What is positive about this trend toward mobile video gaming? What could be its disadvantages?
2. What other sorts of products besides video games exist to entertain people while they are on the go?
Resources Are Limited

All economic resources have a limited supply. Most resources can be used to produce several different products and services. If resources are used to produce one type of product, they will not be available for the production of something else.

Individuals, businesses, and even countries compete for access to and ownership of economic resources. Those resources that are in very high demand or that have a limited supply will command high prices. Because there is a limited amount of natural resources, there will also be a limit to the amount of goods and services that can be produced.

CHECKPOINT

What are the three types of economic resources? Give an example of each type of resource.

CHECKPOINT

How can a country plan for future limits on its natural resources?

Assessment

Key Concepts

Determine the best answer.

1. True or False. It is not always easy to determine the products and services that are needs and those that are wants.
2. Which of the following would an economist most likely classify as a need?
   a. gasoline
   b. a high school diploma
   c. a television
   d. a part-time job to earn extra money
3. An example of a natural resource is
   a. sunlight
   b. a computer programmer
   c. a fishing net
   d. money

Make Academic Connections

4. Economics List the three types of economic resources. Choose a product and describe how each economic resource is needed and used in its production. (Hint: refer to the chicken soup example in the lesson.)
5. Communication Locate an article from a business publication or newspaper that illustrates the concepts of unlimited wants and needs and limited resources. Write a two-paragraph summary of the article that incorporates several of the key terms from the lesson.
THE BASIC ECONOMIC PROBLEM

Individuals and businesses have unlimited wants and needs. The economic resources they have are limited. The mismatch of unlimited wants and needs and limited economic resources is called the basic economic problem. You may want to purchase several products but have a limited amount of money. Your school may have to cut back on certain classes or extracurricular activities because operating costs are increasing faster than the annual budget. A business may want to expand but does not have access to adequate land for a new larger building. A country may not be able to provide adequate health care for all of its citizens because it does not have enough doctors or hospitals.

The basic economic problem results from scarcity. Scarcity means not having enough resources to satisfy every need. Scarcity affects everyone, but some people are more affected than others. People with limited incomes have to carefully choose the best way to spend their money to meet their needs and wants. Countries with few natural resources or people with limited education and low skills may not be able to produce enough products and services for their citizens. Areas with poor transportation or distribution systems or where few businesses are located may not have enough goods to meet the needs of the people.
not have access to the variety of products and services found in other areas.

**Choices**
Everyone makes decisions based on scarcity. Individuals and families must decide how to spread their income among all of the things they want and need. City, state, and national governments must cope with the problem of providing the many services citizens demand using the tax dollars they collect. In each case, someone has to make the difficult choices.

Scarcity forces you to make choices or decisions among the alternatives. How do you decide which option is best? You usually choose the things you want the most or can afford. Suppose you earn $75 a week from a part-time job. If you spend the money you earned this week on a new pair of shoes, you will not have enough left over to spend on a movie and pizza with your friends on Saturday night. Due to the limited resource or amount of money you have, you cannot afford everything. You must make a choice. You must decide which of your wants—the shoes or pizza and movie—you want the most. How do you determine which of these two options will satisfy you the most?

Following a logical process can help you make better decisions. It is a proven way to make many decisions, but is especially useful for making important economic decisions.

**Economic decision-making** is the process of choosing which wants, among several options, will be satisfied. Once you learn the process, your decision-making will be easier and your decisions may lead to better choices.

**Tradeoffs and Opportunity Costs**
Most of the choices you make result from considering a number of alternatives. When you decide on one alternative, you give up on the alternatives you might have chosen. When you give up something to have something else, you are making a tradeoff. You aren’t able to buy a pair of shoes because you decided to spend your money on a movie and pizza with your friends.

The decision-making process helps you select the best and most satisfying alternative from among a set of choices. Economists evaluate an alternative by considering the opportunity cost of a decision. The opportunity cost is the value of the next-best alternative that you did not choose. In making a personal decision, part of your choice will be what you are giving up by the choice you make. The benefit you get from your choice should be greater than the benefit from the next-best choice.

Businesses carefully calculate the opportunity costs of decisions before they make a decision about how they will invest their money. If they use money to purchase land for a new building, what choices must they give up? Would there be a greater value if they spent the money to purchase new equipment that is faster and more reliable? Part of the cost of the land is the opportunity to have better equipment.
THE DECISION-MAKING PROCESS

There are six steps in the decision-making process. You will use the model shown in Figure 1-1 many times as you proceed through the chapters in this book. You will also use it in day-to-day decisions you make. Businesses and individuals use the process as they choose the best uses for their limited resources.

1. Define the problem.
For every decision, the problem must be clearly defined in order to make a decision that will lead to a satisfying solution. If you only have two hours of study time available while you have three tests the next day, your problem is how to best use your time in a way that will bring you the most satisfaction, in this case, preferred test grades.

2. Identify the choices.
It is common for you to face choices with many alternatives. Along with spending money on shoes or the movies and pizza, some other choices you might be faced with are the cost of your lunch and the need to save money for college. In fact, there are many ways you might choose to spend (or save) your $75. It is important to identify and then consider all of the alternatives when making a decision.

3. Evaluate the advantages and disadvantages of each choice.
You might find it helpful to write down your choices and then list the advantages and disadvantages of each choice. If you buy the new shoes, you will be able to wear them many times. It means you will miss the fun of pizza and a movie with friends on the weekend. If you choose to save some of the money, you may be able to make a larger purchase later. You and your friends may determine a less expensive way to spend your time on the weekend.

4. Choose one.
Select the choice that you believe will be the best for you at this particular time. Even if you have done a good job with the first three steps, this is often a difficult step. Realize that choices have consequences that can lie in the future. If you choose option A, how might it affect you later as well as right now?

5. Act on your choice.
Once you have made what you believe is the best decision, do whatever you have chosen. If you have decided to spend your money on a movie and pizza with your friends, go and enjoy yourself. Try not to worry about the choices
you have decided against. Agonizing over a choice or regretting your decision after it is made can take away from the activity you decided upon. Life is full of choices. No matter what you do, there will be times when you will regret a decision even if you carefully considered the alternatives. The next step will help you with those situations.

6. Review your decision.
After you have had a chance to experience the results of your choice, it is important to review your choice. On a scale of one to ten, how would you rank your decision in terms of the level of satisfaction it provided? What was good and not so good about it? If you had to do it over again, would you make the same choice? Given what you now know, do you think there was a better alternative? Were there consequences you hadn't identified?

Based on your review of the decision, how well did you follow the steps of the decision-making process? This step gives you an opportunity to think about your decision and learn from it. Next time you face a similar decision, you may be more comfortable with your choices.

Some decisions have to be made quickly and some with very little information available. For most decisions, the decision-making process will help you make wiser choices.

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**Work as a Group**

You and some friends are meeting with city council members to ask them to build a skateboarding park that would cost $30,000. They ask you to identify the opportunity costs of other recreation alternatives for teenagers. As a group, identify two other alternatives for the city and discuss how you would determine the opportunity costs of each.

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**CHECKPOINT**

What are the six steps in the decision-making process?
Sharpen Your Life Skills

Research Skills

Your abilities are more than just the sum of your experiences. Whether the goal is to improve a business or your own performance, you need to make sound decisions based on the best information available. Research skills are needed to improve decision-making.

Research is a systematic, objective study to establish facts and principles. The research process begins with a question or problem and results in a possible answer that can become the basis for further research.

Here are the steps to follow when conducting research.

Formulate a question. What is the problem you are facing or what is the issue you are trying to resolve? The question should be as specific as possible and relate to an important personal or business issue.

Gather and review information related to the question. Determine if others have studied the same problem and if they have reported on the results of their study. This step usually involves a careful search of library information including books, magazines, and documents.

Separate fact from opinion. Effective research relies on objective data. The opinions of others may provide interesting ideas to consider but should not be relied on for answers to your question. Consider if the sources of information are credible and if the information provided is factual.

Propose a hypothesis. A hypothesis is a prediction about the answer to your research question. The hypothesis can be based on the information gathered, your experience, or your beliefs. You will conduct a study to gather information that will either support the hypothesis or determine that it is wrong.

Collect data to test the hypothesis. Researchers carefully design studies to gather information related to the question and hypothesis. The common methods of collecting data are the use of surveys, making observations, or conducting an experiment.

Analyze the data. After data has been collected, it is organized and then analyzed using statistical procedures. Careful review of the results of the data analysis will provide evidence to support or disprove the hypothesis.

Report the results. It is important that researchers document and report the results of their research. The report will help others understand the research and repeat it or improve upon it. It will also provide evidence that you were objective in the way you completed your research.

Put the research results into practice. You began the research process to answer a question or solve a problem. You need to apply what you learned and determine if what you learned makes a difference. No matter the results, you will want to continue to conduct research and study the research of others. It will help you make sound decisions and have confidence in your knowledge and abilities.

Think Critically
1. Why should you be careful of basing your actions on opinions rather than facts?
2. Do you believe some questions can be answered by just gathering and reviewing information rather than collecting data? Why or why not?
THE THREE ECONOMIC QUESTIONS

All economies (or nations) of the world face the basic economic problem of scarcity of resources. They also have citizens with many basic needs as well as unlimited wants. Each country must decide how the available resources will be used to meet the needs and wants. All economies must answer three economic questions.

1. What goods and services will be produced?
2. How will the goods and services be produced?
3. What needs and wants will be satisfied with the goods and services produced?

How the questions are answered indicates the type of economic system that exists in each country.

What to Produce?

Nations differ in the type and amount of resources just as individuals differ in their skills and abilities. Some nations have rich soil and regular rains that yield large food supplies. Other nations have desert climates or long, cold winters that make farming difficult. Some

Focus on Real Life

Jiang Liang is a resident of modern-day China. His family lived for decades in a small farming community outside of Beijing. There, they faced strict government regulations on what they could and could not grow. Jiang was able to attend Beijing University, where he learned a great deal about computers. With this valuable skill, Jiang moved to Hong Kong, where he worked for a large multinational computer corporation. Jiang was surprised to learn that this company operated without any direct government oversight. The company produced as many computers as it desired and set prices at whatever level it thought best. Jiang has experienced two very different economic systems. Which seems the most like the economic system in the United States?
countries have abundant supplies of oil, coal, and other energy sources, while many countries have only a limited supply. A nation will use its natural resources to determine what can be produced. It can also decide to trade some of its resources with other countries to obtain those it needs.

Just as nations differ in the type and amount of resources, they also differ in their needs. One country may invest heavily in manufacturing, another in agriculture, and a third in security. Some nations have colleges and universities that produce a large number of skilled engineers and technology experts. Other countries have low literacy rates and many unskilled workers. Highways, roads, airports, and shipping ports may be highly developed and functional or transportation may be very difficult.

Deciding how to use resources and what to produce is a very difficult decision. If a country spends too much in one area, there may not be enough resources to meet other needs. If most resources are used to produce the products consumers want, not enough attention may be paid to meeting business needs.

**How to Produce?**

Nations must decide what combination of resources will best suit its circumstances. As a country evolves, tasks that are traditionally performed by human skills, such as farming in the United States, are now performed with faster, more efficient tools and equipment. Two centuries ago, more than 80 percent of U.S. citizens were involved in agriculture. Today, less than 3 percent of the U.S. population produces the food the country consumes. The labor needs of the U.S. economy have changed. The complex 21st century economy requires highly specialized health care professionals, financial managers, computer specialists, and others who can design and produce the goods and services that you need and want.

Each country decides how to use its resources to produce the goods and services it needs. It may rely on unskilled or skilled labor, on advanced or simple technology, on its own resources, or on those it obtains from other countries. Economic resources combine in different ways to produce the same goods and services.

**What Needs and Wants to Satisfy?**

Because wants and needs are unlimited, many will remain unmet when a country decides what goods and services to produce. A country must determine which needs and wants are the most critical when deciding what goods and services to produce. Some countries may decide to invest in capital goods, while others produce more consumer goods. Some countries devote more resources to producing the goods and services required by the government. Other economies respond to those citizens who have the most money or the most political power.

In the United States, goods and services are plentiful. What wants and needs you satisfy largely depends on how much money you have and how you choose to spend or save it. The amount of money you have available to spend depends a great deal on your education and ability and how you decide to use them to earn income.

**CHECKPOINT**

What are the three economic questions?
Types of Economic Systems

A nation’s plan for answering the three economic questions is called its economic system. The type of system is based on how much the government is involved in the marketplace. There are several kinds of economic systems operating in the world today. Each is based on one of the three main types.

Command Economy

In a command economy, the resources are owned and controlled by the government. Government officials decide what and how goods are produced and how they will be distributed and shared. They decide how much of the resources will be used to produce goods and services for consumers such as food products, vehicles, or houses. They also decide how much of the resources will be used to produce capital goods including machinery, equipment, and factories.

In a command economy, the government may decide to build a superior military or a world-class education system. They may decide to spend money to research new technologies or to build housing for the poor. Some command economies are so strict that government officials assign people to specific schools and even careers. Personal economic freedom is limited in a command economic system.

Market Economy

In a market economy, the resources are owned and controlled by the people of the country. The three economic questions are answered by individuals through buying and selling of goods and services in the marketplace. The marketplace is anywhere that goods and services exchange hands. This includes a supermarket, the Internet, a business office, or even a flea market.

When a business buys a new truck or orders several tons of steel, it is making an economic decision. An individual consumer who orders a movie on a pay-per-view channel, takes a vacation, or enrolls in college is also making an economic decision. No one directs consumers to make a particular purchase or tells businesses what they must produce. The government has limited involvement in a market economy.

Consumers and businesses make decisions based on their own self-interest. Every time consumers buy products in the marketplace, they “vote” with their dollars. They send a message to businesses regarding their buying preferences, helping to direct the use of resources. Businesses make decisions on what goods and services will be produced based on how they decide to
Work as a Group

Your group represents the citizens of a new country deciding on an economic system. You want to establish a successful economy that provides the greatest benefit to its citizens. What information about the country would you need to know in order to answer the three economic questions?

Traditional Economy

Before complex economic systems developed, simple economies operated according to tradition or custom. In a traditional economy, goods and services are produced the way it has always been done. The traditional economy is used in countries that are less developed and are not yet participating in the global economy.

In those countries, the answers to the three economic questions are still established by their traditions. Goods are produced the way they have always been produced, generation after generation. Children are taught to use the same methods to make the same goods their ancestors produced. They often use the natural resources readily available to them and the hand tools they make. They will consume most of what they produce and sell or trade the rest with people who live close to them.

The traditional economy is usually centered on meeting the basic needs of people such as food, clothing, and shelter. While the global economy has brought change and growth to the farthest corners of the world, there are still pockets of people living in traditional economic systems. Because these economies lack the many formal structures found in more advanced systems, they usually have limited amounts of material wealth and limited investment in improving their conditions.

Mixed Economies

Most nations of the world can be classified as a mixed economy. A mixed economy combines elements of the command and market economies. While the past half-century has seen a shift away from command economies and toward market economies, various degrees of government involvement in the marketplace exist.

The former Soviet Union disbanded and became 15 independent nations in the early 1990s. For over 70 years, the Soviet Union operated under a command economic system called communism. Under communism, the Soviet Union underwent a series of government-led plans to direct resources toward economic growth. This led to a
limited choice and supply of consumer goods. Often, consumers found it difficult to find such products as bread or a hammer.

During the past decade several of the Eastern European nations that had used a command economy have made major progress in changing over to a mixed economy. Several of these countries recently earned membership into the European Union.

The 1.3 billion Chinese citizens live under a different type of communist government that controls most of the resources and decisions. The economy of China is adopting elements of a market system for a growing number of economic decisions. Entire regions of the country, particularly the eastern cities bordering the ocean, are enjoying a booming consumer economy based on greater individual freedom of choice. China is fast becoming a world leader in goods and services produced. A competitive education system produces many skilled workers who are opening businesses daily and earning money to pay for the goods and services they want.

As many countries with traditional economies develop, they often adopt mixed economies. The government makes many of the decisions about how the country’s resources will be used to develop schools, hospitals, roads, and utilities. As people become educated and develop new skills, they are able to obtain jobs and earn money. They then have the resources to purchase more goods and services. Often businesses from other countries will begin to sell products and services in the developing country or even open a business offering jobs and locally produced products to the citizens.

THE U.S. ECONOMIC SYSTEM

Can you identify the economic system of the United States? Since individual businesses and consumers make most of the decisions about what will be produced and consumed, the U.S. system best fits the definition of the market economy.

Another name for the economic system in the United States is capitalism. Capitalism refers to the private ownership of resources by individuals, rather than by the government. Individual owners are free to decide what to produce. Individual consumers are also free to decide what they want to buy. This freedom of production and consumption decisions lends itself to another name often associated with the U.S. economy—free enterprise or private enterprise. Individual freedom is vital to the success of the U.S. economy.

The U.S. economic system is based on four important principles. They are private property, freedom of choice, profit, and competition.

**Private Property**

The right of private property means you can own, use, or dispose of things of value. In the U.S., you can own anything you want and decide what you want to do with it, as long as it does not violate the law. If you invent something of value, you are protected from others taking your idea.

**Freedom of Choice**

The private enterprise economy is based on freedom of choice. Freedom of choice means that you can make decisions independently and must accept the consequences of those decisions. Business owners can decide where to open a business, what to sell, and how to operate the company. Consumers can decide where to shop, what to buy, and what they want to spend. Only when individual decisions harm others will the government regulate freedom of choice.

> Describe the economic system of the United States.

WHAT ARE THE MAIN DIFFERENCES AMONG THE THREE ECONOMIC SYSTEMS?
**Profit**

Businesses invest resources and take risks for one primary purpose—to earn a profit. Profit is the money left from sales after all of the costs of operating a business have been paid. Because businesses are not guaranteed a profit, they may lose the money they have invested. They are challenged to work hard, invest wisely, and produce goods and services that are needed in order to make a profit.

Profit is at the heart of the private enterprise system. Earning a profit is not the only reason for investing money and operating a business. People enjoy the challenge and freedom of business ownership as well as the satisfaction of providing goods and services that other people want.

**Competition**

The rivalry among businesses to sell their goods and services is known as competition. Consumers have many choices of products and services and will select the one they believe will provide the greatest satisfaction for the money. Businesses must work to improve their products and reduce their costs. If customers are not satisfied with one company’s offerings, they will look for another choice. Competition forces businesses to improve products, keep costs low, provide effective customer service, and search for new ideas.

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**1-3 Assessment**

**Key Concepts**

Determine the best answer.

1. Which of the following addresses the economic question of how to produce?
   a. growing corn instead of potatoes
   b. requiring individuals to work in a particular career
   c. producing more capital goods and fewer consumer products
   d. selling natural resources to other countries

2. In which of the following economic systems is the government’s role most limited?
   a. mixed
   b. traditional
   c. market
   d. communism

3. The primary reason business owners make investments and take risks is to
   a. make a profit
   b. satisfy customer needs
   c. develop new products
   d. make their own decisions

**Make Academic Connections**

4. Research Choose one of the following five countries. Research that country and write a report describing its current economic system.
   - Chile
   - Latvia
   - Costa Rica
   - Zimbabwe
   - Singapore

5. Math Use an Internet search engine to gather pricing information on each of the products listed. Identify the highest and lowest price at which each of the products is sold. Calculate the difference in the prices for each product. Create a bar chart that illustrates each of the prices and the amount of difference between the high and low prices.
   a. Ford Focus
   b. Apple iPod
   c. 1 year of college tuition
Focus on Real Life

Jody and Dennis are both in the mood for some Italian food. Their town has two Italian restaurants, Restaurante Italia and Mamma’s Pizzeria. Both Jody and Dennis are on a limited budget, so they are always careful about how they spend their money. Mamma’s Pizzeria is famous for its delicious pizza and has excellent service. Restaurante Italia has a broader menu offering both pizza and pasta dishes. Jody and Dennis both feel the food is good but doesn’t have that authentic Italian flavor. Often, the restaurant is crowded with slow service. Because Momma’s is known for the best pizza in town, the prices are quite a bit higher than at Restaurante Italia. If you were going to eat with Jody and Dennis, how would you decide which restaurant to choose?

PARTICIPATING IN A MARKET ECONOMY

In a market economy, buyers and sellers use the marketplace to make economic decisions. Buying decisions are made by consumers—including individuals, businesses, and government. A consumer is a person who buys and uses goods and services. The individual buying decisions of consumers have a tremendous influence on the market economy. Consumers decide what to buy, where to buy, from whom to buy, and what price they are willing to pay.

Producers pay close attention to the needs and activities of consumers. Producers are individuals and organizations that determine what products and services will be available for sale. Producers invest resources and take risks in order to make a profit. They determine what products and services will be available in the economy, what needs and wants they will try to satisfy, and the prices they want to receive.

Goals

> Describe supply and demand orally and with graphs.
> Discuss how supply and demand affect prices of products and services.

Key Terms

consumer
producers
demand
supply
market price

It may seem that the economy is a big, unorganized system in which everyone pursues his or her own self-interest. You may wonder how the system can work when each business makes its own decisions about what to produce, while each consumer makes a decision about what and where to buy. The system does work and works well based on the principles of supply and demand.
Consumers Set Demand

When consumers make decisions about what they will purchase, they determine the demand for goods and services. Demand is the quantity of a good or service that consumers are willing and able to buy. A business can prosper or fail based on the demand for their products and services. For example, if a new restaurant opens in your town, but the service is slow, the quality of the food is poor, and the noise level is high, will consumers continue to eat there? It is not likely. Suppose a new restaurant opens with terrific food as well as fast and friendly service. That restaurant will probably be packed with people waiting in line for dinner.

Producers Establish Supply

Understanding demand tells a business what type and what quantity of products and services to supply. Supply refers to the quantity of a good or service that businesses are willing and able to provide. If consumers are seeking a popular product and are willing to pay a high price for it, businesses will provide the product to meet customer needs. On the other hand, if there is heavy competition for a product keeping the prices low or if customers are tiring of an older product, businesses are less likely to want to offer the product for sale.
product illustrates the relationship between the price of a product and the quantity demanded by consumers. As the price decreases, the number of consumers willing and able to purchase the product will increase. Figure 1-2 illustrates the possible demand for movie rentals at various prices.

In the same way, the supply curve for a product illustrates the relationship between the price of the product and the quantity businesses will supply. As the price increases, businesses will be willing to supply larger quantities of the product. Figure 1-3 illustrates the possible supply of movie rentals at various prices.

DETERMINING PRICE
Why is the price of a hotel room in Phoenix, Arizona, higher in winter than summer? Why do the prices for many of the products sold by farmers remain quite low? Prices are affected by the relationship between supply and demand, plus other factors.

Factors Influencing Demand
If many consumers want (or demand) a particular good or service, its price will tend to go up. More people vacation in Phoenix in the winter than in the summer so demand and prices for hotel rooms rise. When fewer people visit that area during the hot summer, the supply of hotel rooms is greater than the demand. Therefore, prices will decline.

When customers see a number of products that they believe will satisfy a particular want or need, demand for any one of those products will not be as high. Customers will be willing to switch from one product to another if the price of one is much higher than the others. When customers cannot find a good substitute for a product they want, demand for that product will be high. Even if the price increases, they will be willing to pay the higher price because they are unwilling or unable to switch to another choice.

Factors Influencing Supply
The supply of a product can also affect the price. Because the supply of many of the crops and livestock raised on farms is large, prices remain low. If a drought cuts the quantity of corn grown by Midwest farmers one year, the price of corn will increase.

Competitors are businesses offering very similar products to the same customers. As the number of competitors increases, a business will not be able to easily raise its prices. It will have to be much more sensitive to the prices charged by its competitors.

When competition is limited, consumers cannot find good alternatives. If you live in a part of town where there is only one supermarket, the prices at that store will often be higher due to a lack of competition. The prices of products featuring new technology will often be high since the company offering the new product seldom has direct competition.

Sometimes a natural disaster or other unforeseen circumstance affects supply. If the supply of oil, gasoline, or water is disrupted, their prices will increase. The supply of other products that use those resources will decrease, causing their prices to increase as well.

The prices of some products change a great deal in a short time, while the prices for other products remain quite stable. Work as a group to identify several products that experience regular price changes and several that do not. Discuss how supply and demand appear to affect the prices of the products in each of the groups.
resources in production may also be affected and their prices can increase as well. Sometimes businesses will try to restrict supply of products in order to obtain a higher price. That will only work if customer demand is high and if there are no good substitutes for the product.

**Determining Market Price**

Supply, demand, and competition determine the market price for a product or service. The market price is the point where supply and demand are equal. Figure 1-4 shows the market price for movie rentals. Consumers are willing to rent nearly 2,000 movies and businesses are willing to supply that same number of movies if the rental price is just below $6.00 per movie.

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### Figure 1-4

The market price for a product is the point where supply and demand are equal.

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### Market Price for Movie Rentals

![Graph showing supply and demand curves with the market price at $6.00 per movie]

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### CHECKPOINT

How is the market price for a product determined?

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### 1-4 Assessment

#### Key Concepts

Determine the best answer.

1. True or False. Both individuals and organizations can be producers.

2. True or False. Supply is the quantity of a good or service that a consumer is willing and able to buy at a particular price.

3. As competition increases, prices
   a. usually increase as well
   b. are not affected so will usually not change
   c. usually will decrease
   d. There is no way to predict what will happen to prices.

#### Make Academic Connections

4. **Math** Calculate the total value of sales at each possible price for a product with the consumer demand shown in the table.

<table>
<thead>
<tr>
<th>Price</th>
<th>Quantity demanded</th>
</tr>
</thead>
<tbody>
<tr>
<td>$20.00</td>
<td>8,500</td>
</tr>
<tr>
<td>$22.50</td>
<td>7,800</td>
</tr>
<tr>
<td>$25.00</td>
<td>6,200</td>
</tr>
<tr>
<td>$27.50</td>
<td>5,900</td>
</tr>
<tr>
<td>$30.00</td>
<td>4,300</td>
</tr>
</tbody>
</table>

5. **Communication** Write a memo to an entrepreneur who is opening a new restaurant in your community. Explain the importance of supply and demand in determining the prices to charge at the restaurant. Give the new business owner advice on how to avoid lower prices due to competition.
Business Improving Society

Heifer International

Ending hunger and poverty around the world! It sounds like such a big dream that no one would undertake it. Nevertheless, since 1944, Heifer International has had that dream as its goal. Through a unique program of giving communities a source of food rather than just distributing food, the organization has reached millions of families in over 115 countries.

Dan West was a midwestern farmer serving as a relief worker during the Spanish Civil War. With a limited supply of milk and food, he had to decide who would receive the rations and who would not.

As a farmer, Mr. West realized that if people had livestock, farming tools, and some assistance in learning effective farming practices, they would have the capability to raise food for themselves and their families for a lifetime.

He returned to the United States and formed Heifers for Relief. He asked other farmers to donate a heifer. Dan delivered the first shipment of 17 heifers to Puerto Rico, giving them to families with malnourished children who had never tasted milk before. Why heifers? The young cows would give birth to a new calf. Each family that received a heifer and training in how to raise and maintain dairy animals was asked to “pass on the gift” by donating a calf to another family.

For 60 years, Heifer International has been developing new projects around the world. Their mission is to work with communities to end hunger and poverty and to care for the earth. They envision a world of communities living together in peace and sharing the resources of a healthy planet. Today hundreds of thousands of people continue to donate heifers, rabbits, goats, and chickens. Others make cash contributions to purchase livestock and supplies. Many people volunteer their time to travel to the rural communities with the animals to provide training and assistance so that the livestock will remain healthy, grow, and multiply for further distribution.

Recent projects of Heifer International include:
- Sending five rural veterinarians to Mongolia to work with animal herders to teach them improved animal management. These herders will then work with 500 additional herding families.
- Distributing 140 dairy cattle to 100 farm families in Kosovar who were victims of the war in their country in 1999.
- Placing 500 hives of bees in five Adaklu communities in Ghana, Africa. The communities will be taught hive management and honey harvesting techniques that do not harm the environment. Honey is a major source of nutrition in an otherwise malnourished area that suffers from illiteracy and high child mortality.

Think Critically

1. How does this approach to solving world hunger differ from other relief efforts that distribute food, milk, clothing, and health supplies?

2. Use the Internet to locate examples of other organizations that are working to reduce hunger around the world. How are they similar to or different from Heifer International?
1-1 Satisfying Needs and Wants
1. Things that are necessary in order to live are needs. Things that add comfort and pleasure to life are wants.
2. Goods are things that you can see and touch. Services are intangible, meaning they have no physical characteristics.
3. Economic resources are the means through which goods and services are produced. Economic resources are also known as factors of production. The three kinds of economic resources are natural resources, human resources, and capital resources.

1-2 Economic Choices
4. Most choices result from considering a number of alternatives. When you give up something to have something else, you are making a tradeoff. The opportunity cost is the value of the next best choice.
5. The six steps in the decision-making process are: define the problem, identify the choices, evaluate each choice, make a choice, act on the choice, and review your decision.

1-3 Economic Systems
6. All economies must answer three economic questions. What goods and services will be produced? How will the goods and services be produced? What needs and wants will be satisfied with the goods and services produced?

7. A nation’s plan for answering the three economic questions is its economic system. In a command economy, the resources are owned and controlled by the government. In a market economy, the resources are owned and controlled by the people of the country. In a traditional economy, goods and services are produced the way it has always been done. A mixed economy combines elements of command and market economies.

8. Capitalism refers to the private ownership of resources by individuals rather than by the government. The U.S. economic system is based on the principles of private property, freedom of choice, profit, and competition.

1-4 Supply and Demand
9. In a market economy, buyers and sellers use the marketplace to make economic decisions. Demand is the quantity of a good or service that consumers are willing and able to buy. Supply is the quantity of a good or service that businesses are willing and able to provide.
10. If many consumers demand a particular good or service, its price will go up. If competition increases so customers have choices, businesses will not be able to easily raise their prices. The market price is the point where supply and demand are equal.

Communicate Business Concepts
1. Identify five products or services that could be either a need or a want. Provide an example for each that illustrates when it would be considered a need and when it would be considered a want.
2. Select a business with which you are familiar. Describe factors of production used by the business that fit within each of the three kinds of economic resources.
3. Find a newspaper or magazine article that deals with scarcity of a product, service, or natural resource. Write a summary of the article in which you identify who is affected by the scarcity and the affect it is having on business or consumer markets.
4. Identify a problem you will face in the near future, such as selecting a college or career or making a major purchase. Describe how you would complete each step in the decision-making process for the problem.
5. Identify a possible opportunity cost for each of the following:
   a. Trying out for an athletic team
   b. Accepting a part-time job
   c. Studying for an important exam
   d. Saving money to buy a used car
   e. Obtaining a loan to start a business

6. Develop a table that compares the answers to the three economic questions in a command economy, a market economy, and a traditional economy.

7. Explain how freedom of choice can affect the availability of products and services for consumers. Now explain how it can also affect the profit a business might make on the products and services it sells.

8. Do you agree that the term “private enterprise” is a good description of the United States economy? Why or why not?

9. Select a product that is a regular purchase of many consumers. Use a graphing program to develop an illustration of a supply and demand curve for the product. Prepare a brief oral description of the illustration.

10. Review recent news reports of products and services where the price has been affected by supply and demand factors. Write a report using those examples that discusses the effect of supply and demand on prices.

>> Develop Your Business Language

Match the terms listed with the definitions.

11. Process of choosing which wants, among several options, will be satisfied.

12. Individuals and organizations that determine what products and services will be available for sale.

13. A nation’s plan for answering the three economic questions.

14. Means through which goods and services are produced.

15. Things that are required in order to live.

16. Not having enough resources to satisfy every need.

17. Quantity of a good or service that businesses are willing and able to provide.

18. Person who buys and uses goods and services.

19. System in which resources are owned and controlled by the government.

20. Things that you can see and touch.

21. Private ownership of resources by individuals rather than by the government.

22. System in which goods and services are produced the way it has always been done.

23. System that combines elements of the command and market economies.

24. Quantity of a good or service that consumers are willing and able to buy.

25. Point where supply and demand are equal.

26. Things that add comfort and pleasure to your life.

27. Activities that are consumed at the same time they are produced.

28. Giving up on something to have something else.

29. Value of the alternative you did not choose.

30. System in which the resources are owned and controlled by the people of the country.

Key Terms
   a. capitalism
   b. command economy
   c. consumer
   d. demand
   e. economic decision-making
   f. economic resources
   g. economic system
   h. goods
   i. market economy
   j. market price
   k. mixed economy
   l. needs
   m. opportunity cost
   n. producers
   o. scarcity
   p. services
   q. supply
   r. tradeoff
   s. traditional economy
   t. wants
**Decision-Making Strategies**

31. Countries that make efficient use of capital goods can produce more with fewer people in a shorter time than countries in which many workers perform the work by manual labor. Study the figures below for farm workers and their yearly output in two different kinds of economic systems, then answer the questions that follow.

<table>
<thead>
<tr>
<th></th>
<th>Traditional economy</th>
<th>Market economy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Size of the agriculture labor force</td>
<td>34,350,000</td>
<td>4,380,000</td>
</tr>
<tr>
<td>Number of people supplied with food from the labor of each agriculture worker</td>
<td>7</td>
<td>49</td>
</tr>
</tbody>
</table>

**Make Academic Connections**

32. **RESEARCH** Identify a product for which you believe there is a great deal of competition and one that you believe has very little competition. Use the Internet, newspapers, or personal shopping to identify the prices charged by three companies offering the product. Prepare a table to show the information you collected. Based on that information, do you believe you were correct in your original decision about the amount of competition for each product? How does the information support your belief?

33. **DECISION-MAKING** Sheila’s father told her that with the family’s limited resources, she would have to choose between continuing her dance lessons or a season ticket to the monthly performances of the local theater. This means that Sheila is on step 3 of the decision-making process. Complete step 4 for Sheila, listing the advantages and disadvantages of the two choices.

34. **COMMUNICATION** Your community has received a gift of 100 acres of land from a long-time citizen. A community group is encouraging the city council to use the land to develop a park. Another group would prefer that it be developed as an area for new small businesses. Prepare a one-page report for the city council comparing the two choices based on opportunity costs.

35. **MATH** The table below shows the average number of working hours it takes a worker in three cities in different countries to earn enough money to purchase several products and services. Use the information to answer the following questions:

<table>
<thead>
<tr>
<th></th>
<th>Country 1</th>
<th>Country 2</th>
<th>Country 3</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 lb. of ground beef</td>
<td>17.0 min.</td>
<td>29.0 min.</td>
<td>56.0 min.</td>
</tr>
<tr>
<td>Large-screen TV</td>
<td>65.0 hr.</td>
<td>132.0 hr.</td>
<td>701.0 hr.</td>
</tr>
<tr>
<td>1 tube of toothpaste</td>
<td>16.0 min.</td>
<td>13.0 min.</td>
<td>27.0 min.</td>
</tr>
<tr>
<td>City bus fare</td>
<td>7.0 min.</td>
<td>11.0 min.</td>
<td>3.0 min.</td>
</tr>
<tr>
<td>1 pair of men’s shoes</td>
<td>8.0 hr.</td>
<td>7.0 hr.</td>
<td>25.0 hr.</td>
</tr>
<tr>
<td>1 week of food for a family of 4</td>
<td>18.6 hr.</td>
<td>24.7 hr.</td>
<td>53.5 hr.</td>
</tr>
</tbody>
</table>
Linking School and Home

Gather information or make observations in your home and neighborhood that illustrate how supply and demand work to establish the market price for products and services. Find one example where there appears to be evidence of high consumer demand, another with evidence of a great deal of competition among businesses, and a third where other factors seem to be influencing the market price of a product or service. Prepare an oral report to describe what you learned about supply, demand, and price to other students in your class.

Portfolio Activity

To provide tangible evidence of your learning about the economic environment of business, do the following:

COLLECT an example that illustrates an economic principle or concept you learned in one of the lessons from this chapter. The example could be a picture, drawing, product, or written description of something you observed.

CREATE a diagram or flowchart that illustrates how the three economic decisions are answered in the United States economic system.

CONNECT the example you collected to the diagram or flowchart you developed by describing how it connects to the U.S. economic system.

Entrepreneurship Event

Entrepreneurs are leaders who take the risk of starting new business ventures. Individuals who are willing to start a business face more than a 50 percent chance of failure within the first five years of operation. Successful entrepreneurs must conduct research, secure financing, and convince consumers to purchase the goods/services they offer.

You must develop a business plan for a new business in your community. The business plan must not exceed ten single-spaced pages.

Your business plan must include the products or services to be provided, market analysis, customer profile, competition, short-range operational goals, financial analysis (income statement, balance sheet, cash flow statement, and other analyses), and supporting research documents.

You will orally present your business plan to the class/judges for 10 minutes. Class members or judges have up to five minutes to ask you questions about your business plan.

Performance Indicators Evaluated

- Develop a written business plan for a start-up business.
- Identify the customer base, including consumer and organizational markets and highlighting demographics.
- Analyze financial data.
- Demonstrate successful price selection methods.
- Identify and use internal and external resources.
- Knowledge and understanding of entrepreneurship
- Communication of research in a clear and concise manner both orally and in writing
- Demonstration of effective persuasive and informative communication and presentation skills

For more detailed information about performance indicators, go to the BPA web site.

Think Critically

1. Why does your community need the business you have selected?
2. What are your strengths, weaknesses, opportunities, and threats with this business proposal?
3. What is the most effective means to advertise your business?
4. Who are the sources to finance your business idea?
5. When do you plan on first making a profit with this business venture?
Planning a Career in...
Economic Development

A career in the economic development field could involve a variety of employment opportunities. If you have the interest and obtain the required training, you could be a corporate executive, a government research director, or a field training consultant. Each of these jobs provides contributions to economic growth.

As you study various topics in this book, your awareness of economic development work will expand. Many positions in the economics profession are related to employment in government, technology, research, engineering, health care, nutrition, marketing, and financial planning. Every country in the world is in need of efforts to enhance its economic development and improve the quality of life for its citizens. Your decision for a career in economic development will have you participating in how a society allocates its scarce resources among its unlimited wants and needs.

Employment Outlook

• Job growth in the economic development field will continue to grow over the next decade.
• Specialized technical skills (engineering, health care, computer technology, food processing) will be in demand, especially in developing economies of the world.

Job Titles

• Economist
• Transportation Engineer
• Urban and Regional Planner
• Survey Researcher
• Statistician
• Statistical Assistant
• Budget Analyst
• Financial Analyst
• Operations Research Analyst

Needed Skills

• Requires a bachelor’s degree. More advanced positions need a master’s degree or even a doctorate.
• Sociology and cultural knowledge is needed for work in urban settings and in developing nations.
• Special training in statistics, research, health care, technology, nutrition, and other fields will be helpful.

What’s it like to work in...
Economic Development

As the sun rises over the mountains, hundreds of workers are already on the job. The people in this village know that they have to harvest enough crops to sell for their family income. The task is difficult, as working by hand has limits.

In a nearby village, an international organization has helped some of the people obtain oxen and used farm equipment. These items have allowed the workers to double and triple their daily harvests.

Many government and private agencies work to help people improve their labor productivity. The use of new growing methods, machinery, and other agricultural advances can provide families with more money for food, housing, clothing, and health care. Funding for these improvements is often uncertain. Money may come from private investors or government grants and loans.

What about you? In what aspects of economic development might you be interested in working?
GROSS DOMESTIC PRODUCT (GDP)

Economic growth refers to a steady increase in the production of goods and services in an economic system. Just as you use different ways to measure your own growth, different methods can be used to measure the growth of an economy.

One way to find out how well an economy is doing is to compare output from year to year. Governments collect information from producers and estimate national output. The most widely used measure is gross domestic product. Gross domestic product or GDP is the total dollar value of all final goods and services produced in a country during one year. Figure 2-1 reports the GDP of various countries in a recent year.

Components of GDP

Gross domestic product includes four major categories of economic activity:

1. Consumer spending for food, clothing, housing, and other spending

<table>
<thead>
<tr>
<th>Country</th>
<th>Total GDP (U.S.$)</th>
<th>GDP per capita</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States</td>
<td>$10.9 trillion</td>
<td>$36,000</td>
</tr>
<tr>
<td>China</td>
<td>$6.4 trillion</td>
<td>$4,300</td>
</tr>
<tr>
<td>Japan</td>
<td>$3.6 trillion</td>
<td>$28,700</td>
</tr>
<tr>
<td>India</td>
<td>$3.0 trillion</td>
<td>$2,500</td>
</tr>
<tr>
<td>Germany</td>
<td>$2.3 trillion</td>
<td>$26,200</td>
</tr>
<tr>
<td>Brazil</td>
<td>$1.4 trillion</td>
<td>$7,560</td>
</tr>
<tr>
<td>Canada</td>
<td>$957 billion</td>
<td>$29,000</td>
</tr>
<tr>
<td>Mexico</td>
<td>$942 billion</td>
<td>$8,800</td>
</tr>
<tr>
<td>South Africa</td>
<td>$456 billion</td>
<td>$10,000</td>
</tr>
<tr>
<td>Poland</td>
<td>$426 billion</td>
<td>$9,660</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>$286 billion</td>
<td>$10,600</td>
</tr>
<tr>
<td>Vietnam</td>
<td>$204 billion</td>
<td>$2,100</td>
</tr>
<tr>
<td>Nigeria</td>
<td>$113 billion</td>
<td>$840</td>
</tr>
<tr>
<td>Bolivia</td>
<td>$21.4 billion</td>
<td>$2,600</td>
</tr>
</tbody>
</table>
2. Business spending for buildings, equipment, and inventory items
3. Government spending to pay employees and to buy supplies and other goods and services
4. The exports of a country less the imports into the country

Some goods and services are not included. For example, GDP does not include the value of the work you do for yourself, such as cutting your own lawn or building a picnic table for your yard. If you buy the lawn service or the picnic table from a business, they would be included.

Only final goods, such as cars, are counted when you measure GDP. Intermediate goods used in manufacturing, such as steel and fabrics, are not included. If intermediate goods were counted as well, the value of the intermediate goods would be counted twice.

If the GDP increases from year to year, this usually signals that an economy is growing and is healthy.

**Comparing GDP**
The United States had an annual GDP of about $11 trillion in recent years. The more goods and services produced, the healthier an economy is considered to be. Just referring to the dollar value of GDP as a measure of economic growth does not tell the whole story.

Another way to measure economic growth is **GDP per capita** or output per person. GDP per capita is calculated by dividing GDP by the total population (see Figures 2-1 and 2-2). For example, suppose that there is no change in GDP this year over last year. Suppose, also, that the population increases. The same output would have to be divided among more people.

An increase in GDP per capita means that an economy is growing. A decrease may mean that an economy is having trouble.

**Work as a Group**
The GDP of a country presents information about the economic output of a country. In your group, prepare a list of drawbacks resulting from only looking at GDP when evaluating the economic progress of a nation. What aspects of economic growth may not be reflected in the GDP of a country?
LABOR ACTIVITIES

The workers of a country contribute to the economy in several ways. First, their labor activities create needed goods and services. In addition, the wages they receive are spent to create demand for various items.

Employment

Today, more than 130 million people work in the United States. These members of the labor force are employed in thousands of different jobs. They produce thousands of different products and services. The labor force consists of all people above age 16 who are actively working or seeking work. Students, retired people, and others who cannot or do not wish to work are not part of the labor force.

One economic statistic of concern is the unemployment rate. The unemployment rate is the portion of people in the labor force who are not working. People are considered to be “unemployed” if they are looking for work and willing to work but unable to find a job.

Unemployment rates vary from year to year and in different areas of the country. The main cause of unemployment is reduced demand for the goods and services being provided by various workers. If fewer people travel by bus, for example, bus companies will need fewer workers.

Productivity

A vital source of economic growth is an increase in output per worker. Productivity is the production output in relation to a unit of input, such as a worker. Improvements in capital resources (equipment and technology), worker training, and management techniques can result in more output per worker.

Over time, the rate of growth in labor productivity has ups and downs. While increases in productivity occur in many years, the amount of the increase often becomes smaller. Sometimes, productivity may actually decrease.

If wages increase faster than gains in productivity, the cost of producing goods increases and prices rise. Even though workers earn more money, they are not able to improve their standard of living because of rising prices. For that reason, strong attention has been given to ways of motivating workers to increase productivity. By doing so, workers will be contributing to a higher standard of living in the nation while also improving their own life situation.

An ability to produce more goods and services makes it possible to reduce the number of hours in a workweek. In the early 1890s, the average worker in the U.S. put in about 60 hours a week. Today, the average workweek for many factory and union-contracted jobs has decreased to less than 40 hours. At the same time, some people have decided to take positions that require working more than 40 hours a week.

In many industries, even though U.S. employees work fewer hours, more is produced and earned than ever before. More can be produced in less time because of technology and efficient...
work methods. The training and skill of workers also contribute to improved productivity.

CONSUMER SPENDING
The money you earn and spend is one of the most important factors for economic growth.

Personal Income
Each day, people receive money from their participation in production. Personal income refers to salaries and wages as well as investment income and government payments to individuals. These funds provide the foundation for buying needed goods and services.

Retail Sales
On a monthly basis, the U.S. Department of Commerce measures retail sales, or the sales of durable and nondurable goods bought by consumers. These retail sales are an indicator of general consumer spending patterns in the economy. Increasing retail sales usually points toward economic growth.

The main items measured for estimating retail sales include automobiles, building materials, furniture, gasoline, and clothing, as well as purchases from restaurants, department stores, food stores, and drug stores.

FYI
The labor force in many countries of the world may not be well defined. Poor economic conditions may require family members of all ages to work on farms or in home factories to provide an income to cover the costs of basic living expenses.

CHECKPOINT
What are ways to increase productivity?

CHECKPOINT
What are the main sources of personal income?

2-1 Assessment

Key Concepts
Determine the best answer.

1. Which of the following would not be included in GDP?
   a. exports to other countries
   b. purchases of computers by government
   c. automobiles purchased
   d. dinner preparation for your family

2. Productivity would likely increase as a result of
   a. higher taxes
   b. expanded production technology
   c. decreased training programs
   d. lower government spending

Make Academic Connections

3. Retail sales include
   a. taxes collected
   b. companies buying new equipment
   c. borrowing by business
   d. school supplies bought by students

4. Technology Using the data in Figure 2-1, create a graph with a spreadsheet program to compare the GDP and GDP per capita for five countries you select.

5. Visual Art Obtain data on the total U.S. unemployment rate for recent years and the rate in various cities or regions of the country. Prepare a graph to show changes in the unemployment rate.
The Business Cycle

Over the decades, economists have observed that our economic activity tends to move in cycles. All nations experience economic good times and bad times. Fortunately, over time, bad conditions disappear and good conditions return.

Looking at the economic changes during the history of the United States shows a pattern of good times to bad times and back to good times. This movement of the economy from one condition to another and back again is called a business cycle.

Business cycles are the recurring ups and downs of GDP. Business cycles have four phases: prosperity, recession, depression, and recovery.

Prosperity

At the peak of the business cycle is prosperity. Prosperity is a period in which most people who want to work are working, businesses produce goods and services in record numbers, wages are good, and the rate of GDP growth increases.

The demand for goods and services is high. This period is usually the high point of the business cycle. Prosperity, though, does not go on forever. The economy eventually cools off and activity slows down.
Recession
When the economy slows down, a phase of the business cycle known as recession occurs. **Recession** is a period in which demand begins to decrease, businesses lower production, unemployment begins to rise, and GDP growth slows for two or more quarters of the calendar year.

This phase may not be too serious or last very long, but it often signals trouble for some groups of workers in related businesses. This drop in related businesses is called the ripple effect. Eventually, production weakens throughout the economy, and total output declines in the next quarter. Some recessions last for long periods as fewer factors of production are used and total demand falls.

**Depression**
If a recession deepens and spreads throughout the entire economy, the nation may move into the third phase, depression. **Depression** is a phase marked by a prolonged period of high unemployment, weak consumer sales, and business failures.

GDP falls rapidly during a depression. Fortunately, our economy has not had a depression for more than 60 years. This period in U.S. history (1930–1940) is referred to as the Great Depression.

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**A Question of Ethics**

**Ethical Analysis Guidelines**

1. **Is the action legal?** Laws vary among states and in different countries. Most companies base international decisions on the laws in their home countries. When a conflict occurs, managers usually consider other factors, such as professional standards and the effect of the action on society.

2. **Does the action violate professional or company standards?** Professional or company standards will frequently exceed the law. This helps to ensure that decisions will be in the best interest of both the company and the society in which it operates.

3. **Who is affected by the action and how?** An action may be legal and within professional or company standards. Decision-makers should also consider possible effects on employees, consumers, competitors, and the environment.

**Think Critically**

1. What are some examples of situations faced by workers and consumers that require ethical decisions?

2. Describe the effect on business activities if no ethical guidelines existed.

3. Research recent ethical situations that have been in the news. How have these situations affected workers, investors, and others?
Approximately 25 percent of the U.S. labor force was unemployed. Many people could not afford to satisfy even their basic needs.

**Economic Activity**

**Recovery**

Economic downturns do not go on forever. A welcome phase of the business cycle, known as recovery, begins to appear. **Recovery** is the phase in which unemployment begins to decrease, demand for goods and services increases, and GDP begins to rise again.

People gain employment. Consumers regain confidence about their futures and begin buying again. Recovery may be slow or fast. As it continues, the nation moves back into prosperity.

**CONSUMER PRICES**

Have you ever noticed that packages of some items get smaller while the price stays the same? Have you bought new technology products that are less expensive than earlier ones? These are examples of changes in the buying power of your money.

**Inflation**

A problem with which most nations have to cope is inflation. **Inflation** is an increase in the general level of prices. In times of inflation, the buying power of the dollar decreases. For example, if prices increased 5 percent during the last year, items that cost $100 then would now cost $105. This means it now takes more money to buy the same amount of goods and services.

Inflation is most harmful to people living on fixed incomes. Due to inflation, retired people and others whose incomes do not change are able to afford fewer goods and services.

**Causes of Inflation**

One type of inflation occurs when the demand for goods and services is greater than the supply. When a large supply of money, earned or borrowed, is spent for goods that are in short supply, prices increase.

Even though wages (the price paid for labor) tend to increase during inflation, prices of goods and services usually rise so fast that the wage earner never seems to catch up.

Most people think inflation is harmful. Consumers have to pay higher prices for the things they buy. Therefore, as
workers, they have to earn more money to maintain the same standard of living. Producers may receive higher prices for the goods and services they sell. If wages go up faster than prices, businesses tend to hire fewer workers and so unemployment worsens.

**Measuring Inflation**

Inflation rates vary. During the late 1950s and early 1960s, the annual inflation rate in the United States was in the 1 to 3 percent range. During the late 1970s and early 1980s, the cost of living increased 10 to 12 percent annually.

Mild inflation (perhaps 2 or 3 percent a year) can actually stimulate economic growth. During a mildly inflationary period, wages often rise more slowly than the prices of products. The prices of the products sold are high in relation to the cost of labor. The producer makes higher profits and tends to expand production and hire more people. The newly employed workers increase spending, and the total demand in an economy increases.

In the United States, one of the most watched measures of inflation is called the Consumer Price Index (CPI). A price index is a number that compares prices in one year with some earlier base year. There are different types of price indexes.

Inflation rates can be deceptive since the Consumer Price Index is based on a group of selected items. Many people face hidden inflation since they may not buy the exact items used to calculate the index. The cost of necessities (food, gas, health care) may increase faster than non-essential items, which could be dropping in price. This results in a reported inflation rate much lower than the actual cost-of-living increase being experienced by consumers.

**Deflation**

The opposite of inflation is called deflation. Deflation means a decrease in the general level of prices. It usually occurs in periods of recession and depression. Prices of products are lower, but people have less money to buy them.

Significant deflation occurred in the United States during the Great Depression of the 1930s. Between 1929 and 1933, prices declined about 25 percent.

**INTEREST RATES**

In simple terms, interest rates represent the cost of money. Like everything else, money has a price. Interest rates have a strong influence on business activities. Companies and governments that borrow money are affected by interest rates. Higher interest rates mean higher business costs.

As a consumer, you are affected by interest rates. The earnings you receive
CHAPTER 2 Economic Activity

Interest rates influence many aspects of our economy. In your group, look over the seven “Types of Interest Rates” discussed. Then, prepare a description of who in our economy would be most likely to be affected by each of these types of interest rates.

as a saver or an investor reflect current interest rates. Consumers also borrow. People with poor credit ratings pay a higher interest rate than people with good credit ratings.

Types of Interest Rates
Many types of interest rates exist in every economy. These rates represent the cost of money for different groups in different settings. Some of these types of interest rates include the following:

• The prime rate is the rate banks make available to their best business customers, such as large corporations.
• The discount rate is the rate financial institutions are charged to borrow funds from Federal Reserve banks.
• The T-bill rate is the yield on short-term (13-week) U.S. government debt obligations.
• The mortgage rate is the amount individuals pay to borrow for the purchase of a new home.
• The corporate bond rate is the cost of borrowing for large U.S. corporations.
• The certificate of deposit rate is the rate for six-month time deposits at savings institutions.

Changing Interest Rates
Each day, the cost of money (interest) changes because of various factors. The supply and demand for money is the major influence on the level of interest rates. As amounts saved increase, interest rates tend to decline. This occurs since more funds are available. When borrowing by consumers, businesses, and government increases, interest rates are likely to rise.

Work as a Group

Interest rates influence many aspects of our economy. In your group, look over the seven “Types of Interest Rates” discussed. Then, prepare a description of who in our economy would be most likely to be affected by each of these types of interest rates.

as a saver or an investor reflect current interest rates. Consumers also borrow. People with poor credit ratings pay a higher interest rate than people with good credit ratings.

Types of Interest Rates
Many types of interest rates exist in every economy. These rates represent the cost of money for different groups in different settings. Some of these types of interest rates include the following:

• The prime rate is the rate banks make available to their best business customers, such as large corporations.
• The discount rate is the rate financial institutions are charged to borrow funds from Federal Reserve banks.
• The T-bill rate is the yield on short-term (13-week) U.S. government debt obligations.
• The mortgage rate is the amount individuals pay to borrow for the purchase of a new home.
• The corporate bond rate is the cost of borrowing for large U.S. corporations.
• The certificate of deposit rate is the rate for six-month time deposits at savings institutions.

Changing Interest Rates
Each day, the cost of money (interest) changes because of various factors. The supply and demand for money is the major influence on the level of interest rates. As amounts saved increase, interest rates tend to decline. This occurs since more funds are available. When borrowing by consumers, businesses, and government increases, interest rates are likely to rise.

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As you pay for your purchase with U.S. dollars, you receive some coins as change. While these coins are the size you expect, something is different. You look at the coins and notice these are not U.S. quarters, dimes, and nickels. What’s the deal with this?

While the U.S. dollar is the official currency of Ecuador, the country does not have enough U.S. coins to handle the many business transactions. Paper currency was abundant. In fact, over 60 percent of all U.S. paper money is in circulation outside the United States. Coins, though, were in short supply. Due to this shortage, Ecuador had to create its own coins with a similar shape but a different design.

In the late 1990s, Ecuador faced many economic difficulties including high inflation, increased poverty, and a declining value of the sucre (its previous currency). Actions to address these concerns included adoption of the U.S. dollar.

When doing business in Ecuador, you will be expected to wear conservative clothing for business settings. You are likely to greet others with a handshake. As you get to know your business contacts, an embrace is likely; women may give “air” kisses on both cheeks.

Business meetings will likely start with an exchange of pleasantries. The importance of family in Ecuador is often reflected in these conversations. Avoid discussion of politics and the country’s relations with Peru.

You will be expected to be on time for a business meeting, but don’t expect it to start on time. For social gatherings, plan to arrive approximately 30 minutes after the appointed time. Lunch is usually taken between 1 p.m. and 2 p.m. For dinner invitations, prepare to eat as late as 11 p.m.

A local agent for selling goods and services is vital. This representative is necessary to do business with the Ecuadorian government. The use of a local attorney will ease the difficulty of maneuvering the country’s complex legal system.

**Think Critically**

1. What are benefits and possible disadvantages of a country using the U.S. dollar as its official currency?
2. How do business customs in Ecuador differ from others with which you are familiar?
3. Conduct library or Internet research to obtain additional information about business activities and economic conditions in Ecuador.
INVESTMENT ACTIVITIES

Investing for the future can happen in several ways. Your time in school is an investment for your future. When companies buy buildings and equipment, they are also investing in their future.

*Capital spending* refers to money spent by a business for an item that will be used over a long period. *Capital projects* involve spending by businesses for items such as land, buildings, equipment, and new products. The money for capital projects comes from three main sources: personal savings, stock investments, and bonds.

**Personal Savings**

A major source of investment funds is personal savings. Companies use money you deposit in a bank or other financial institution. These funds provide the money necessary for buying expensive equipment or creating new products. In return, savers are paid interest on the money they deposit.

The savings rate of a country is an important factor for economic growth. In recent years, the personal savings rate of the United States has been quite low,

Focus on Real Life

You can’t expect to have enough money for a large purchase in the future if you always spend everything you receive. Too many people never learn this simple rule. Today’s savings makes tomorrow’s economic growth possible.

Governments, businesses, and consumers each must learn to save and invest for their futures. Government needs to have funds available for needed services desired by citizens. Companies must obtain equipment and other productive resources for a profitable future. Individuals must make choices that balance current spending with future financial security.
often below one percent. This situation can cause economic concerns in the future.

The Stock Market
Corporations are a major type of business organization. Many people invest by becoming part owners of a corporation. Stock represents ownership in a corporation. Stock ownership is commonly called equity. This term means “ownership.”

The value of shares of stock is affected by many factors. Once again, supply and demand are the major influences. If a company has higher earnings, more people will want to buy its stock. This causes the value to increase.

The Bond Market
Another investment activity involves the sale of bonds. A bond represents debt for an organization.

If you purchase a corporate or government bond, you are a creditor. This means you have lent money to the organization. In return, bondholders are paid interest for the use of their money.

Borrowing
“Buy now, pay later” commonly occurs in most economies of the world. Borrowing by governments, businesses, and consumers can have an important economic influence.

Government Debt
People expect services from federal, state, and local governments. Those services cost money. Often, government uses borrowing to finance various projects. New schools, public buildings, highways, and parks are often financed by borrowing.

E-Commerce in Action
Global Online Activities
Quite often, a manager may be asked, “In how many countries does your company do business?” In the past, the response was most likely a number or a list of countries. Today, the answer will more likely be: “In every country that has Internet access!”

Technology allows firms to buy, sell, and exchange information around the world in just a few minutes.

While e-commerce within the United States continues to grow, online exporting activities have even greater potential. Federal and state governments help promote international trade by providing information and web sites for locating foreign customers.

In the past, many companies did not face international competition. Now these organizations must be concerned that customers with Internet access can easily locate and purchase products from around the world. For example, at one time, publishers in Germany, France, and several other European nations could legally dictate retail book prices—both in stores and online. Today, online shoppers seek out more competitive prices elsewhere. A German consumer might buy a book online, but instead of using the online company Amazon’s German web site, he may find a better deal through Amazon’s United Kingdom site.

Think Critically
1. What types of global business activities are faster and easier because of technology?
2. Locate an Internet site that buys and sells online. What special information is available for international customers? Does the company have separate web sites for customers in other countries?
A government may spend less than it takes in. When this occurs, a **budget surplus** is the result. If a surplus exists, government may reduce taxes or increase spending on various programs.

In contrast, a government may spend more than it takes in. This situation is called a **budget deficit**. Over time, deficits build up. The total amount owed by the federal government is called the **national debt**.

**Business Debt**

Loans, bonds, and mortgages are common borrowing methods used by businesses. Most companies, large and small, use debt at some time.

Efficient use of borrowing can be helpful to companies. Using the funds of others can help expand sales and profits. Sometimes, when poor decisions are made, debt creates problems. Poor debt management can result in a company going out of business.

**Consumer Debt**

People commonly use credit cards, auto loans, and home mortgages to finance their purchases. The use of credit can be convenient. Often, overuse of credit results in financial difficulties for individuals and families.

Careful use of credit can be important for economic growth. In contrast, unwise borrowing can result in legal action and other trouble.

**FUTURE ECONOMIC CHALLENGES**

The ability of an economy to produce output determines its growth. The private enterprise system in the United States has worked quite well. Government leaders and citizens know that it can be made to work even better as they

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**Work as a Group**

Getting involved in economic and social issues is a vital role for citizens. In your group, select a current topic that needs attention. Prepare a list of actions that government, businesses, and consumers might take to address this concern.
strive to develop new technologies and find solutions for economic problems.

Various economic problems exist that need to be solved. Many people do not have access to adequate health care. Some people do not have proper housing, especially in large cities. Traffic and crime are also matters of concern for many. Too many workers are unemployed or do not have appropriate employment.

No one knows for sure what the future economic situation will be. In order to maintain or increase a country’s standard of living and to prevent unemployment from rising, economic growth is needed. Economic growth is important because it provides jobs and allows people an opportunity to better meet their needs and wants.

**CHECKPOINT**

What are future economic concerns for a country’s economy?

What do you think is the biggest economic problem to be solved?

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**Assessment**

**>> Key Concepts**

Determine the best answer.

1. Equity refers to
   a. reduced spending by government
   b. ownership in a company or other asset
   c. borrowing to finance a capital project
   d. increased government taxes

2. Which of the following would most likely cause a budget surplus for government?
   a. higher spending
   b. lower spending
   c. higher borrowing
   d. lower taxes

**>> Make Academic Connections**

3. **Economics** Taxes are a necessity. They provide necessary money for government services. What types of taxes do you believe would be best for a society?

4. **Social Issues** How might the future economic concerns of other countries differ from those of the United States?
Measuring Economic Activity

1. Gross domestic product (GDP) is the total dollar value of all final goods and services produced in a country during one year. GDP per capita is calculated by dividing GDP by the total population.

2. There are several economic measures of labor. The labor force of an economy consists of all people above age 16 who are actively working or seeking work. The unemployment rate is the portion of people in the labor force who are not working. People are considered to be unemployed if they are looking for work and willing to work but unable to find a job.

Productivity is the production output in relation to a unit of input, such as a worker.

3. There are several economic indicators for consumer spending. Personal income refers to salaries and wages as well as investment income and government payments to individuals. Retail sales measures the sales of durable and nondurable goods bought by consumers.

Economic Conditions Change

4. The movement of the economy from good times to bad and back again is called a business cycle. A business cycle has four phases: prosperity, recession, depression, and recovery.

5. Inflation is a general rise in the level of prices. Inflation can occur when the demand for goods and services is greater than the supply. Deflation is a decrease in the general price level. Deflation can occur when prices of products are lower, but people have less money to buy them.

6. Interest rates represent the cost of money. The level of interest rates in an economy is affected by the supply and demand for money. Interest rates affect both consumer and business activities.

Other Measures of Business Activity

7. Investment activities that promote economic growth involve personal savings, buying stock as ownership in a corporation, and purchasing bonds from businesses and government.

8. Governments, businesses, and consumers commonly use borrowing to finance various purchases. Careful borrowing can be important for economic growth. In contrast, unwise borrowing can result in legal action and other problems.

9. Economic growth in the future will require consideration of various issues related to unemployment, housing, traffic, and crime. Economic growth is important because it provides jobs and allows people an opportunity to better meet their needs and wants.

Communicate Business Concepts

1. “GDP is the best measurement of a country’s economy.” Explain whether you agree or disagree with this statement.

2. The GDP of Country A is $400,000. The GDP of Country B is $800,000. Does this mean that the per capita output of Country B is about twice that of Country A? Explain.

3. Name three factors that can contribute to increased output of goods and services in a country. Explain how these factors can improve productivity.

4. What is the effect of increased productivity on a country’s leisure time? How might increased productivity affect career opportunities?

5. Retail sales is a measure of durable and nondurable goods bought by consumers. What are some examples of durable and nondurable goods?

6. Suppose that many auto and steel plants close in a country. Thousands of workers lose their jobs in a short period. If the country has been enjoying prosperous times, it may now be
headed into what phase of the business cycle? Describe other conditions that might begin to occur.

7. What actions might be taken by businesses and government in each phase of the business cycle? Describe the present U.S. economy and identify the current phase of the business cycle.

8. Why is a high rate of inflation generally considered harmful to an economy?

9. Other than the economic indicators discussed in this chapter, what are some other data items that might be used to measure business and economic activities?

10. What are some economic concerns that may need to be addressed in the future?

>> Develop Your Business Language

Match the terms listed with the definitions.

11. A decrease in the general price level.

12. The movement of an economy from one condition to another and back again.

13. Spending by businesses for items such as land, buildings, and equipment.

14. The total value of all final goods and services produced in a country in one year.

15. Government spends less than it takes in.

16. A phase marked by a long period of high unemployment, weak consumer sales, and business failures.

17. Represents debt for an organization.

18. Salaries and wages as well as investment income and government payments to individuals.

19. The GDP divided by the total population of a country.

20. Production output in relation to a unit of input, such as a worker.

21. The phase in which unemployment decreases, demand for goods and services increases, and GDP begins to rise.

22. An increase in the general price level.

23. Represents ownership in a corporation.

24. Government spends more than it takes in.

25. The portion of people in the labor force who are not working.

26. The sales of durable and nondurable goods bought by consumers.

27. A period in which unemployment is low, businesses produce many goods and services, and wages are good.

28. A number that compares prices in one year with some earlier base year.

29. A period in which demand, production, and GDP growth decrease and unemployment begins to rise.

30. The total amount owed by the federal government.

Key Terms

a. bond
b. budget deficit
c. budget surplus
d. business cycle
e. capital project
f. deflation
g. depression
h. gross domestic product (GDP)
i. GDP per capita
j. inflation
k. national debt
l. personal income
m. price index
n. productivity
o. prosperity
p. recession
q. recovery
r. retail sales
s. stock
t. unemployment rate
>> Decision-Making Strategies

In determining GDP, only final goods and services are included. This avoids having some items counted more than once. For example, a mining company sells iron ore to a steel-producing firm. That firm sells the steel to an auto manufacturer who uses it to produce a car. The iron ore, converted to steel, is counted once—in the price paid for the car, the final product. Read carefully the following list of goods and services produced in our economy and then answer the questions.

a. Electric toaster oven bought as a gift
b. Telephone service installed in a government office
c. Fiberglass sold to a company for use in making boats
d. Grooming services for your pet
e. Paper sold to a newspaper publishing company
f. Computer paid for by a city government
g. Computer bought for your family’s use
h. Broccoli bought by a food-processing firm

31. Which of these items should be listed as a good and counted in GDP? Give reasons for your answer.
32. Which of these items should be listed as a service and counted in GDP? Give reasons for your answer.

>> Make Academic Connections

33. TECHNOLOGY Describe ways in which computers and other technology might affect a country's GDP.

34. RESEARCH Conduct research on the “Index of Leading Economic Indicators.” Prepare a short written or oral summary to explain what this index involves.

35. GEOGRAPHY Select five countries. Create a map showing various economic statistics for each country. Explain reasons for differences among the countries.

36. SCIENCE Technology is often the basis for increased productivity. Prepare a poster or other visual presentation to demonstrate how the use of computers or other technology might make workers more productive.

37. CULTURE How might culture affect opportunities to increase productivity in different countries? Describe cultural and political factors that may enhance or limit actions to increase productivity.

38. MATH Productivity for a small country was 25 units per worker hour in 1997. Productivity increased 20 percent between 1997 and 2002. What was the productivity figure for 2002? If the rate of increase is maintained, what will the figure be in 2007? In 2012?

39. MATH Workers are paid a rate of $0.30 per unit. Using productivity figures from the previous question, determine how much workers earned per hour in 2002. If their rate increases to $0.35 in 2007 and $0.40 in 2012, how much would they earn per hour in those years?

40. HISTORY Research various phases of the business cycle in the United States over the past 200 years. Create a graph showing the ups and downs of the economy. What conclusions could be drawn from this research?

41. COMMUNICATION Prepare a visual presentation to report (a) reasons government, businesses, and consumers borrow, and (b) potential problems that could occur for each group if credit is not used properly.

42. LAW What are some of the legal concerns that can result from unwise use of credit by businesses and consumers?

43. ECONOMICS Compare the use of stocks and bonds by companies to raise funds. Describe situations in which each would be most effective.

44. COMMUNICATION Select two interest rates from the list in the chapter. Create a chart showing these rates for the past four or five years. Explain possible reasons for changes in these rates.
> > Portfolio Activity

To provide tangible evidence of your learning, do the following:

**COLLECT** current data for one of the economic indicators discussed in this chapter such as GDP, unemployment, consumer prices, or interest rates.

**CREATE** a graph with visuals to communicate: (1) the data trend over the past three or four years, and (2) people and businesses affected by this data (use photos or other graphics).

**CONNECT** your visual presentation to other learning in this class or relate it to information from other classes. Prepare a short summary of the causes and possible effects of this data.

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**Emerging Business Issues Event**

This team event (two or three members) challenges FBLA members to develop and demonstrate research and presentation skills for an emerging business issue. Your team must research one of the following emerging business issues. Your research should find affirmative and negative arguments for each topic.

- Changing the federal income tax to a federal sales tax
- Strengthening the economy with tax refunds
- Alternative plans for Social Security
- Changing careers in a highly productive economy
- Providing more people with health insurance

Fifteen minutes before your presentation, you will draw to determine whether you will present an affirmative or negative argument for your emerging business issue. Any presentation that lasts more than five minutes will receive a five-point deduction. Following each oral presentation, the judges have five minutes to ask questions.

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**Performance Indicators Evaluated**

- Understand the given emerging business issue.
- Present a relevant affirmative or negative argument for the topic.
- Conduct research to support your argument with relevant quality evidence.
- Demonstrate persuasive speaking and oral presentation skills.
- Involve all team members in the research and presentation.

*For more detailed information about performance indicators, go to the FBLA web site.*

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**Think Critically**

1. Why must entrepreneurs pay attention to emerging business issues?
2. List two advantages and two disadvantages for changing federal income tax to federal sales tax.
3. Why is health care such a hot topic during an election year?
4. How has a productive economy influenced the types of jobs available to Americans?
5. How can young people successfully prepare for future careers when considering outsourcing of manufacturing and production jobs?

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http://www.fbla-pbl.org/
Chapter 3

Business in the Global Economy

3-1 International Business Basics
3-2 The Global Marketplace
3-3 International Business Organizations
Global business creates many employment opportunities. Jobs could include directing foreign sales, negotiating with foreign distribution centers, arranging shipping, and planning conversion of products from American to foreign specifications. While the skills necessary to perform these tasks are increasingly important, job titles often will not reflect them directly because the people will also have duties unrelated to importing and exporting. Transportation managers, for example, oversee both foreign and domestic shipping, including settlements between shippers. U.S. Customs Service agents investigate persons, common carriers, and merchandise arriving in or departing from the United States to prevent prohibited importing or exporting.

**Employment Outlook**
- Strong growth is expected for interpreters and translators.
- Employment of inspectors and compliance officers is not usually affected by economic fluctuations. Recently, increased security concerns have expanded demand for federal, state, and local government examiners.
- Continued growth of many international business positions is expected as companies expand global operations.

**Job Titles**
- Customs Inspector
- Interpreter/Translator
- Global Purchasing Manager
- Transportation/Freight Inspector
- Cross-cultural Trainer
- International Sales Representative

**Needed Skills**
- Foreign language skills, cultural awareness, and knowledge of geography provide the foundation for most international business work.
- Many international business positions require knowledge in a field such as accounting, marketing, finance, or information technology.

**What’s it like to work in... International Business**

“I’m sorry, your shipment is being held at the Port of Hong Kong until the proper documentation is prepared.”

These are words no exporter wants to hear. Companies such as M.E. Day exist to help exporters avoid these types of situations. The main service provided by companies such as this freight forwarder is to ship goods to customers in other countries. M.E. Day also helps international companies by knowing export regulations, comparing costs for various shipping methods, and moving goods through the customs process.

M.E. Day serves as a customs broker, helping international companies pass inspections when goods enter another country. Custom brokers also prepare needed documents and make sure the required tariffs are paid.

**What about you?** What are some aspects of international business that you might find of interest in the future?
International Business Basics

**Goals**
- Describe importing and exporting activities.
- Compare balance of trade and balance of payments.
- List factors that affect the value of global currencies.

**Key Terms**
- imports
- exports
- balance of trade
- balance of payments
- exchange rate

**Focus on Real Life**

What did you and your family have for breakfast this morning? Coffee, cereal, and sliced bananas, perhaps? If it were not for trading with Brazil for coffee and with Honduras for the bananas, you might have had only cereal. The sugar on your table may have come from the Philippines. Even your morning newspaper was printed on paper that may have come from Canada.

As you look around your home, you will find many products made in other countries. For example, you may find a TV made in Japan or Korea, a stereo made in Taiwan or China, clothing made in the Philippines or Honduras, kitchen appliances made in Hong Kong or Malaysia, and coffee from Brazil or Colombia. Look around your classroom. Can you identify products made in other countries?

**TRADING AMONG NATIONS**

Most business activities occur within a country’s own borders. *Domestic business* is the making, buying, and selling of goods and services within a country. *International business* refers to business activities needed for creating, shipping, and selling goods and services across national borders. International business is frequently referred to as *foreign* or *world trade*. Evidence of foreign trade is everywhere.

While the United States has many natural resources, a skilled labor force, and modern production facilities, not everything can be provided. Companies and consumers go beyond the U.S. borders to obtain many things. The United States conducts trade with over 180 countries.

In the past, economies were viewed in terms of national borders. With international trade expanding every day, these boundaries are no longer fully valid in defining economies. Countries are interdependent and so are their economies. Consumers have come to expect goods and services from around the world.
Absolute Advantage
Two economic principles define buying and selling among companies in different countries. *Absolute advantage* exists when a country can produce a good or service at a lower cost than other countries. This may result from an abundance of natural resources or raw materials in a country. For example, some South American countries have an absolute advantage in coffee production, and Saudi Arabia has an absolute advantage in oil production.

Comparative Advantage
A country may have an absolute advantage in more than one area. If so, it must decide how to maximize its economic wealth. A country may be able to produce both computers and clothing better than other countries. The world market for computers might be stronger than the market for clothing. This means it would be better for the country to produce computers but to buy clothing from other countries. *Comparative advantage* is a situation in which a country specializes in the production of a good or service at which it is relatively more efficient.

Importing
*Imports* are items bought from other countries. Did you know that imports account for the total supply of bananas, coffee, cocoa, spices, tea, silk, and crude rubber in the United States? The U.S. buys about half of its crude oil and fish from other countries. Imports also account for 20 to 50 percent of the supply of carpets, sugar, leather gloves, dishes, and sewing machines. U.S. companies must import tin, chrome, manganese, nickel, copper, zinc, and several other metals to manufacture certain goods. Figure 3-1 shows how dependent the United States is on imported raw materials.

Without foreign trade, many things you buy would cost more or not be available. Other countries can produce some goods at a lower cost because they have the needed raw materials or have lower labor costs. Some consumers purchase foreign goods, even at higher prices, if they perceive the quality to be better than domestic goods. They may simply enjoy owning products made in other countries. French perfumes, Norwegian sweaters, and Swiss watches are examples.
Exporting

Goods and services sold to other countries are called **exports**. Just as imports benefit you, exports benefit consumers in other countries. Workers throughout the world use factory and farm machinery made in the United States. They eat food made from U.S. agricultural products and use chemicals, fertilizers, medicines, and plastics from the United States. People in other countries like to view U.S. movies. They also watch CNN and ESPN. They read books, magazines, and newspapers published by U.S. companies. The goods and services exported by the United States create many jobs. One of every six jobs in the United States depends on international business. Figure 3-2 shows U.S. balance of trade with various nations.

**MEASURING TRADE RELATIONS**

A major reason people work is to earn money to buy things. First, they sell their labor for wages. They then spend the major part of those wages for goods and services. People usually try to keep their income and spending in balance. They know that if they spend more than they earn, they can experience financial problems. Nations are also concerned about balancing income with expenditures. When people buy more than their income allows, they go into debt. In the same way, when a country has an unfavorable balance of trade it owes money to others. **Foreign debt** is the amount a country owes to other countries.

**U.S. Trade Balances**

<table>
<thead>
<tr>
<th>Goods Exported (in billions)</th>
<th>Goods Imported (in billions)</th>
<th>U.S. Trade Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,018.6</td>
<td>1,507.9</td>
<td>-489.3</td>
</tr>
<tr>
<td>169.8</td>
<td>224.2</td>
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</tr>
<tr>
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</tr>
<tr>
<td>17.5</td>
<td>31.6</td>
<td>-14.1</td>
</tr>
<tr>
<td>28.4</td>
<td>152.4</td>
<td>-124</td>
</tr>
<tr>
<td>150.5</td>
<td>244.8</td>
<td>-94.3</td>
</tr>
</tbody>
</table>

**Balance of Trade**

The difference between a country’s total exports and total imports is called the **balance of trade**. If a country exports (sells) more than it imports (buys), it has a **trade surplus**. Its trade position is said to be favorable. If it imports more than it exports, it has a **trade deficit** and its trade position is unfavorable.

A country can have a trade surplus with one country and a trade deficit with another. Overall, a country tries to keep its international trade in balance. Figure 3-3 shows why it is better to export more than you import.
3-3 on page 56 shows the two possible trade positions. After a long history of a favorable balance of trade, the U.S. has had a trade deficit in recent years.

**Balance of Payments**

In addition to exporting and importing goods and services, other forms of exchange take place among nations. Money goes from one country to another through investments and tourism. A citizen of one country might invest in a corporation in another country. A business may invest in a factory in another country. One government might give financial or military aid to another nation. Banks may deposit funds in foreign banks.

When tourists travel, they add to the flow of money from their country to the country they are visiting. Some countries limit the amount of money their citizens can take out of the country when they travel.

The *balance of payments* is the difference between the amount of money that comes into a country and the amount that goes out of it. A *positive* or *favorable* balance of payments occurs when a nation receives more money in a year than it pays out. A *negative* balance of payments is *unfavorable*. It is the result of a country sending more money out than it brings in.

A country attempts to have a favorable balance of payments. Create a list of actions a nation might take to improve its trade relations with other countries.

**CHECKPOINT**

**How does balance of trade differ from balance of payments?**

**A Question of Ethics**

**Bribery and Gift Giving**

In the United States, it is considered unethical for a businessperson to pay bribes to government officials or to other businesspersons in exchange for favorable treatment, such as the awarding of well-paid contracts. In fact, it is against the law, whether the recipient is an American or someone in another country. The Foreign Corrupt Business Practices Act of 1977 outlawed the payment of bribes by Americans to foreign officials, companies, or individuals. At times, not doing so may put U.S. businesses at a competitive disadvantage. In some countries, paying and accepting bribes of various sorts is common, even expected. As more countries recognize how harmful bribes are to economic progress, the practice is ending.

While it is relatively easy to outlaw bribes, it is much harder to define and identify what is a bribe and what is a gift given as a token of appreciation. Gift giving among businesspeople is relatively limited and infrequent in the United States and Canada. In other cultures, it is very common and regarded as entirely appropriate. Many organizations have policies that limit the monetary value and type of gifts that are acceptable. Policing intent is much more difficult because it is highly subjective. A social dinner invitation is usually meant to influence the recipient’s behavior, even if in a subtle way.

**Think Critically**

1. How can U.S. businesspeople handle situations in foreign countries where officials expect bribes to be paid as a condition for doing business there?
2. Suppose you work for a manufacturing company. A plastics supplier who is trying to get more business sends you a case of golf balls made with one of its high-tech composite materials. What would you do?
INTERNATIONAL CURRENCY

One challenge faced by businesses involved in international trade is the various currencies used around the world. Nations have their own banking system and money. For instance, Russia uses the ruble; the European Union, the euro; Brazil, the real; India, the rupee; and Saudi Arabia, the riyal.

Foreign Exchange Rates

The process of exchanging one currency for another occurs in the foreign exchange market, which consists of banks that buy and sell different currencies. Most large banks provide currency services for businesses and consumers. The exchange rate is the value of a currency in one country compared with the value in another. Supply and demand affects the value of currency. The approximate values of various currencies on a recent date in relation to the U.S. dollar (USD) are given in Figure 3-4.

Travelers and businesspeople must deal with currency exchanges as they go from one country to another. Travelers in another country can go to a currency exchange window at the airport, train station, or local bank and buy any amount of local currency they want. The amount of local currency they receive depends on the value of the two currencies at that time. Rates are posted at exchange windows, and there is a charge made for exchanging currency.

Factors Affecting Currency Values

Three main factors affect currency exchange rates among countries: the country’s balance of payments, economic conditions, and political stability.

Balance of Payments When a country has a favorable balance of payments, the value of its currency is

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**Figure 3-4**

Which currency is worth the most in terms of U.S. dollars?

<table>
<thead>
<tr>
<th>Country</th>
<th>Currency</th>
<th>Units per USD*</th>
<th>Value in USD*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Britain</td>
<td>pound</td>
<td>0.55 pounds</td>
<td>1.82</td>
</tr>
<tr>
<td>Brazil</td>
<td>real</td>
<td>3.15 reals</td>
<td>0.32</td>
</tr>
<tr>
<td>Canada</td>
<td>dollar</td>
<td>1.36 Canadian dollars</td>
<td>0.73</td>
</tr>
<tr>
<td>European Union</td>
<td>euro</td>
<td>0.83 euro</td>
<td>1.20</td>
</tr>
<tr>
<td>Japan</td>
<td>yen</td>
<td>110.1 yen</td>
<td>0.009</td>
</tr>
<tr>
<td>Saudi Arabia</td>
<td>riyal</td>
<td>3.75 riyals</td>
<td>0.27</td>
</tr>
<tr>
<td>South Africa</td>
<td>rand</td>
<td>6.49 rands</td>
<td>0.154</td>
</tr>
<tr>
<td>South Korea</td>
<td>won</td>
<td>11162.79 won</td>
<td>0.00086</td>
</tr>
<tr>
<td>Venezuela</td>
<td>bolivar</td>
<td>1923 bolivars</td>
<td>0.00052</td>
</tr>
</tbody>
</table>

* United States Dollar

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*Do you think different colors are helpful to distinguish currency?*
usually constant or rising. An increased demand for both the nation’s products and its currency causes this situation. When a nation has an unfavorable balance of payments, its currency usually declines in value.

**Economic Conditions** When prices increase and the buying power of the country’s money declines, its currency will not be as appealing. Inflation reduces the buying power of a currency. High inflation in Brazil, for example, would reduce the demand for the real.

*Interest rates* are the cost of using someone else’s money. These rates can affect the value of a country’s currency. Higher interest rates usually create lower consumer demand. This often results in a reduced demand for a nation’s currency, causing a decline in its value.

**Political Stability** Companies and individuals want to avoid risk when they do business in other nations. If a government changes suddenly, this may create an unfriendly setting for foreign business. A company could lose its building, equipment, or money on deposit in banks.

Political instability may also occur when new laws are put in place. These laws may not allow foreign businesses to operate as freely as they did under the old laws. Uncertainty in a country reduces the confidence that businesspeople have in its currency.

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**FYI**

The U.S. dollar is the official currency of Ecuador, El Salvador, and Panama. A country may adopt a “dollarization” policy in an attempt to reduce economic troubles and enhance trade with other nations. The dollar is also the unofficial monetary unit for tourist transactions in countries such as the Bahamas and Haiti.

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**CHECKPOINT**

What factors affect the value of a country’s currency?

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**Assessment**

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**Key Concepts**

Determine the best answer.

1. Which of the following would be an example of international business?
   a. A farmer in Iowa using U.S. produced equipment
   b. A sales staff in South Carolina representing a foreign producer
   c. A restaurant in Chicago offering Asian menu items
   d. A retail store in Oregon selling craft items from local artists

2. When a country’s imports exceed its exports, this is a trade
   a. surplus
   b. deficit
   c. exchange
   d. balance

3. The value of a country’s currency is likely to decline as a result of
   a. higher inflation
   b. lower interest rates
   c. a trade surplus
   d. a favorable balance of payments

**Make Academic Connections**

4. Culture While business knowledge is important, often cultural awareness in foreign markets is even more important. Talk to someone who has lived in or visited another country. Obtain information about cultural factors that affect business activities in that country.

5. Technology Explain how the Internet and other technology helps to expand international trade and global business activities.
The International Business Environment

Doing business in other countries requires knowledge of the differences that exist among people and places. As shown in Figure 3-5, businesses must consider four main factors—geography, cultural influences, economic development, and political and legal concerns.

### Geography
The location, climate, terrain, seaports, and natural resources of a country influence business activity. Very hot weather will limit the types of crops that can be grown. A nation with many rivers or ocean seaports can easily ship products for foreign trade. Countries with few natural resources must depend on imports.

### Cultural Influences
In some societies, hugging is an appropriate business greeting. In other societies, a handshake is the custom. These differences represent different cultures. *Culture* is the accepted behaviors, customs, and values of a society. A society’s culture has a strong influence on business activities. In Mexico, many businesses close in the afternoon by tradition while people enjoy lunch and a siesta (relaxing rest period).

The main cultural and social factors that affect international business are language, religion, values, customs, and social relationships. These relationships include interactions among families, labor unions, and other organizations.

### Economic Development
Every country and every individual faces the problem of limited resources to satisfy needs and wants. You continually make decisions about the use of your time, money, and energy. In a similar way, every country plans the use of its land, natural resources, workers, and wealth to best serve the needs of its people.

In some countries, people travel on a high-speed bullet train to manage a

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**Focus on Real Life**

Clear and complete exchange of ideas among international business partners is vital. A U.S. retail company contracted with a foreign shirt maker to make men’s shirts. The contract stated that the shirts must be made of 60 percent cotton and 40 percent polyester. While the manufacturer supplied shirt labels to that effect, the actual shirts were 35 percent cotton and 65 percent polyester.

Without verifying the material content, the U.S. company accepted the shirts. It sold them with the incorrect information on the label. The Federal Trade Commission fined the company for deceptive labeling.
computer network in a high-rise building. In other countries, people go by oxcart to a grass hut to operate a hand loom to make cloth for people in their village. These differences in living and work environments reflect the level of economic development. The key effects on a country’s level of economic development are:

- **Literacy Level** Countries with better education systems usually provide more and better goods and services for their citizens.

- **Technology** Automated production, distribution, and communications systems allow companies to create and deliver goods, services, and ideas quickly.

- **Agricultural Dependency** An economy that is largely involved in agriculture does not have the manufacturing base to provide citizens with great quantity and high quality of a product.

Another factor that supports international trade in industrialized countries is **infrastructure**. Infrastructure refers to a nation’s transportation, communication, and utility systems. A country such as Germany—with its efficient rail system, high-speed highways, and computers—is better prepared for international business activities than other nations with a weaker infrastructure.

### Political and Legal Concerns

Each day you come upon examples of government influence on business. Governments regulate fair advertising and enforce contracts. They require safety inspections of foods and medications. People in the United States have a great deal of freedom in their business activities. This is not true in all countries of the world. In many places, the activities of consumers and business operators are restricted. The most common political and legal factors that affect international business activities include the type of government, the stability of the government, and government policies toward business.

#### Work as a Group

Knowledge of the international business environment is important for all global activities. In your group, create a list of items for each of the following categories: geography, cultural influences, economic development, and political–legal concerns. Explain how these items could affect a company when doing business in another country.
INTERNATIONAL TRADE BARRIERS

Government actions can create **trade barriers**, which are restrictions to free trade. These political actions are **formal** trade barriers. Three common formal trade barriers are quotas, tariffs, and embargoes.

In contrast, the culture, traditions, and religion of a country can create **informal** trade barriers. These situations are not based on formal government actions but they do restrict trade.

**Quotas**

To regulate international trade, governments set a limit on the quantity of a product that may be imported or exported within a given period. This limit is called a **quota**.

Quotas may be set for many reasons. Countries that export oil may put quotas on crude oil so that the supply will remain low and prices will stay at a certain level. Quotas may be set on imports from another country to express displeasure at the policies of that country.

Quotas can also be set by a country to protect one of its industries from too much competition from abroad. This often is done by a nation to shield its “infant industries,” which need protection to get started. In the past, the United States government has imposed quotas on sugar, cattle, dairy products, and textiles.

**Tariffs**

Another device that governments use to control international trade is the **tariff**. A tariff is a tax that a government places on certain imported products. Suppose you want to buy an imported bicycle. The producer charges $140, but the government collects a 20 percent tariff ($28) on the bicycle when it is imported. Therefore, you will have to pay $168 plus shipping charges for the bike. The increased price may cause you to decide to buy a U.S. manufactured bike at a lower price.

Some tariffs are a set amount per pound, gallon, or other unit, while others are figured on the value of the good, as in the example of the bicycle. A tariff increases the price for an imported product. A high tariff tends to lower the demand for the product and reduce the quantity of that import. Many people believe that tariffs should be used to
protect U.S. jobs from foreign competition.

**Embargoes**

If a government wishes to do so, it can stop the export or import of a product completely. This action is called an **embargo**. Governments may impose an embargo for many reasons. They may wish to protect their own industries from international competition more than either the quota or the tariff will achieve. The government may wish to prevent sensitive products, especially those vital to the nation’s defense, from falling into the hands of unfriendly groups or nations. A government sometimes imposes an embargo to express its disapproval of the actions or policies of another country.

**ENCOURAGING INTERNATIONAL TRADE**

Specific actions by governments can promote international business activities. Governments view exporting as an effective way to create jobs and foster economic prosperity. Common efforts to encourage international trade include free-trade zones, free-trade agreements, and common markets.

**Free-Trade Zones**

To promote international business, governments often create free-trade zones in their countries. A **free-trade zone** is a selected area where products can be imported duty-free and then stored, assembled, and/or used in manufacturing. A free-trade zone is usually located around a seaport or airport. The importer pays duty only when the product leaves the zone.

**CHECKPOINT**

What are three formal trade barriers?

**Foreign Language Translation**

While on the job at an exporting company, you receive a phone call from a customer in Kenya. Unable to understand the caller’s language, you switch on the language translation service. This software allows you to understand, in your language, the product questions of your customer.

Computerized translators recognize speech in one language and convert the spoken words into another language. In a language translation system, three components work together—speech recognition, machine translation, and speech synthesis. The computer recognizes words spoken in the first language and converts them into a computer-readable file. Then, the words are translated into the second language. Finally, a voice synthesizer “speaks” the translated version.

Today, translation technology exists for all commonly used international business languages, such as Arabic, Chinese, English, French, German, Italian, Japanese, Korean, Portuguese, Russian, Spanish, and Vietnamese. In addition, hand-held, low-cost electronic language translators are available for use by businesspeople, travelers, and students.

These technologies allow you to say, “I would like to register for the conference” to a person who only speaks German. Then, using language translation technology, a German businessperson will hear, “Ich möchte für die Konferenz registrieren.”

**Think Critically**

1. What are possible benefits and drawbacks of computerized language translators?
2. Conduct a Web search to obtain information about the latest technologies for foreign language translation systems.
Free-Trade Agreements
Many countries set up free-trade agreements with other nations. Under a free-trade agreement, member countries agree to remove duties and trade barriers on products traded among them. This results in increased trade between the members. For example, the United States, Canada, and Mexico created the North American Free Trade Agreement (NAFTA) in 1993. This pact does away with taxes on goods traded among the three countries and eases the movement of goods. NAFTA is designed to enlarge the markets and economic bases of the countries involved.

Common Markets
In a common market, members do away with duties and other trade barriers. They allow companies to invest freely in each member’s country. They allow workers to move freely across borders. A common market is also called an economic community. Common market members have a common external duty on products being imported from nonmember countries. Examples of common markets include the European Union (EU) and the Latin American Integration Association (LAIA). The goals are to expand trade among member nations and promote regional economic integration.

Assessment

3-2

3-2

Assessment

>> Key Concepts
Determine the best answer.

1. True or False. Infrastructure is a significant factor that affects the economic development of a country.
2. True or False. An informal trade barrier is created by government actions.
3. Religion is an element of the _?_ component of the international business environment.
   a. geographic  
   b. economic  
   c. cultural  
   d. political
4. A country that wishes to enhance international trade activities would most likely use
   a. a tariff  
   b. a common market  
   c. an embargo  
   d. a quota

>> Make Academic Connections

5. Law Use the Internet to locate information about laws in foreign countries that are different from those in the United States.
6. Geography Using library resources or the Internet, obtain copies of maps for various geographic regions. On your map, indicate how the terrain, climate, and waterways might influence international trade activities. Present a 1-2 minute summary of your findings.
7. History Conduct research on the history of a common market such as the EU or the LAIA. Describe some of the benefits the community provides to its member nations.
MULTINATIONAL COMPANIES

A multinational company (MNC) is an organization that does business in several countries. MNCs usually consist of a parent company in a home country and divisions or separate companies in one or more host countries. The country in which the MNC places business activities is called the host country.

MNC Strategies

Multinational corporations can use either a global or multinational strategy. A global strategy uses the same product and marketing strategy worldwide. The same product is sold in essentially the same manner throughout the world. One example with which you are probably familiar is Coca-Cola.

A multinational strategy treats each country market differently. Firms develop products and marketing strategies that adapt to the customs, tastes, and buying habits of a distinct national market. Many restaurant chains employ a multinational strategy when they modify their menus to local tastes.

Focus on Real Life

Before taking a new course of action, Ghana, located on the west coast of Africa, had many economic problems. Inflation was 120 percent. Exports had declined by 50 percent. The nation had a crumbling infrastructure. An overvalued currency did not promote widespread exporting of cocoa, Ghana’s main export. Between 1983 and 1990, the cedi decreased from 2.75 per U.S. dollar to 350 per U.S. dollar.

Ghana obtained suggestions from the International Monetary Fund. The actions that were implemented, along with lower tax rates, helped to improve the country’s balance of payments and stimulate economic growth.

Key Terms

- multinational company (MNC)
- joint venture
Drawbacks of Multi-national Companies

An MNC can become a major economic power in a host country. The workers of the host country may depend on the MNC for jobs. Consumers become dependent upon it for goods and services. The MNC may actually influence or control the political power of the country.

GLOBAL MARKET ENTRY MODES

As companies expand into other countries, several methods are available for their use.

Licensing

Some companies want to produce items in other countries without being actively involved. They may allow a foreign company to use a procedure they own. Licensing is selling the right to use some intangible property (production process, trademark, or brand name) for a fee or royalty.

The Gerber Company started selling its baby food products in Japan by means of licensing. The use of television characters or sports team emblems on hats, shirts, jackets, notebooks, luggage, and other items also involves a licensing agreement. Licensing has a low financial investment, so the potential financial return is often low. The risk for the company is also low.

Franchising

Another method often used to expand into other countries is the franchise. A franchise is the right to use a company name or business process in a specific way. Organizations enter into contracts
with people in other countries to set up a business that looks and runs like the parent company. The company obtaining the franchise will usually adapt a range of business elements. Marketing elements such as food products, packaging, and advertising messages must meet both cultural sensitivities and legal requirements.

Both franchising and licensing involve a royalty payment for the right to use a process or company name. Licensing usually involves a manufacturing process. Franchising commonly involves selling a product or service. Franchise agreements are popular with fast-food companies. McDonald’s, Burger King, Wendy’s, KFC, and Pizza Hut all have used franchising to increase their presence in foreign markets.

Joint Venture
Business partnerships can provide benefits to all parties involved. One type of global partnership is the joint venture. The joint venture is an agreement between two or more companies to share a business project.

The main benefit of a joint venture is the sharing of raw materials, shipping facilities, management activities, or production facilities. Concerns of this business agreement include sharing of profits and not as much control since several companies are involved.

This arrangement is very popular for manufacturing. Joint ventures between Japanese and U.S. automobile manufacturers have been common. For example, the Ford Motor Company entered a joint venture with Mazda Motor Corporation. Ford used Mazda-produced parts for several of its cars. Mazda set up assembly plants for Ford Motor vehicles.

INTERNATIONAL TRADE ORGANIZATIONS
International business activities can be very complex. As a result, several organizations have been created to help companies with global trade activities.

World Trade Organization
The World Trade Organization (WTO) was created in 1995 to promote trade around the world. With over 150 member countries, WTO settles trade disputes and enforces free-trade agreements between its members. Other goals of WTO include the following.

- Lowering tariffs that discourage free trade
- Eliminating import quotas
- Reducing barriers for banks, insurance companies, and other financial services
- Assisting poor countries with economic growth

International Monetary Fund
The International Monetary Fund (IMF), with over 150 member nations, helps to promote economic cooperation. It maintains an orderly system of world trade and exchange rates. The IMF was established in 1946 when the economic interdependence among nations was growing at a greater pace than ever before in history.

F Y I
Cereal Partners Worldwide (CPW) is a joint venture between General Mills and Nestle to sell cereal in Latin America, Europe, the Middle East, and other areas of the world. General Mills brought popular products, such as Cheerios, Lucky Charms, and Trix, into the partnership. Nestle, well known all over the world, has a broad distribution system and a well-known brand in most foreign countries.

> Describe activities of international trade organizations and agencies.

C H E C K P O I N T
How does licensing differ from a franchise?
Before the International Monetary Fund, a country could often change the value of its legal tender to attract more foreign customers. As other countries lose business, they may impose trade restrictions or lower the value of their currency. As one nation tries to outdo another, a trade war may result. Today, cooperation among IMF nations makes trade wars less likely.

World Bank
The International Bank for Reconstruction and Development is commonly called the World Bank. It was created in 1944 to provide loans for rebuilding after World War II. Today, the bank’s key function is to give economic aid to less developed countries. These funds build communications systems, transportation networks, and energy plants.

The World Bank, with over 180 member countries, has two main divisions: the International Development Association and the International Finance Corporation. The International Development Association (IDA) makes loans to help developing countries. The International Finance Corporation (IFC) provides capital and technical help to private businesses in nations with limited resources. The IFC promotes joint ventures between foreign companies and local companies to further capital investment in the developing nation.
The Hunger Site

Each day, over 1,000 tons of edible food is thrown away in the United States. Elsewhere, several million people go hungry. Around the world, over 20,000 people die every day from hunger-related causes. But what can one person do to solve this problem?

Tim Kunin and Greg Hesterberg decided to take action with The Hunger Site (www.thehunger-site.com). On average, over 220,000 people from around the world visit the website each day to click the “Give Free Food” button and help feed the hungry.

Kunin and Hesterberg launched The Hunger Site in June 1999. The Hunger Site focuses the power of the Internet on a specific charitable cause: the elimination of world hunger. Since it started, over 200 million visitors have given more than 300 million cups of staple food to the hungry all over the world. Site sponsors pay for the staple food, distributed to those in need by Mercy Corps and America’s Second Harvest.

When visitors to The Hunger Site homepage click on the “Give Free Food” button, they view sponsor banner ads on the “Thank You” page. Money from banner advertising fees goes to the charity partners. Funds are divided among the organizations to help hungry people in over 74 countries. Included are those in Africa, Asia, Eastern Europe, the Middle East, Latin America, and North America. Tim and Greg, long-time friends and social activists, are committed to using this online effort to end world hunger.

Sponsors on The Hunger Site benefit in several ways. First, they are able to reach well-educated, upper-income consumers who are a desired target audience for many goods and services. Also, advertising on The Hunger Site creates goodwill. Consumers usually appreciate a company’s support of a cause they care about. Sponsorship builds customer loyalty. Research shows that over three-fourths of adults are more likely to buy a product linked with a cause they care about. Over half would be willing to pay more for the product if it benefits a social cause in which they believe.

Think Critically
1. Locate another web site that promotes and attempts to solve a social concern of society. How successful do you believe this effort will be?
2. Plan a web site that might be used to help solve a concern of society.
> > Business Notes

3-1 International Business Basics

1. Domestic business is the making, buying, and selling of goods and services within a country. International business refers to the business activities needed for creating, shipping, and selling goods and services across national borders.

2. A country is said to have an absolute advantage when it can produce a good or service at a lower cost than other countries. If a country specializes in the production of a good or service at which it is more efficient, it is said to have a comparative advantage.

3. Imports are items bought from other countries. Exports are goods and services sold to other countries. Nations do business with each other to increase the variety of goods and services available to their consumers.

4. Balance of trade is the difference between a country’s exports and imports. The difference between a country’s total payments to other countries and its total receipts from other countries is the balance of payments.

5. The exchange rate is the value of a currency in one country compared with the value of a currency in another country.

6. The value of global currencies is affected by three main factors: balance of payments, economic conditions, and political stability.

3-2 The Global Marketplace

7. The international business environment involves four main components: geography, cultural influences, economic development, and political and legal concerns.

8. Three formal barriers to international trade are quotas, tariffs, and embargoes. A quota is a limit set on the quantity of a product that may be imported or exported within a given period. A tariff is a tax placed on certain imported products. An embargo stops the import or export of a product completely.

9. Actions to encourage international trade include free-trade zones, free-trade agreements, and common markets.

3-3 International Business Organizations

10. Multinational companies conduct business activities in several countries and have management capable of doing business worldwide.

11. Common methods used for global business include licensing, franchising, and joint ventures.

12. The World Trade Organization was created to promote trade around the world. The International Monetary Fund helps to promote economic cooperation by maintaining a system of world trade and exchange rates. The World Bank provides economic assistance to less developed countries.

> > Communicate Business Concepts

1. Describe how an absolute advantage might affect a country’s imports and exports.

2. Explain why it is difficult for a community or a nation to be completely independent.

3. How does international business contribute to a better standard of living for many people in various countries?

4. What are some attitudes and behaviors that might make it difficult for a foreign-based company to do business in the United States?
5. For the following situations, decide whether this is an example of an informal or formal trade barrier.
   a. Law requiring that stores be closed on Sunday
   b. Beliefs about not eating certain foods
   c. Special tax on the sale of books
   d. Required nutritional information on food packaging
   e. Hiring family members when jobs are available in an organization

6. Describe situations in which a joint venture would benefit a company involved in international business.

7. A country sometimes uses high tariffs to protect its new and developing industries. What are two examples of new and developing industries either in the United States or in other countries? Do you think that such industries should be protected by high tariffs? If so, how long should they be protected?

8. Some people believe that the United States should place stiff controls on imports of goods that compete with U.S. businesses to prevent the “exporting of American jobs” to other countries. Give arguments for and against such a position.

>> Develop Your Business Language

Match the terms listed with the definitions.

9. Goods and services sold to another country.
10. A limit on the quantity of a product that may be imported and exported within a given period.
11. Government restrictions to reduce free trade.
12. An organization that conducts business in several countries.
13. The value of money of one country expressed in terms of the money of another country.
14. Goods and services bought from another country.
15. Stopping the importing or exporting of a certain product or service.
16. An agreement between two or more companies from different countries to share a business project.
17. The difference between a country’s total exports and total imports of goods.
18. A tax that a government places on certain imported products.
19. The difference between a country’s total payments to other countries and its total receipts from other countries.
20. A nation’s transportation, communication, and utility systems.

Key Terms
a. balance of payments
b. balance of trade
c. embargo
d. exchange rate
e. exports
f. imports
g. infrastructure
h. joint venture
i. multinational company (MNC)
j. quota
k. tariff
l. trade barrier
**Decision-Making Strategies**

Assume you have started a business that manufactures electric toasters that you want to sell to the people of China.

21. What are some potential difficulties that you might encounter when doing business in the Chinese market?

22. What actions could your company take to help improve your opportunities for success?

**Make Academic Connections**

23. **GEOGRAPHY** Locate examples of multinational companies in different countries. Create a map showing where the companies are based and the other nations in which the companies operate.

24. **ECONOMICS** Go to the web site of an economic community (common market) or a regional trade organization. Make a list of the countries involved and describe some of the organization’s activities.

25. **HISTORY** Conduct research on the history of money systems that have been used in other countries. Find examples of the use of a country’s currency in another country.

26. **MUSIC** Very often, the music of a country reflects its history, culture, and religion. Find examples of music from other nations that reflect the past and current culture. What aspects of the music are distinctive to that country?

27. **METRIC CONVERSION** To make their exports suitable for use in other countries, U.S. manufacturers must produce goods that are measured in the metric system. For example, if a manufacturer wanted to export paint, which is sold in gallons in this country, it would probably export the paint in 4-liter cans (about 11.4 gallons). To what sizes would the items listed be converted for export to countries using the metric system? (See Appendix D.)
   a. A quart bottle of liquid detergent
   b. A 50-yard bolt of fabric
   c. An automobile engine measured in cubic inches
   d. A 12-inch ruler
   e. A bathroom scale that measures in pounds

28. **TECHNOLOGY** Using a spreadsheet program, create a table and graph to report the changing value of the U.S. dollar compared with currencies of three other countries.

29. **MATH** Using the information in Figure 3-4 on page 58, determine how many U.S. dollars someone could buy for these amounts of currencies from other countries.
   a. In Japan, 1200 yen
   b. In Canada, 5 Canadian dollars
   c. In Saudi Arabia, 150 riyals

30. **CAREER PLANNING** Investigate what types of legal agreements a person would encounter when applying for a job to work for a multinational company in another country.

**Linking School and Home**

Conduct a survey of clothing labels in your home. Examine 10 or more labels and create a list of the countries in which these items were manufactured. Prepare a summary with the following information:

Which countries are most often on your list?

Are there several countries from the same geographic region?

What are some possible similarities among these countries?

What are possible economic advantages of these countries involved in clothing manufacturing?
**Portfolio Activity**

To provide tangible evidence of your learning about international business, do the following:

**COLLECT** an example of a package for a food item from another country. These are usually available in the ethnic section of a supermarket or at an ethnic grocery store.

**CREATE** a visual to identify the following information about your package:

- Country of origin for the product
- Main exports and imports of the country
- Cultural factors that influence the design and information on the package
- Unusual aspects about the product ingredients or flavor
- Characteristics of the likely consumers who buy this item

**CONNECT** your visual to other items already in your class portfolio, or relate the visual to an important concept you learned in another class. Prepare a one-paragraph summary of how international business links to another topic you have studied in this class or other classes.

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**Desktop Publishing Event**

You and a partner have been hired to create, design, and produce a business publication using desktop publishing software. You have two hours of class time to prepare a newsletter that focuses attention on *International Business Basics*, *The Global Marketplace*, and *Organization for International Business*. Your team is allowed to use two computers, a scanner, and/or clip art. No other equipment may be used. The finished product may be submitted in black and white or in color on plain paper. Word division manuals and dictionaries may be used as reference materials. The second part of this competition includes a one-hour written objective test to determine your knowledge of desktop publishing; the score received on this portion of the event will equal 15 percent of the final event score.

**Performance Indicators Evaluated**

- Understand graphics, text creation, layout, creativity, and selection of appropriate fonts and type sizes for desktop publishing.
- Prepare an interesting newsletter about international business.
- Incorporate graphics and layout that is pleasing to the reader.
- Incorporate correct punctuation, grammar, and sentence structure.
- Illustrate creativity throughout the publication.

For more detailed information about performance indicators, go to the FBLA web site.

**Think Critically**

1. What is the difference between an average publication and a great publication?
2. What strategies can be used to make a publication more reader-friendly?
3. Who should be considered when producing a publication?
4. Give two examples of items that are distracting on publications.

http://www.fbla-pbl.org/
Chapter 4

Social Responsibility of Business and Government

4-1 Social Responsibility
4-2 Government Protection Activities
4-3 Government Regulation and Assistance
Planning a Career in...
Government

Accountants, interviewers, restaurant inspectors, and engineers are just a few of the many employment opportunities in government. Federal, state, and local agencies employ more than 18 million people. As you can see, government is a major employer in the U.S. economy.

About 60 percent of federal workers hold managerial, business, financial, and professional positions. While some government jobs require training similar to that of business workers, other positions demand training that is more specialized. Food production regulators and homeland security officials need academic and practical experiences related to their fields.

Employment Outlook
• Increased job opportunity in some federal agencies is being offset by slow growth and declines in other federal sectors.
• Despite increased demand for services from state and local governments, employment levels will be affected by economic conditions and the availability of tax revenues.
• Staffing of government positions is directly affected by budget levels approved by legislative bodies and local governing boards.

Job Titles
• Purchasing Agent
• Conservation Scientist
• Correctional Officer
• Firefighter
• Highway Maintenance Engineer
• Municipal Clerk
• Registered Nurse
• Revenue Agent
• Social Worker
• Urban Planner
• Job Placement Counselor

Needed Skills
• A college education is vital for many government jobs.
• Specialized training and field experience will vary depending on the occupational field in which you desire to work. Elected government positions will require skills in communication, campaigning, and fund-raising, along with organizing and motivating staff.

What's it like to work in...
Government

Kathleen leaves her part-time job as a dental hygienist a few minutes early so she can quickly eat dinner before going to her medical training course. As an emergency medical technician (EMT) for the local fire department, she has many responsibilities.

On a typical 12-hour shift, she might be called to a major auto accident or a home fire. Other times at the station are spent cleaning, maintaining, and repairing medical equipment and firefighting vehicles. On days when supplies arrive, Kathleen coordinates the check-in and storage of several hundred items that might be needed in a medical emergency.

Kathleen’s training courses not only upgrade her skills, but also keep her informed of the latest medical technology. While her days are long and stressful, the satisfaction of EMT work and firefighting duties provide Kathleen with a very rewarding career choice.

What about you? What are some government jobs that you might interest you?
**SOCIAL RESPONSIBILITY ISSUES**

**Social responsibility** refers to the duty of a business to contribute to the well-being of a community. In considering its responsibility to society, a business must weigh the interests and concerns of many groups. A broadened social responsibility of business calls for more attention to social concern. This includes protection of the environment, minorities and women in the workplace, employment of the physically challenged and older workers, and a healthy and safe work environment.

**Environmental Protection**

*Conservation* is saving scarce natural resources. It is a goal of many companies. For example, lumber companies that consume trees have reforestation programs. Some natural resources cannot be replaced. A **non-renewable resource** is a natural resource that cannot be replaced when used up. Examples are gas, oil, and minerals, such as copper and iron ore.

*Pollution* occurs when the environment is tainted with the by-products of human actions. Some production methods cause pollution of lakes, rivers, and...
and air. A socially responsible business takes action to improve or change operations that cause pollution. Engineers design new equipment for reducing pollution.

The federal government has set measurable standards for water and air quality. The Environmental Protection Agency (EPA) monitors and enforces those standards. Businesses and the EPA work closely together to reduce pollution. They try to make the environment healthier.

**Workplace Diversity**

Businesses are more and more sensitive to the role of women, ethnic groups, the physically challenged, and older workers. The workforce of a business should reflect the range of groups in a community. Members of these groups must have equal access to education, training, jobs, and career advancement. The major challenge facing businesses today involves learning how to manage a workforce made up of the diverse cultures in society.

Another issue involves the removal of employment barriers for women. Employers are not allowed to exclude women applicants from a physically demanding job unless the business can prove the job requires physical skills that women do not have.

Employers also have taken steps to accommodate individuals who are physically challenged. The Americans with Disabilities Act (ADA), along with other federal and state legislation, has caused major improvements to be made toward accommodating workers who are physically challenged. Buildings must have access for wheelchairs. People with sight or hearing limitations must be accommodated on the job.

Other laws have been passed to eliminate bias against older workers. The passage of the Age Discrimination in Employment Act bars employers from using age as a basis for employment decisions (hiring, promotions, or termination from a job). The law protects all persons aged 40 and older.

**Job Safety**

Having a safe place in which to work is important to all employees. They should be able to work in an office or factory free from the risks that could cause accidents. The work environment should provide full protection from fire and other hazards. In addition to protection from physical harm, workers need to know how to manage the unexpected. Safety also involves employee training in how to work safely and what to do in case of an emergency.

To ensure the right to safety, most employers have put a variety of programs into practice to protect workers. Federal and state governments have also passed laws to make the workplace safer. Safety standards are regulated and enforced by agencies such as OSHA, the Occupational Safety and Health Administration.

**FYI**

Company safety programs often reward employees with cash bonuses, prizes, or additional vacation days for ideas that improve the safety of the workplace.
Employee Wellness
A healthy workforce is a productive workforce. Workers who have good physical health are valuable assets. Businesses today do a number of things to improve the health of their workforce. Among programs offered are stop-smoking seminars, counseling for employees with drug problems, and weight-loss sessions.

Your general well-being as an employee needs to be protected, too. Clauses that relate to employee well-being are often included in labor contracts and company policy manuals. These clauses are conditions of work that pertain to the health and safety of employees while on the job.

Companies have a number of programs to promote good health. Seminars on eating a balanced diet, getting proper exercise, and maintaining a healthy lifestyle are a few examples. Some businesses sponsor sports teams and encourage employees to take part.

Social Responsibility Evaluation
Socially responsible actions can cause controversy. While a number of benefits exist, these actions also have various costs.

Benefits
Common benefits of socially responsible activities include the following:

• Expanded justice for groups of a society
• Enhanced company image
• Reduced need for government actions
• Improved quality of life in a community and around the world
• Increased awareness of social issues among workers, consumers, and others

Costs
There are costs involved when a business takes socially responsible actions. Money must be spent for new non-polluting or safer equipment, for building repairs to remove risks, for wellness and rehabilitation programs, and for social projects sponsored by a company.

A business must make a profit to stay open. If a business does not earn a profit, the business will close and employees will be laid off. Spending on social programs must be at a suitable level so a business can still earn a reasonable profit.

Checkpoint
What are four areas of social responsibility that may require the attention of business?

Checkpoint
What are the main benefits of social responsibility?
BUSINESS ETHICS
A socially responsible business engages in ethical business practices. Ethics are principles of morality or rules of conduct. Business ethics are rules about how businesses and their employees ought to behave. Ethical behavior involves conforming to these rules. Unethical behavior violates them. In dealing with business ethics, a code of ethics can help a business identify proper employee behavior.

Code of Ethics
A code of ethics is a set of rules for guiding the actions of employees or members of an organization. Codes of ethics address topics such as confidentiality of business information. Figure 4-1 shows a statement of values, called “Blue Box Values,” that guide the ethical conduct of employees at the American Express Company, a large U.S. corporation.

A code must be worded in terms of acceptable behavior rather than forbidden action. Even with a code of ethics, the choice of proper behavior can cause dilemmas for decision-makers within a business. Here are some examples of ethical dilemmas.

• Should a company expand into a profitable market in another country where doing business requires giving expensive gifts to key government officials?

• Should a company continue to produce a popular product after it discovers a minor defect in it?

Ethical Conduct Guidelines
The ethical conduct of a business is greatly determined by its top management. Executives who show strong moral character and make ethical business decisions set the ethical standards for a business.

Work as a Group
Using the three ethical guidelines on page 80, select a situation in a work setting that might be considered unethical. As a group, use these three questions to assess the ethical aspects of the situation.

Companies concerned about ethical behavior in their employees have set up educational programs on ethical conduct. These programs are designed to promote employee honesty and integrity. Program topics range from making personal phone calls during work hours to taking supplies for personal use (stealing). Employees are also

AMERICAN EXPRESS BLUE BOX VALUES

All our activities and decisions must be based on, and guided by, these values.

■ Placing the interests of clients and customers first.

■ A continuous quest for quality in everything we do.

■ Treating our people with respect and dignity.

■ Conduct that reflects the highest standards of integrity.

■ Teamwork—from the smallest unit to the enterprise as a whole.

■ Being good citizens in the communities in which we live and work

To the extent we act according to these values, we believe we will provide outstanding service to our clients and customers, earn a leadership position in our businesses and provide a superior return to our shareholders.

Figure 4-1
Do you think a code of ethics can increase a business’ profits? How?
trained on how to make ethical decisions on the job.

When considering the ethics of business situations, you could follow these guidelines.

1. Is the action legal?
2. Does the action violate professional or company standards?
3. Who is affected by the action and how?

A common concern in ethical decision-making involves a conflict of interest. This can occur when an action by a company or individual results in an unfair benefit. For example, it would be a conflict of interest if a person serving on a board of directors required that the company buy items only from businesses that he owns or controls.

**CHECKPOINT**

What is the purpose of a code of ethics?

What are some costs to society of unethical behavior?

**4-1**

**Assessment**

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**Key Concepts**

Determine the best answer.

1. An example of a non-renewable resource would be
   a. solar energy
   b. gold
   c. agricultural products
   d. a library book

2. The Americans with Disabilities Act (ADA) requires that a company
   a. provide training to people with disabilities
   b. find ways to help workers who are physically challenged
   c. hire a certain number of people with special needs
   d. adapt products manufactured for special-needs customers

3. A code of ethics is designed to
   a. meet government regulations
   b. reduce operating costs of a company
   c. provide guidelines for proper behavior
   d. improve employee productivity

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**Make Academic Connections**

4. **Science** List a variety of natural resources and agricultural products used in the production of goods and services. What actions might be taken by companies to improve the efficient use of these resources?

5. **Technology** Search the Internet to locate an example of a code of ethics. Describe the benefits of this code of ethics for the organization.
Sharpen Your **Life Skills**

**Working in Teams**

Each day, thousands of workers make decisions and apply business actions in team settings. The ability to work in a team is rated by most employers as one of the most important career skills. The combined skills of the people in a team are greater than that of individuals working alone. When working in a team in class or on the job, consider the following.

- Be prepared for minor conflicts in the first phase of a team project. Differences in opinions will surface. Be ready to adapt to the personalities, behaviors, and actions of others.
- Agree upon guidelines for project goals, meeting times, location, agenda, missed meetings, conflict resolution, and other procedures.
- Define leadership and other roles. Some team members will keep notes and bring needed materials. Others will conduct research or create visuals for a presentation.
- Determine methods for decision-making. Usually this will be done based on agreement among team members after discussion of various issues and opposing points of view.
- Keep focused on your goals. Avoid being distracted by minor issues and personality conflicts. Maintain a team-oriented environment by saying “we, us, ours;” not “I, me, my, mine.”
- Be courteous to others. Respect differences in opinions, personalities, and decision-making styles.

Working in teams is something you are likely to do throughout your life. These experiences can be enjoyable and productive. Members of effective teams take responsibility for its work and take pride in its accomplishments. Some team projects will be frustrating. It is important to maintain a positive attitude. Some of the best learning and most valuable experiences result from encounters with others with different backgrounds and diverse points of view.

**Think Critically**

1. What do you like about working in teams? Are there any aspects about working in teams that you dislike?
2. Describe a problem that might occur when working in teams. Explain how this situation might be resolved.
Government plays a role in all economic systems. Your role as a citizen and voter has an effect on the decisions and actions taken by government. In a private enterprise system, government’s role is much less extensive than in other economic systems. It is still a vital one. The role of government in the economy often changes as newly elected officials take office.

**Roles of Government**

As issues facing society change, so must government change. There are some basic roles of government. Government is mainly concerned with these roles:

- Providing services for members of society
- Protecting citizens, consumers, businesses, and workers
- Regulating utilities and promoting competition
- Providing information and support to businesses
- Buying goods and services
- Hiring public employees
- Raising revenue

Each of these roles has either a direct or indirect impact on business expansion, consumer affairs, and economic growth in the economy.

**GOVERNMENT IN SOCIETY**

Brenda Hiam was driving to school when, all of a sudden, a crack in the road caused her car to swerve and hit a bump. While there was no obvious damage to the vehicle, this was a disturbing event.

At this point, Brenda wanted to contact a government agency to notify them of this potentially dangerous driving hazard. She asked her friend, Kevin, if she should contact the city, county, state, or federal highway department.

“That depends if the road is a city, county, state, or federal highway,” he answered.

“Well, this might not be as easy as I thought,” said Brenda in a confused tone.
GOVERNMENT PROTECTION ACTIVITIES

Government protects your rights in a number of ways. Citizens are protected through police and firefighting services. The armed forces provides for national defense. National security is a chief concern of the federal government.

Worker Protection

Laws have been established to help provide a safe work environment. As a worker, you have a basic right to safe working conditions. Safety standards for buildings, machines, and chemicals are set by government agencies. Government inspection and regulation of work areas help reduce the number of job-related accidents.

More government regulations result from the need to protect the basic human rights of workers. For example, you cannot be denied work because of your race, religion, sex, or age. Selection of someone for a job must be based on job requirements, training, and experience. Prejudices and personal biases must not affect a hiring decision.

Contract Enforcement

Contracts are another example of government protection. A contract is an agreement to exchange goods or services for something of value, usually money. It is a basic part of doing business. A contract may be written or unwritten. Certain elements must be

FYI

Reading and understanding a contract must be done before signing it. Your court system does not protect you from your own lack of common sense.
Describe types of intellectual property.

Contract Basics

Valid, enforceable contracts must contain:

- **Agreement**: An offer must be made, and an acceptance must occur.
- **Competent Parties**: Those entering into the contract must be of legal age and must be mentally competent.
- **Consideration**: Something of measurable value must be exchanged by the parties involved.
- **Legality**: The contract must be for a product or service that may be legally sold; also, no fraud or deception exists in the agreement.

Included for the contract to be enforceable. Figure 4-2 highlights the main provisions of every enforceable contract.

These four elements—agreement, competent parties, consideration, and legality—are the basis for many legal disputes. An item seen as having different values (consideration) by different people can result in a legal dispute. Examples of contracts include a lease to rent an apartment, a credit card agreement, and documents that state the terms of a purchase.

Both consumers and businesses benefit from government enforcement of contracts. If you agree to have repairs made on your car for $65, the business firm must do the work as agreed upon. You must pay for the work when it is finished. If work is not done correctly or if you fail to pay, legal action can be taken to force the work to be corrected or force you to pay. Without enforcement, dishonest consumers or business owners could refuse to honor their agreements. Daily business activities would be very difficult.

PROTECTION OF INTELLECTUAL PROPERTY

Intellectual property is purely intangible with no physical characteristics—a person cannot touch it. Intellectual property includes patents, copyrights, and trademarks.

**Patents**

When individuals or companies create new products, they may obtain a patent. A **patent** gives the inventor the sole right to make, use, or sell the item for 17 years. A company that creates a new means to record programs from television could get a patent for this process. It would prevent other companies from making or selling recorders using this process.

Work as a Group

Intellectual properties are also called intangible assets. In your group, prepare a list of various patents, copyrights, and trademarks owned by companies and nonprofit organizations. Explain how these assets contribute to the success of the organization. Why is protection of intellectual property important?
Copyrighst
A copyright protects the creative work of authors, composers, and artists. Copyright protection lasts for the life of the person receiving the copyright. It also extends for 50 years after the person’s death. Examples of copyright statements can be found on the front pages of most books. Copyrights are identified with the symbol ©.

Trademarks
A trademark is a word, letter, or symbol linked with a specific company or product. Businesses register company names, team emblems, and label designs with the government. A trademark can be very valuable. Many are famous all over the world and often identified with a symbol, called a logo. Can you think of some logos that you see frequently?

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**4-2 Assessment**

**Key Concepts**

Determine the best answer.

1. True or False. International trade with other countries is the responsibility of state and local governments.
2. True or False. An oral contract can be legally binding.
3. Fire and police protection is the main responsibility of
   a. local government
   b. state government
   c. federal government
   d. all levels of government
4. A _?_ would protect the composer’s musical score.
   a. patent
   b. trademark
   c. copyright
   d. contract

**Make Academic Connections**

5. **Math** A city government spends $186,000 a month on public services. Of that amount, 46 percent is used for fire and police protection.
   a. How much is spent each month for fire and police protection?
   b. How much is spent each month for other services?
   c. How much is spent by the city in a year for fire and police protection?
6. **Math** In a city in which there are 90,000 employed workers, 18,000 are public employees. Of this number, the federal government employs 6,000; the state, 8,000; and the city, 4,000.
   a. What percentage of all workers are public employees?
   b. What percentage of the public employees does the federal government employ?
   c. What percentage of all employees are employees of the state government?
7. **Law** Prepare a list of possible problems that could occur in a contract situation.
One minute you see peaceful villages with carts pulled by animals. A moment later, you see busy city streets in which seven of ten Vietnamese families use a motorcycle as their main method of transportation.

Vietnam is a country of contrasts, combining traditional production methods with modern business activities. The nation is evolving from decades of strong central planning to emerging areas of capitalism.

While the country is officially atheist, the culture is significantly influenced by religion. Active religions include Buddhism, Confucianism, Taoism, Christianity, Islam, Caodaism, and Hoahaoism. These traditional values result in strong family connections. Several generations may live together in the home. Children show great respect for the elders of the family, even their older brothers and sisters.

When doing business in Vietnam, you will need to get approvals from several levels of government agencies. In recent years, the government has tried to attract foreign investment for factories, technology, and infrastructure. Making connections with government officials and joint venture partners is especially important for business success.

At the start of a meeting, the exchange of business cards occurs. Cards should be presented and received with both hands. If your card is in both English and Vietnamese, it is polite to have the Vietnamese side facing up. You may be asked how old you are. This classifies you as either older or younger than the Vietnamese person in order to determine the correct form of address.

The business meal is likely to include tea and perhaps some exotic foods. You may be served bat meat, stir-fried baby birds, dog, or snake, as well as many types of seafood. It is polite to taste and drink small amounts of all items you are offered.

The conversation will slowly lead to business negotiations. Take care to not move too quickly through the agenda since this is considered rude. Use a low-pitched voice and low-key gestures. Do not allow your hosts to see the soles of your shoes.

**Think Critically**
1. What cultural factors affect business activities in Vietnam?
2. How do business activities in Vietnam differ from other countries?
3. Conduct library or Internet research to obtain additional information about business and economic activities in Vietnam.
Business activity in the United States is structured as a private enterprise or free market system. Private organizations own the factors of production. They choose efficient methods of production in order to earn a profit. Price and output decisions are made not by the government, but by businesses and consumers acting under varying economic conditions.

Government does get involved in some areas of business activities. These include regulating utilities and preventing unfair business practices.

**Regulation of Utilities**

Most goods and services you use come from private businesses. These businesses are for the most part free of government regulation. A **public utility** is an organization that supplies a service.
or product vital to all people. These include companies that provide local telephone service, water, and electricity. A public utility is chosen to serve a community. If your city had six different electric companies, each might have its own utility poles, lines, and expensive equipment. The service you would get would be more expensive and less efficient. The extra poles and wires would create an unattractive environment.

While many utility companies are privately owned, usually government closely regulates them. The rates they can charge for things such as electricity, water, or natural gas have to be approved by government agencies. In recent years, there has been a trend toward deregulation of prices where competition can be introduced.

Prevent Unfair Business Practices
Most businesspeople are fair and honest. A few may try to take advantage of their customers or competitors.

Government attempts to promote fair competition. If a company charges different prices to different people for the same product, it is treating its customers unfairly. If one business receives lower rates for the same quality and quantity of supplies that other businesses receive, it has an advantage. Such action may result in unfair competition.

A monopoly exists when a business has control of the market for a product or service. A public utility monopoly may benefit consumers by making sure they receive a needed service at a fair price. Other monopolies may not be good for the economy. If the same company owned all food stores in your city, consumers might not be treated fairly. This business could charge high prices and sell poor-quality products. When competition is present, consumers get the best values at the fairest prices.

One government action meant to promote competition and fairness and to avoid monopolies was the passage of antitrust laws. Antitrust laws prevent other unfair business practices such as false advertising, deceptive pricing, and misleading labeling. Each of these unfair practices hurts competition and reduces consumer choice.

GOVERNMENT ASSISTS BUSINESS
Government helps businesses by collecting and reporting valuable information. Data gathered by the government can help with planning. Information about incomes, prices, worker availability, and business failures can help a businessperson make wiser choices. For example, census information can help a business decide
where a majority of potential customers live. The Bureau of Labor Statistics, the Department of Agriculture, and the Department of Commerce are a few of the government agencies that provide information.

New businesses can obtain government loans to help them get started. The federal government, through the Small Business Administration (SBA), is a key source of business loans. Farmers and others may receive financial help in times of great hardship such as during a drought, flooding, or other natural disasters. Destruction of home and property by a tornado may make a person eligible for a low-interest government loan. These programs are designed to promote the financial well-being of society.

**Government Buys Goods and Services**

Government spends a great deal of money each day to buy an array of products and services. Total federal, state, and local government purchases of goods and services make up about 20 percent of all the goods and services produced in the United States.

Governments buy everything from file cabinets to buildings to military jet aircraft. In this role, government is a key economic force. Many businesses depend on government contracts for their survival. For instance, government pays businesses to construct highways and build schools.

**Government Employs Workers**

Government is the single largest employer in the U.S. economy. About one of every nine workers is a public employee. Most people think only of police officers, firefighters, and sanitation workers as government workers. Government also employs the same types of workers as private businesses.

Administrative assistants, lawyers, teachers, meat inspectors, and data analysts are all employed by government. Although the number of employees has grown slowly in recent years, good employment opportunities in government continue—in spite of efforts to eliminate or reduce the size of some agencies.

**CHECKPOINT**

How does government assist business?
GOVERNMENT RAISES MONEY

Government must have a way to raise money to fund operations and pay wages to workers. Government income is called revenue. Governments can obtain revenue through taxes and borrowing. In addition, governments can raise revenue in other ways. Fines for traffic violations and other violations of the law provide revenue for government. Fees and licenses are a source of income. Certain types of ventures require a business license. For example, insurance and real estate agents pay a fee for the privilege of running a business. Governments also charge fees for such things as driver’s licenses and fishing privileges.

Taxes

A government creates tax policies to pay for the services it provides. Taxes are levied on earnings, the value of property, and on the sale price of goods and services.

Your earnings as an individual are subject to an income tax. Income taxes are levied on the income of individuals. The individual income tax is the largest source of revenue for the federal government. Corporate income taxes also provide government revenue. The corporate income tax is based on business profits.

A major source of revenue for local governments is the real estate property tax. This tax is based on the value of land and buildings. Most property tax revenue is used to pay for schools and

E-Commerce in Action

Mass Customization

When the automobile was first mass-produced in the early 1900s, Henry Ford would tell potential customers... “you can have any color car you want as long as it’s black!” Since then, businesses have continually tried to make items that meet the distinct needs and wants of consumers.

Today, companies with millions of customers are making products designed for the individual. Consumers can buy vitamins matched to their health needs. CDs are offered with selected music tracks. Cosmetics can be mixed to match facial features and skin tone. Financial services companies offer computerized investment advice based on a person’s income, age, and household situation.

Many online companies are involved in mass customization. They provide goods and services tailored to customer demand. Dell Computer only builds personal computers that have actually been ordered. This approach keeps profit margin up by keeping inventory costs down.

Mattel allows girls to go online to design a friend for Barbie. They can choose the doll’s skin tone, eye color, hair color, clothes, accessories, and name. The doll is sent with a computer-generated paragraph about its personality.

This approach can improve customer service and add to sales. Many online merchants tailor messages and suggest purchases based on a customer profile. Previous items bought as well as interests of the buyer will promote future purchases of books, music, DVDs, clothing, and other goods and services.

Think Critically

1. Locate a web site or local business with another example of customized products or services. How does technology make this situation possible?
2. Describe an idea to offer a customized product or service online or in your community.
other local government services, such as police protection and community parks. Businesses also pay a property tax.

The cost of buying things is increased by a sales tax. A *sales tax* is a state or local tax on goods and services that is collected by the seller. If you buy a can of paint for $15.00 and the state sales tax is 6 percent, the seller collects $15.90 from you. The seller then will pay 90 cents to the state. You were the one who provided the money for the tax.

Paying taxes is a duty of citizens and businesses. You should pay your fair tax, but not more than your share. Tax laws and policies are set to make the paying of taxes fair. Whether a particular tax or tax policy is fair is always subject to debate. Businesses, in spite of public misconceptions, pay a lot of taxes to all levels of government.

**Borrowing**

Government income from taxes and other sources may not always be enough to cover the costs of providing services. Borrowing is another activity of government. When a government wants to construct a building, such as a new courthouse or convention center, the funds needed are often raised through borrowing.

Government borrows money by selling bonds. When you buy a government bond, you are helping to fund the services provided by government. Banks, insurance companies, and other financial institutions help finance governments by purchasing bonds in large numbers.

By borrowing money, the government becomes a debtor and must pay interest on its debt. Bonds issued by the U.S. government are backed by the “full faith and credit” of the federal government. Bonds issued by the federal government are considered the least risky of all debt.

**CHECKPOINT**

What is the difference between tax revenue and borrowing by government?

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**4-3**

**Assessment**

**>> Key Concepts**

Determine the best answer.

1. Antitrust laws are designed to
   a. reduce utility rates
   b. lower taxes
   c. create more jobs
   d. maintain competition

2. A(n) _?_ tax is a common source of revenue for state and local governments.
   a. sales
   b. import
   c. gift
   d. unemployment

3. True or False. A monopoly is never a benefit to consumers.

**>> Make Academic Connections**

4. **History** Conduct research about various antitrust laws. What situations caused the creation of these laws?

5. **Communication** Conduct a survey of people to obtain their opinions about which types of taxes are most appropriate to raise government revenue. Prepare a summary data table with your findings.

6. **Economics** Describe government actions to raise money that might have a positive or negative influence on business activities.
Business Notes

4-1 Social Responsibility

1. Socially responsible businesses care about their communities. They help make them better places in which to live. Social responsibility concerns relate to environmental protection, workplace diversity, safety on the job, and employee wellness.

2. Benefits of social responsibility include expanded justice for societal groups, enhanced company image, reduced need for government action, improved quality of life, and increased awareness of social issues. Costs of social responsibility are that money must be spent for new or safer equipment, for building renovations to remove hazards, for wellness and rehabilitation programs, and for social projects sponsored by a company. These costs must be balanced with profits to make sure the business stays viable.

3. A code of business ethics is a guide for behavior within an organization.

4-2 Government Protection Activities

4. The primary roles of government are to provide services to society; protect citizens, consumers, businesses, and workers; regulate utilities and promote competition; provide information and help to businesses; buy goods and services; hire public employees; and raise revenue. The levels of government are federal, state, and local.

5. Government protects citizens through police and fire services, protects consumers and business owners by enforcing contracts and intellectual property rights, and protects workers through laws that require safe working conditions.

6. The three types of intellectual property are patents, copyrights, and trademarks.

4-3 Government Regulation and Assistance


8. Government buys a wide range of goods and services and employs workers. Governments also collect and report valuable information and provide loans to help businesses get started or overcome natural disasters.

9. Governments raise needed funds through taxes and borrowing.

Communicate Business Concepts

1. What are some natural resources that you use every day? Which of those natural resources need to be protected? What can you as an individual do to avoid using up non-renewable resources?

2. Safety is often a matter of individuals being careful about where they place things and how they conduct their own business. Name some ways in which you and others can help make a workplace safe.

3. What does the term “discrimination” mean to you? What examples of discrimination in the workplace are you aware of?

4. Why do you think employers are willing to spend money to help employees improve their general health? Be specific about how a company might benefit.

5. Make a list of public utilities that serve your community.
   a. What services do they provide?
   b. Do you think it would be better for these services to be offered by several competing businesses? Explain your answer.
6. Here is a list of some of the public services provided by government. For each item, tell whether the federal, state, or local government would most likely have the responsibility for the service. (Some services may be provided by more than one level of government.)
   a. Fire protection
   b. Education
   c. Parks and recreation
   d. Water supply
   e. Highways between cities
   f. Assistance to low-income families
   g. Sewage and trash disposal
   h. Public buses
   i. Police protection
   j. Public libraries
   k. Street maintenance
   l. National defense

7. Each day people enter into many contracts, both written and unwritten.
   a. Give examples of contracts between a consumer and a business, between two businesses, and between a worker and a business.
   b. What services does government provide to enforce contracts?

8. Two students are discussing the topic “Government Is Our Biggest Business.” Dan believes that some government activities are in direct competition with private businesses. He thinks that this is unfair. He believes that government should limit its activities to those that private businesses cannot or will not take on. Brian thinks that government should undertake any business activities that it can perform better or at a lower cost than private business. What do you think? Give some examples of business activities undertaken by both private businesses and by government.

9. Why do you suppose government raises revenue through bonds that create debt and require interest payments when government could raise the revenue through an increase in taxes?

> > Develop Your Business Language

Match the terms listed with the definitions.

10. Principles of morality or rules of conduct.

11. The obligation of a business to contribute to the well-being of a community.

12. Rules about how businesses and their employees ought to behave.

13. A natural resource, such as gas, coal, copper, or iron ore, that cannot be replaced once it is used up.

14. A statement of values and rules that guides the behavior of employees or members of an organization.

15. A business that supplies a service or product vital to all people; the price charged for the service (or product) is determined by government regulation rather than by competition.

16. Laws designed to promote competition and fairness and to prevent monopolies.

17. Protection of the work of authors, composers, and artists.

18. An agreement to exchange goods or services for something of value.

19. The exclusive right given to a person to make, use, or sell an invention for a period of 17 years.

20. A word, letter, or symbol associated with a specific product or company.

21. A business that has complete control of the market for a product or service.

Key Terms

a. antitrust laws
b. business ethics
c. code of ethics
d. contract
e. copyright
f. ethics
g. monopoly
h. non-renewable resource
i. patent
j. public utility
k. social responsibility
l. trademark
Decision-Making Strategies

Centerville wants to build a new All-Sports Complex—the ASC. The ASC will be located near the center of town. It will have facilities appealing to just about every kind of person who wants to exercise or play sports. The complex will cost $250,000. There are two financing proposals:

A Issue $250,000 worth of bonds at an interest rate of 4 percent. The town will pay $10,000 per year in interest for 15 years. The total interest would be $150,000. The amount borrowed ($250,000) would have to be paid off in 15 years. Fees charged to users of the complex would pay the interest each year and the amount due bondholders ($250,000). Construction of the complex could begin right away.

B Establish a 1/4 percent city sales tax on all purchases. The revenue needed could be raised in about 5 years. There would be no user fee charged to residents of Centerville. Construction of the complex would be delayed a few years.

22. What are the advantages and disadvantages of the two proposals?

23. Which proposal do you favor, and why?

Linking School and Home

Talk to people at home and in your neighborhood about ethics. Obtain information about actions that need to be considered when hiring people, designing products, and making other business decisions. Ask them how ethics might affect their daily lives and the lives of others.
>> Portfolio Activity

To provide tangible evidence of your learning about social responsibility and government, do the following:

**COLLECT** an example of a government regulation that affects your life. This could be a food packaging label, a safety warning, a license requirement, or a government report. The example should illustrate a government activity to protect, regulate, or inform.

**CREATE** a visual to show how this government regulation affects your life and the lives of others. Use photos and other graphics to communicate the influence of this government action on consumers, workers, business, or other groups.

**CONNECT** your visual to other items already in your class portfolio or relate it to an important concept you learned in another class. Make the connection by preparing a one-minute presentation to explain the costs and benefits of this government action.

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**Community Service Project Event**

Successful businesses are actively involved in their communities. Community service projects can range from cleaning up the community to giving money to worthwhile projects or causes, and frequently focus on helping elderly citizens or young students.

This team event (2 or 3 members) challenges FBLA members to develop a community service project. Reports produced for this event must describe one chapter project that serves the community and is designed for chapter participation rather than individual participation.

Written reports must include the purpose of the project, scope and intensity of the project, uniqueness of the project, benefits to and impact on the community, and evidence of publicity. The report should be clearly written in a concise manner with logical arrangements of information. Creativity of written presentation, design, and graphics is encouraged. Correct grammar, punctuation, spelling, and acceptable business style are expected.

During the first round of oral presentations, team members have 2 minutes to give an oral abstract of the project. Visual aids and audiovisual equipment may not be used in the preliminary round. Judges are allowed 5 minutes to ask questions about the project.

During the second oral presentation, team members are given 5 minutes to set up and 10 minutes to present with visual aids and audiovisual equipment.

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**Performance Indicators Evaluated**

- Define the purpose of the project by stating project goals and service provided to the community and its citizens.
- Highlight the scope and intensity of the project (planning, development, and implementation).
- Explain what makes the project unique.
- Describe the benefits to the community.
- Demonstrate evidence of publicity.

You will be evaluated for your:

- Clear and concise presentation with logical arrangements of information
- Creativity of written presentation, design, and graphics
- Correct grammar, punctuation, spelling, and acceptable business style

*For more detailed information about performance indicators, go to the FBLA web site.*

**Think Critically**

1. What makes your project unique?
2. Who benefits from your project?
3. How will you generate the maximum amount of participation in the project by FBLA members?
4. Why do businesses participate in community service?

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CHAPTER 4  Assessment  95
Global Business Project

Identify International Business Opportunities

Goals
- Explore the economic environment of another country.
- Research the cultural impact on a nation’s business environment.
- Identify political factors affecting the business activities in a foreign country.
- Select a business idea (product or service) for selling in another country.
- Analyze trade barriers that may affect international business activities.

Activities
Use your textbook, library materials, web sites, interviews with people, and other resources to complete the following.

1. Select a country. Conduct economic research for this country. Obtain information on natural resources, agricultural products, imports, exports, standard of living, GDP, and inflation. Write a summary to describe this information.

2. Locate information about foods, habits, customs, traditions, and beliefs of people in the country. Try to talk to a person who has visited or lived in the country. List two or three ways in which the country is different from most others.

3. Laws regulating business differ from country to country. Research the political and legal environment of your chosen country. Present your findings on laws, barriers, and taxes in a chart, table, or other visual format.
4. Based on your country research, describe a new business idea. This business opportunity could be based on climate, health care, food, transportation, natural resources, technology, or other aspects of the nation’s economy.

5. Foreign governments often take actions to protect companies in their own country. These trade barriers might include tariffs, import quotas, taxes, and other restrictions. Discuss an existing or potential trade barrier for the country you have researched.

Present

1. Prepare a portfolio (folder, file, or notebook) to store the information and materials you created in the activities above.

2. Create a poster (or other visual display) conveying the main points of a business idea (product or service) that could be sold in other countries. Highlight how the business opportunity was created and what needs or wants will be satisfied.

3. Interview a person who has lived in or traveled to another country. Ask questions related to the culture, food, leisure, customs, holidays, and business activities unique to the nation. Ask the person for permission to tape (audio or video) the interview.
Unit 2

Business Organization and Management

5 Business Organization
6 Entrepreneurship and Small Business Management
7 Management and Leadership
8 Human Resources, Culture, and Diversity
9 Career Planning and Development
From Lawyer to Learning Expert

Trained as a lawyer, Gene Wade realized the importance of education. Today, his emphasis is in the classroom instead of the courtroom. Wade is the head of Platform Learning, a tutoring service that assists over 50,000 underprivileged students each year. The company, based in New York City, makes use of “Learn-to-Succeed” tutoring. The program brings together parents, schools, community organizations, and local educators. These groups combine to provide appropriate motivation and teaching materials for individual student needs.

Wade has had a strong influence on the lives of many young people who come from difficult situations. Wade was raised in a Boston housing project laced with gang activity. He was an average student who was helped by a community youth leadership program. After achieving success as a lawyer, Wade was drawn to helping students. Wade’s Platform Learning organization tutors students in 18 states to “Believe ... Achieve ... Succeed.” The young people gain confidence, improve academic skills, and gain a foundation for lifelong learning.

Think Critically

What are needs in your community that could result in a business for improving people’s lives?

Comfortable and Profitable

A product you create for yourself can result in a $100 million company. That’s exactly what happened for Karen Neuburger. She was a stay-at-home mom who wanted to avoid being part of a major corporation. A former fashion industry executive, Karen created comfortable, oversized pajamas for herself to wear around the house. She then realized others might also want this product. Now, Karen is CEO of Karen Neuburger, a company that specializes in pajamas, pillows, socks, and other comfort products.

Karen’s fashion and clothing business background started as a buyer at Maurice’s, a small women’s clothing store in Minnesota. Then, she became a merchandise manager as the company grew into a 700-store chain. After moving to the San Francisco area, she began her pajama business. She designed a pair for herself based on her husband’s pajamas. Karen sewed a pair of ultra soft, comfortable, fun pj’s to wear around the house. Soon her friends at Macy’s and Nordstrom were asking for the product. Karen maintains strong enthusiasm for her products. This helps convince others to carry them in their stores.

Think Critically

Have you had ideas for a product or service that could be the basis for a start-up company?
Chapter 5

Business Organization

5-1 Business in the U.S. Economy
5-2 Forms of Business Ownership
5-3 Organizational Structure for Businesses
Planning a Career in...
Corporate Leadership

Rising to the top of one of the world’s largest corporations seems like the dream job in business. The Chief Executive Officer (CEO) of a corporation may make several million dollars a year in salary and bonuses, have a large office with dozens of support staff, travel worldwide on a corporate jet, and make daily decisions that directly influence the success of the company. Corporate executives also work long hours and face the competing expectations of stockholders, the Board of Directors, employees, and customers. While they receive many perks and benefits, their success or failure may be determined more by economic conditions, government regulation, and the stock market than their own decisions and abilities.

A corporation’s goals and policies are established by the top executives. The executives meet frequently to set direction, review company performance, and establish policy. They then delegate work to the organization’s managers and employees. They know that they are ultimately responsible and accountable for the performance of the company.

Employment Outlook
- There are about three million top executive positions in business today, with the greatest opportunities in the fastest growing industries including service businesses, communications, technology, and health care.
- Corporations are constantly looking for skilled and creative executives to lead their businesses. However, most top executive positions are filled by people who have many years of experience in the industry and a successful management track record.

Job Titles
- Chief Executive Officer
- Chief Operating Officer
- President

Needed Skills
- Corporate executives have varied backgrounds, but often are skilled in finance, management, and business operations.
- Executives must study large amounts of information, listen carefully to the ideas and opinions of others, and juggle many activities.
- They must be willing to take risks, handle stress, and be decisive.
- Executives need highly developed public relations and speaking skills as well as the ability to interact effectively with individuals and groups in high pressure situations.

What’s it like to work as a Corporate Executive

The schedule of a CEO is packed most days. It may start with an hour of reading before attending a conference with the heads of other companies and government officials. Lunch is with the management team to review the company’s financial performance, followed by a press conference. Two hours are spent on the telephone talking to a senator about a telecommunications law, discussing labor contract negotiations with the Vice-President of Human Resources, and speaking with a manufacturer in Japan about a proposed joint venture. After an hour workout at the executive gym and a quick dinner, it is off to the airport for a flight to Brazil to oversee the opening of a new manufacturing facility. The flight will be spent studying reports, completing correspondence, and watching a videotaped briefing on Brazil’s economy.

What about you? How would you prepare for the stress of being a Corporate Executive? Do you believe that the work justifies the high salary and benefits?
Business in the U.S. Economy

**Goals**

- Describe the changing status of U.S. employment.
- Discuss the role of business in the U.S. economy.
- Describe three major types of businesses.

**Key Terms**

- contingent worker
- intermediary
- service business

**Focus on Real Life**

Sami Rehm loves digital photography. Last year she bought a professional-quality camera with several lenses. She has become very good at using photo editing software. While Sami’s photography is currently a hobby, she has framed and sold several of her photographs at local art shows.

Sami has started to wonder if she might be able to use her interest and skills in photography for a career. She knows newspapers, magazines, advertising agencies, and other businesses use photographers. She also knows that people have their own photography studios.

Sami expressed her feelings to her mother. “I know I love photography now. Would I like it as much if I did it every day as a job? I wonder what training and skill a business expects when they hire a photographer?”

**THE CHANGING U.S. JOB MARKET**

As the 21st century begins, there are striking changes in employment and careers in the U.S. The end of the 20th century saw many new career prospects in the dot.com world. It also saw the decline of some traditionally important jobs like manufacturing and agriculture.

**Employment Data**

From 1992 to 2002, total employment grew by nearly 17 percent. In 2002, 144 million people held jobs. That number is projected to reach 165 million by 2012, an increase of almost 15 percent.

The term baby boomers refers to the large number of people born between 1946 and 1964. They have dominated the labor market since they began working in the 1960s. They will continue to do so until they begin retiring in the 2010s. The average age of U.S. workers in 2010 will be over 40. A mini boom of younger workers will cause the 16-to-24-year-old age group to grow faster than the overall labor force for the first time in 25 years. Other groups that will go through higher employment growth rates are Asian-, Hispanic-, and
African-American workers. Currently, white workers make up 75 percent of the labor force. That number will drop to 70 percent by 2012. Over the last 50 years, one of the most striking trends in employment has been the participation of women. In the early 1960s, 35 percent of women were working outside the home. The number of working women doubled by 2000. By 2012, nearly one half of all jobs (48 percent) in the U.S. will be held by women.

Pressures on Employees
At one time, it was thought that technology would allow people to work fewer hours. This has not occurred. Economic stress has led to downsizing of the number of people employed by many companies. Companies streamlined production and implemented other cost-cutting procedures. Businesses required employees to take on new tasks and work extra hours. Some full-time jobs were reduced to part-time. Wage rates decreased. Many people were forced to find second jobs to meet their economic needs.

A recent survey reported that seven of ten parents felt they were not able to spend enough time with their children. At the same time, children see their parents changing jobs, taking on more responsibility, completing additional education to improve career opportunities, and making important decisions to balance work and family life. Those experiences will likely shape the career and family decisions of the next generation.

Economic pressures also resulted in the increased use of contingent workers. A contingent worker is one who has no explicit or implicit contract for long-term employment. About 5 percent of the U.S. workforce (nearly 6 million people) is made up of contingent workers. Some estimates project that number will double in ten years. Some people take contingent work because they cannot find permanent employment. Others choose contingent work because they like the flexibility it offers.

BUSINESS AND THE ECONOMY
Businesses make the goods and services you use each day. That includes the products and services used by other businesses as well as those needed by individual consumers. In 2002, all businesses worldwide produced over $32 trillion of goods and services. U.S. businesses were responsible for almost one-third of that production. Nearly 23 million full- and part-time businesses produce those goods and services.

Size of Businesses
Most U.S. businesses are quite small. The largest number, nearly 18 million businesses, have no employees other than the owner. About 5 million companies employ less than 20 people. Just
over 500,000 employ 20–100 people. About 103,000 large U.S. businesses employ 100 or more workers. Of those large companies, 930 employ over 10,000 people. Figure 5-1 shows the distribution of U.S. businesses by employment size.

**Roles of Business**

Businesses play several key roles in the U.S. economy. They provide employment for millions of people. Employee wages are used to purchase goods and services. Profits earned by businesses are used to compensate owners and investors. Most businesses pay taxes to federal, state, and local governments. Governments spend these taxes to provide services such as clean water, well-maintained streets, police and fire protection, hospitals, and schools.

The most important role of businesses is to make and distribute products and services needed by consumers, government, and other businesses. Businesses make the clothing, movies, music, food, and other items you use every day.

**Impact on a Community**

A business can have an important impact on the community in which it operates. When a new business opens, it pays wages to its workers. It also buys goods and services from other businesses in the area. This money has not been in the community before. Employees and businesses in turn spend much of the money to purchase things they need.

The money spent may result in the need for more employees in the community. They will need housing, automobiles, food, and entertainment. They will pay taxes to the community to support needed community services.

When a large business opens in an area, other businesses will often locate there to support the larger business. Small businesses may be started to meet the needs of the residents and other businesses. Successful businesses contribute to more jobs, more income, and a thriving economy in the communities where they operate.

**Business Activities**

Businesses may be large or small, simple or complex. A business might operate in only one community. It may have many locations across the nation or around the world. Although there are many types and sizes of businesses, all firms perform six basic activities.

**Generating Ideas** A business begins with a new idea. Someone must have an idea for a new product or service or a new way to carry out a business process. A business must continue to improve and develop new ideas in order to remain successful. Businesses must remain competitive with other firms that sell similar goods and services. Many companies have a research and development department that works full-time to discover new products, service, and operating ideas.

**Raising Capital** Businesses need financial resources to operate. They use these financial resources to buy buildings and equipment, hire and train
Business in the U.S. Economy

workers, and complete day-to-day business operations. A large amount of capital is needed to start most businesses. Some capital comes from owners. Most is obtained through loans from financial institutions or from investors.

A business needs more capital as it develops and grows. Some of that capital will come from reinvested profits. A business will need to continue to work with banks and attract additional investors to have enough money for ongoing operations.

**Employing and Training Personnel** Businesses need human resources. Even businesses that begin with no employees other than the owner will add part- and full-time employees as they grow. Businesses have procedures for recruiting, hiring, and training employees. They pay wages, benefits, and employment taxes. New employees receive training in order to perform their jobs correctly. Further training will be necessary when procedures change, new tasks are added, or technology is introduced.

**Buying Goods and Services** All businesses buy goods and services.

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**Work as a Group**

If you own a business, would you rather raise capital by obtaining a loan from a financial institution or by offering partial ownership to other investors? In your group, create a list of advantages and disadvantages of each method of raising capital.

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**Technology Topics**

**Expanding E-Government**

Computers have a major impact on the way government operates. Offering services online has become the goal of most agencies. Rather than going to a government office to pick up a form, apply for a license, or make a payment, people can complete many of these activities online.

In a study of the development of e-government services around the world, the United Nations has identified the following five stages:

- **Emerging** Official government online presence established
- **Enhanced** Number of sites increase and become more interesting and useful
- **Interactive** Users can download forms, e-mail officials, and interact through the Web
- **Transactional** Users can complete transactions and pay for services online
- **Seamless** Full integration of information and services across agencies—one-stop service

By 2002, the U.S. government had 22,000 web sites with more than 35 million web pages. Annual spending by the Federal government for information technology services is more than $50 billion. Over 60 percent of all Internet users interact with the federal government through its web sites. Moving government services to the Internet may result in over one billion dollars of savings each year.

Two major barriers stand in the way of the development of e-government. Most important is privacy and security of the personal information contained in government records and submitted by citizens. That information includes tax records, medical histories, and personal information such as driver’s license and social security numbers. The second barrier is the unequal access to technology. Thousands of citizens do not have secure high-speed Internet connections. Others do not have the literacy or computer skills to use government services.

**Think Critically**

1. Search the Web and identify government services provided by your local and state governments. What stage of development is demonstrated by the web sites you visited?
2. What can governments do to reduce the barriers of privacy, security, and citizen access to e-government services?
Businesses use many of the purchases for their own operations. Other purchases are resold. Manufacturers of automobiles must buy steel, aluminum, and plastics to be used to form the frame and body of new cars. They will also purchase tires, batteries, airbags, and air conditioning units that will be installed on the production line.

A retailer buys an assortment of products to sell to customers. It must also buy the display equipment, computers, and cleaning supplies used to operate the business. Businesses purchase an array of services from other companies. These include advertising, legal and accounting services, lawn care and building maintenance, and security.

Marketing Goods and Services
Marketing is the activities directed at providing the goods and services wanted by a business’s customers. Without marketing, even the best products and services may remain unsold. Businesses need to understand and perform many marketing activities. They must satisfy customers who usually can choose to buy from competitors offering similar products and services.

Maintain Business Records
All businesses must have some type of record-keeping system. The records are needed so owners and managers can track performance and make decisions. Customers will need information on orders and payments. Businesses are required by government to keep records and submit information. Today, technology is available to make record keeping easy and accurate. With computer technology, business owners and employees can quickly access information needed to understand business performance and solve problems that occur.

CHECKPOINT

What are the six basic activities completed by all businesses?

TYPES OF BUSINESSES
You, your family, and friends use a variety of businesses to buy the things you use. You recognize other businesses but never use them. You don’t even know about many others. There are three major categories — producers, intermediaries, and service businesses.

Producers
Producers create the products and services used by individuals and other businesses. They are responsible for using resources to make something that is needed by others. A business that takes resources from nature for direct consumption or for use in developing other products is an extractor. Extractors pump oil, mine coal, or cut timber. Farmers cultivate land and use other natural resources to grow crops and livestock for consumption. Manufacturers get supplies from other producers and convert them into products. They sell their products to consumers and other businesses.

Business activities start with producers. A builder obtains lumber, cement, shingles, carpet, and paint to construct a house, factory, or office building. A cereal manufacturer buys wheat and oats, sugar, and dried fruit as well as

Describe three major types of businesses.
cardboard, glue, and ink to process and package your favorite breakfast food.

**Intermediaries**

Intermediaries are businesses involved in selling the goods and services of producers to consumers and other businesses. The most common types of intermediaries are retailers and wholesalers. Many other businesses focus on one or a few activities that assist in distributing and selling products and services. Specialized intermediaries include transportation companies, advertising agencies, storage centers, sales offices, and data processing centers.

**Service Businesses**

Many businesses do not make products. They offer something that is intangible, meaning it has no physical qualities. A service business carries out activities that are consumed by its customers. It does not offer products for sale. Service businesses include dentists, physicians, and lawyers as well as pet sitters, painters, and furniture movers. New types of service businesses are Internet service providers, web designers, and online travel agents. Businesses as well as final consumers use services. A business might contact an international trade specialist to help it set up a sale to a new customer in South Africa. A communications firm could contract to choose and install a new phone system for large telemarketing businesses.

Service businesses are the fastest growing part of the economy. Over 60 percent of all U.S. employment is now in service-producing businesses. While you often hear of low-pay and low-skill service jobs, there are many new businesses offering professional and technical services requiring highly educated employees.

**CHECKPOINT**

How does a manufacturer differ from an extractor?

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**Assessment**

**Key Concepts**

Determine the best answer.

1. The largest number of U.S. businesses employ
   a. over 100 people
   b. between 50 and 100 people
   c. between 10 and 20 people
   d. no employees other than the owner

2. Which of the following is not one of the common activities of all businesses?
   a. producing goods and services
   b. employing and training personnel
   c. marketing goods and services
   d. maintaining business records

3. A retailer is an example of an
   a. extractor
   b. producer
   c. intermediary
   d. service business

**Make Academic Connections**

4. Math If 62 percent of all people working in the U.S. are employed in service occupations, how many people held service jobs in 2002? How many will hold service jobs in 2012 if the percentage increases to 64%? Use employment information from the lesson to make the calculations.

5. Critical Thinking Select a product that involves all of the types of businesses in its production and marketing. Draw a picture that shows each business and its role in the successful production and sale of the product.
BUSINESS OWNERSHIP

Most people have thought at some time that they would like to own a business. The chance to be in control, make decisions, and invest money to make a profit is challenging but exciting. Thousands of people are business owners. The amount of control they have, how decisions are made, the sources of money for the business, and control over profits is not the same for every business owner. The form of ownership affects each of those decisions.

There are three major forms of business ownership—proprietorship, partnership, and corporation. There are also several other specialized forms of ownership.

Proprietorship

A proprietorship is a business owned and run by just one person. It is the easiest form of business to start and end. There are very few legal requirements regarding the business ownership and capital that must be met.

Focus on Real Life

Jaden looked through the daily stock market update in the evening newspaper. He was searching for the listing of the stock he owned—GMS. His grandparents had given him five shares of stock in General Motors Corporation when he was born. He didn’t get interested in it until recently when he learned more about the stock market. Now he knew he was an owner of the auto company. The success of the company determined the value of his ownership. While the stock price had gone up and down, it was now at its highest point since he began following the stock price.

While Jaden couldn’t make day-to-day decisions as a stockholder, he liked to think what it would be like to be the top executive of GM. He knew that if he was responsible for major decisions about the company’s products and operations, thousands of stockholders would be watching to see how those decisions affected the value of their stock.
Many individuals like the proprietorship form of ownership. It gives them sole control over all business decisions. The owner receives all profits made by the business. He or she can determine how those profits are used. The owner is also responsible for all debts of the business. If the business fails, the owner has almost no shelter from creditors. Any money and other assets owned by the proprietor, whether used in the business or not, can be obtained by creditors to pay the business debts.

Partnership

A partnership is a business owned and controlled by two or more people who have entered into a written agreement. A partnership is very similar to the proprietorship in several ways. It is quite easy to start. The owners are both responsible for key business decisions and functions. The partners share both investments and profits based on the terms of the partnership agreement. Each partner is liable for all of the debts of the business should it fail.

Corporation

A corporation is a separate legal entity formed by documents filed with your state. It is owned by one or more shareholders and managed by a board of directors. Most corporations have several owners who invest in the business by purchasing shares of stock. Corporations are more difficult to form than either proprietorships or partnerships. They must also meet more legal requirements. Not all owners have direct involvement in decision-making about business functions. They will not have access to profits unless the board of directors approves it. Corporations protect the liability of stockholders to only the amount of money they have invested.

Most U.S. businesses are organized as proprietorships. However, as shown in Figure 5-2, proprietorships have a very small percentage of business revenues.

<table>
<thead>
<tr>
<th>Form</th>
<th>Number of businesses (2000)</th>
<th>Total revenue (thousands)</th>
<th>Percent of all businesses</th>
<th>Percent of total revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proprietorship</td>
<td>17,904,731</td>
<td>$1,020,957,284</td>
<td>72%</td>
<td>5%</td>
</tr>
<tr>
<td>Corporation</td>
<td>5,045,274</td>
<td>17,636,561,349</td>
<td>20%</td>
<td>85%</td>
</tr>
<tr>
<td>Partnership</td>
<td>1,338,796</td>
<td>1,829,568,091</td>
<td>5%</td>
<td>8%</td>
</tr>
<tr>
<td>Other</td>
<td>718,704</td>
<td>344,751,557</td>
<td>3%</td>
<td>2%</td>
</tr>
</tbody>
</table>
CHAPTER 5

Business Organization

Work as a Group

Compare the unique interests and skills of each member of your group. Identify possible businesses that could be formed as a partnership by combining the talents of two or more of the group members.

Choosing a Partnership

A partnership is a bit more complex and formal than a proprietorship. In many states, a partnership can be formed by the verbal agreement of two or more people. It is usually better to have a written partnership agreement. The partnership agreement is a written agreement among all owners. It details the rules and procedures that guide

to start a business because they prefer the freedom of working for themselves rather than for another person. They want to be in total control of the business. Many new business owners have limited knowledge of the forms of ownership and want to begin the business as easily as possible. Some people form a business from a hobby or have operated a business on a part-time basis. They may expand the business over a few years and spend little time thinking about other ways the business could be organized.

Starting a proprietorship is easy. You just have to begin buying and selling as a business. You don’t even need a business name. You do need to obtain any required government licenses and permits. You will need to account for income and expenses and pay taxes on the profits of the business. If operating the business for several years will be your primary job, it is best to choose a name for the business. You will need to register the name with local, state, and federal governments.

A proprietorship provides a tax advantage for the owner. All income is taxed as a part of your personal income. Many business expenses can be used to reduce the income. That benefit also carries the most significant disadvantage of a proprietorship. In the eyes of the law, the owner is the same as the business. Any debts of the business are the responsibility of the owner. Personal assets not connected to the business will need to be used to pay business debts if the business assets are not adequate to cover those debts. In that way, a failed business may result in the owner losing almost everything.

For people who want total independence, do not want to be exposed to significant government regulation, want to be in control of all business decisions, and are willing to take on the entire risk of a business, the proprietorship offers an effective form of ownership. For a person who wants to expand the business, is willing to share control and decision-making in return for additional resources and reduced risk, and wants some protection for money invested, other forms of ownership are better.

How might a partnership be more advantageous than a proprietorship?
ownership and operations. It typically identifies the business name, the investments, and other contributions of each partner. The agreement shows how profits and losses will be divided among the partners. It defines the authority and responsibilities granted to each person and how the partnership can be dissolved. Most states require that partnerships register a business name as well as the name of each person in the partnership.

The advantage of a partnership is that two or more people can contribute to the investment needed to start the business as well as the expertise required to run a business. At the same time, each partner is responsible for decisions made by all other partners. There is no protection for the personal assets of any partner. If the business fails, each person can lose much more than the amount of the original investment. If a partner chooses to leave the partnership or dies, the partnership normally must be dissolved.

A partnership is a good ownership form for people who share an idea for a business. They want to cooperate in managing and investing in the business. It is the easiest form for people who work well together and want to share the risks and rewards of the business. It has the same liability of a proprietorship and presents problems if other people want to join the partnership or if it needs to be dissolved.

**Choosing a Corporation**

Most people think of corporations as very large businesses. It is the most popular form of ownership for large businesses. It is becoming increasingly popular for new and small businesses as well. Corporations are subject to many more laws and are more difficult to form than either proprietorships or partnerships. They offer a number of advantages to the owners as well.

Corporations are treated as an “individual” by governments. They must follow the laws of the state in which they are organized. To form a corporation, you must file articles of incorporation with the appropriate state government office. The **articles of incorporation** is a written legal document that defines ownership and operating procedures and conditions for the business. Each state has specific information that must be included. States usually provide a form that can be filled out. The business must create **corporate bylaws** that are the operating procedures for the corporation. It must name a **board of directors**, the people who will make the major policy and financial decisions for the business. The corporation also issues shares of stock to the investors and details how more investments can be made.

Even though a corporation is more difficult to form and is subject to more government rules, it offers several advantages to owners. The liability of any owner is limited to the amount of money invested. The amount of debt of the business does not matter. People can invest in the business and receive some of the profit without having to take part in the day-to-day management and operations. The business can be easily expanded and ownership can be changed by the sale of stock.

Disadvantages of corporate ownership are that decision-making is shared among managers, the board of directors, and shareholders. Many more
records are required and more laws regulate operations than for other forms of ownership. Because corporations are treated as individuals by governments, they must pay corporate taxes on profits earned. Then the investors also pay taxes on their individual earnings from the business.

**CHECKPOINT**

Which form of business ownership is the most complex and difficult to form?

**OTHER FORMS OF OWNERSHIP**

Most businesses are organized as one of the three common forms just discussed. There are other choices of ownership. Some are specialized forms of partnerships and corporations. Others are totally unique forms.

**Specialized Partnerships and Corporations**

In a general partnership, all partners take part in ownership and operation of the business. A limited liability partnership identifies some investors who cannot lose more than the amount of their investment, but they are not allowed to participate in the day-to-day management of the business. This type of partnership is difficult and costly to set up. A joint venture is a unique business organized by two or more other businesses to operate for a limited time and for a specific project. It is a type of partnership.

A corporate form that is favored by many small businesses is the S-corporation. An S-corporation offers the limited liability of a corporation. All income is passed through to the owners based on their investment and is taxed on their individual tax returns. A newer ownership form is the limited liability company (LLC). It combines the best features of a partnership and a corporation. A limited liability company provides liability protection for owners. It has a simpler set of organizing and operating requirements than a corporation. No articles of incorporation or bylaws are needed. A simple document much like a partnership agreement must be developed.

A nonprofit corporation is a group of people who join to do some activity that benefits the public. They work in areas such as education, health care, charity, or the arts. Nonprofit corporations are free from corporate income taxes. They can raise funds by receiving grants and donations from individuals and businesses. As with other corporations, they must organize as a corporation. The government must approve their purpose and operations.
**Cooperatives and Franchises**

Sometimes a group of people forms a cooperative to provide goods and services that they all need. A cooperative is owned by members, serves their needs, and is managed in their interest. Members form a consumer cooperative so that they can purchase goods and services cheaper as a group than they could individually. A business cooperative forms to market the products produced by members or to purchase products needed by the members. Large numbers of small businesses will have greater bargaining power than the individual businesses.

A **franchise** is a written contract granting permission to operate a business to sell products and services in a set way. The company that owns the product or service and grants the rights to another business is known as the **franchiser**. The company purchasing the rights to run the business is the **franchisee**. A franchise is a way to expand a business using the investments of others while maintaining control over the name, product quality, and operating procedures.

The franchisee maintains day-to-day operations and receives the profits of the business. It pays a fee and percentage of the profits to the franchiser in return for operating assistance. Some popular and successful franchises include Jiffy Lube, Century 21 real estate offices, Mail Boxes Etc., Wild Birds Unlimited, Merry Maids, CD Warehouse, MAACO Auto Painting, and New York Subs.

**CHECKPOINT**

What are the other specialized forms of business ownership?

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**Assessment**

**>> Key Concepts**

Determine the best answer.

1. The form of ownership that gives one person sole control over all business decisions is the
   a. proprietorship
   b. partnership
   c. corporation
   d. franchise

2. True or False. All investors in a general partnership have full liability for the debts of the business.

3. The people who make the major policy and financial decisions in a corporation are the
   a. investors
   b. board of directors
   c. managers
   d. owners

4. A special form of business organization that combines advantages of a corporation and a partnership is a
   a. franchise
   b. nonprofit corporation
   c. cooperative
   d. limited liability company

**>> Make Academic Connections**

5. **Communication** You have been contacted by a friend who is thinking about opening a retail store to display and sell the work of local artists. Write a two-page memo in which you compare the advantages and disadvantages of the three common forms of business organization. Recommend the one you think would be best for the new business.

6. **Research** Use the Internet to find information on a franchise opportunity that relates to a current career interest. Prepare a chart that describes the franchise, the products or services of the business, the investment requirements, and the benefits of becoming a franchisee.
People who own stock in a publicly traded company must be able to read a stock table. It provides information on the performance of the stock each day and over an extended period of time. By understanding stock tables, investors can determine how well the company is performing. They can decide whether to maintain their investment, buy additional stock, or sell and move their money to another investment.

Stock tables are available in most daily newspapers. They can also be accessed online. They report on the performance of publicly traded stocks on all of the major stock exchanges. Tables may be organized a bit differently, but will contain the same information shown in this example. On weekends, many newspapers report stock performance for the entire week.

52 WK HI-LO is the highest and lowest prices at which the stock was sold in the past year (52 weeks). In the example, the highest price was $28 and the lowest was $13.

SYM is the company symbol or abbreviation that identifies the firm issuing the stock. This symbol is sometimes referred to as the company’s “ticker symbol.” The fictitious symbol in the example is LZD.

DIV represents dividends, which are the amount of money approved by the board of directors of the company to be paid to stockholders. The column shows the most recent dividend paid per share—$1.10. Dividends are a measure of the health of the business. They are one way that stockholders earn a return on their investment in addition to gains in the value of the stock.

VOL shows the volume of shares (in 100s) traded on the date of the table. In the example, 22,800 shares were traded by LZD. Volume gives information on the change in demand for the company’s shares.

YLD approximates the yield of the dividend paid. The dividend yield is the current rate of return on all capital invested in the company. This allows easier comparison of the performance of companies with different stock prices. The yield is calculated by dividing the current dividend by the closing stock price.

\[
\text{Dividend Yield} = \frac{\text{Dividend}}{\text{Price}} = \frac{1.10}{24.00} = 4.58\% \text{ yield}
\]

PE is the comparison of the price per share to the earnings per share. It is called the price/earnings ratio. It shows how much an investor is willing to pay for $1 of current earnings by one share of stock. The ratio is calculated by dividing the price by the earnings per share (EPS). In the example, LZD stock is selling for over 10 times the current earnings.

\[
\frac{\text{Price}}{\text{EPS}} = \frac{24.00}{2.28} = 10.53 \text{ PE}
\]

HI-LO represents the highest and lowest prices of all trades made during the date of the table. In the example, the high was at $25.00 and the low was $23.50.

CLOSE is the last price at which a trade was made during the trading day. In the example, $24.00 is the close.

NET CHG is the change between the closing price for the previous day and the current day. Because the net change listed is 0.5, the price of the stock on the previous day was $23.50.

Think Critically
1. What information from the stock table do you think is most important for a stock owner to watch on a regular basis? What is the least important?
2. How do stock tables help in comparing the performance of two stocks with very different prices?
Organizational Structure for Businesses

5-3

**Goals**
- Understand important principles in designing an effective organization.
- Compare alternative organizational structures for businesses.

**Key Terms**
- mission statement
- goal
- policies
- procedures
- organization chart

**Focus on Real Life**

Mary Jo’s company had just approved a policy that allowed some employees to telecommute. That means they can work from home and complete their work using a computer and other technology. Mary Jo was interested in the idea but wasn’t certain whether to apply.

She was afraid she might not be as motivated to complete her work every day if she didn’t have to go to the office and keep a regular schedule. She also was concerned that it may be much more difficult to communicate with coworkers and get feedback from her manager using the technology. Would she be viewed as a productive and valued employee if people didn’t see her at work every day?

**DESIGNING AN EFFECTIVE BUSINESS ORGANIZATION**

It is not easy to create a successful business. Many new businesses fail in the first few years. Few businesses maintain their success for the lifetime of the owner. Successful businesses need more than a good product or service. Skilled managers, well prepared and motivated employees, adequate resources, and effective procedures add to business success. A business needs to be well organized to help people do their work well. An effective business begins with a clear purpose and the application of key principles for organizing work.

**Setting Direction**

The direction for a business comes from its **mission statement**. A mission statement is a short, specific written statement of the reason a business exists and what it wants to achieve. The mission statement for Marriott Hotels is “To provide economy- and quality-minded travelers with a premier, moderate-priced lodging facility which is consistently perceived as clean, comfortable, well-maintained and attractive, staffed by friendly, attentive and efficient people.”

> Understand important principles in designing an effective organization.
Principles of Effective Organization

When several people work together, their work needs to be organized so they work together well and achieve their tasks. Several principles guide the effective organization of work.

Responsibility, Authority, and Accountability

Responsibility is the obligation to complete specific work. Authority is the right to make decisions about how responsibilities should be accomplished. Accountability is taking responsibility for the results achieved. In an effective organization, all managers and employees have a set of responsibilities as a part of their jobs. With every job assignment, they know they have the authority to make the decisions and obtain the resources needed to complete the assignment. They know they will be recognized and rewarded if they are successful. They will be held accountable if the work is not completed well.

After a mission statement is developed, the business sets goals. A goal is a precise statement of results the business expects to achieve. Goals are used to define what needs to be accomplished and to determine if the business is successful. An example of a goal for an automobile manufacturer is “to produce the top-rated brand for quality and customer satisfaction.”

Finally, the business sets policies and procedures for the organization. Policies are guidelines used in making consistent decisions. Procedures are descriptions of the way work is to be done. Effective policies and procedures provide guidance and direction to people working in the organization.

In an organization, every member has a specific role to fill. Describe some roles.

**FYI**

In a recent Junior Achievement survey, 41 percent of teens believe starting and operating their own business will offer greater job security than being an employee in another company. Nearly 75 percent of the teens indicated they would like to start their own business someday.
**Unity of Command** A key organizing principle is to provide unity of command. Unity of command means there is a clear reporting relationship for all staff of a business. If there is confusion in assignments and unclear relationships among people who are working together, it will be hard for people to know what to do or where to go for help. For each work assignment, people need to know who is the leader and how decisions will be made.

**Span of Control** The last organizing principle is span of control. Span of control is the number of employees who are assigned to a particular work task and manager. A large number of people working with little support from their manager cannot be effective. In the same way, a manager with only a very small number of people may provide too much control. Organizations need to make sure that workers have a balance of supervision and freedom to do their work. The span of control for well trained, experienced, and motivated employees can be much greater than for new and inexperienced employees who are not enthused about their work.

**Types of Organizational Structures**

When only one person works in a business, there is little need for an organizational structure. The sole employee is responsible for all of the work. When more people are hired, there will need to be an agreement on what work each person will do and if one person has authority over the work of others. An organization chart is a diagram that shows the structure of an organization, classifications of work and jobs, and the relationships among those classifications. You can see a simple organization chart for a business in Figure 5-3.

**Why is it important for employees to understand the structure of the company where they work?**

**Figure 5-3**

*Business Organization Chart*

- President
  - VP of Finance
  - VP of Operations
  - VP of Marketing
    - Senior Accountant
    - Chief Auditor
    - National Sales Manager
      - Key Account Manager
Matrix Organizational Structure

A newer organizational structure designed to overcome the drawbacks of the functional structure is the matrix organization. In a matrix organizational structure, work is structured around specific projects, products, or customer groups. People with varied backgrounds are assigned together because their expertise is required for the project or to serve the customer. The assignment may be temporary or long-term.

A matrix organization can be interesting and motivating to employees. They work with many different people. They are focused on a specific project or task. However, it can be confusing and inefficient without effective leadership and communication.

CHECKPOINT

What problems can result from the use of a functional organizational structure?

**Functional Organization Structure**

Most businesses use a functional organizational structure. In that type of organization, work is arranged within main business functions such as production, operations, marketing, and human resources. All of the people with jobs related to one of the functions will work together. They report to managers who are responsible for that function. The advantage of a functional organization is that people work with others who have the same skills. A drawback is that people become more focused on their specific function than on the success of the whole business. Often, people working in one function have little interaction with people in other parts of the business.

**5-3 Assessment**

**Key Concepts**

Determine the best answer.

1. True or False. The direction for a business comes from its policies and procedures.
2. The obligation to complete specific work is
   a. responsibility
   b. authority
   c. accountability
   d. recognition
3. Which of the following is not shown on an organizational chart?
   a. the structure of an organization
   b. work relationships
   c. job descriptions
   d. classifications of jobs

**Make Academic Connections**

4. **Technology** Use the Internet to collect examples of the mission statements of several businesses. Rate each mission statement in terms of how effectively it communicates the purpose and direction of the company.

5. **Critical Thinking** Many schools are organized using a functional organizational structure. Teachers are organized into departments such as English, Mathematics, Science, and Business. How could a school be organized using a matrix structure? Design an organizational chart that illustrates that structure for your school. Describe the advantages and disadvantages of that structure.
**Electricity Where There Was None**

Over 30 percent of the world’s population does not have electricity. Not only does that mean a very difficult day-to-day existence, but also no real chance to improve the standard of living with factories, modern stores, and technology. Fabio Rosa believes that for the same amount of money people spend on kerosene, candles, and batteries, he can rent them low-cost solar kits. Using the “free” energy of the sun, electricity can be delivered to rural areas, mountaintops, and villages in his home country of Brazil in South America. It can also be delivered to the many other places in the world with no access to power lines and generators.

When Mr. Rosa was 22, he was named Secretary of Agriculture in a city in rural southern Brazil. He saw hundreds of people leaving their farms and moving to the city. The lack of electricity made it hard to earn a living in agriculture. That put stress on city services and created the likelihood that there would be few farms in the future. Fabio thought that if low-cost solar energy could be supplied, it would result in higher levels of food production. At the same time, improved health and education services could be available, pollution levels would be reduced, and people could come back to their farms. He envisioned small business communities springing up to serve the local farmers powering their stores with solar energy.

Based on his work, Mr. Rosa knew that farm families spent at least $11 per month on kerosene, candles, and batteries. This was about the same amount that would be needed to rent a simple solar system that would provide enough electricity for one farm. With that knowledge, he set out to electrify the rural areas of his country with solar energy kits.

Currently, the solar systems come in three standard sizes: Kit Number 1 rents for $10 per month. It comes complete with a 60-watt solar panel, high-performance battery, all the wiring, plus a number of 12-volt fluorescent lights and electrical outlets for appliances. The system provides, on average per day, 6-7 hours of light and several hours for running appliances, equipment, and a water pump. Kits 2 and 3 rent for, respectively, $16 and $24 per month and come with more lights, outlets, and wattage. The installation cost for a kit — about $150 — can be paid off over the first 12 months. When Rosa distributes the solar systems to farmers, he includes materials to develop an irrigation system and build electric fences to protect farm animals as well as information on modern farming practices. New tools and equipment are being developed that can be powered with the solar system including saws, drills, refrigerators, and even a solar water heater to provide warm showers.

Fabio Rosa is currently installing about 1,500 new solar systems each year. He wants to increase the rate at which poor families can obtain electricity, so he is traveling worldwide to seek investors who will provide money to expand his work. “At this moment,” he states, “we have millions of people without energy, just like we did 10 years ago, just like we did 20 years ago. Brazil has this problem. India has this problem. China has this problem. Bangladesh has this problem. Two billion people have this problem. First, we will demonstrate results on a small scale, then on a regional scale, then all over Brazil, and then the world.”

**Think Critically**

1. Use the Internet to locate additional information on Fabio Rosa’s work.
2. Suggest ways the standard of living of poor families and communities will improve when they have access to electricity.
Business Notes

5-1 Business in the U.S. Economy
1. The employment status of the U.S. is changing. New jobs develop as older jobs disappear. The labor pool is currently getting older, but that will begin to change as baby boomers retire. Minority groups make up a larger percentage of the workforce.

2. Businesses play several key roles in the U.S. economy. They provide employment for millions of people. They compensate owners and investors. They pay taxes to federal, state, and local governments. They make and distribute products and services needed by consumers, government, and businesses.

3. The three major categories of businesses are producers, intermediaries, and service businesses. Producers create the products and services used by individuals and other businesses. Intermediaries sell goods and services. A service business carries out activities that are consumed by its customers.

5-2 Forms of Business Ownership
4. Most businesses are organized as proprietorships, partnerships, and corporations. A proprietorship is a business owned and run by one person. A partnership is a business owned and controlled by two or more people. A corporation is a separate legal entity owned by one or more shareholders and managed by a board of directors.

5. For people who want to work and make decisions independently, do not want to be exposed to significant regulation, and are willing to take on the risk of a business, the proprietorship is an effective form of ownership. A partnership is good for people who share an idea for a business, want to cooperate in managing and investing, and want to share the risks and rewards of the business. A corporation is more difficult to form and is subject to more regulations. Investors’ liability is limited to the amount invested, and they can invest without taking part in the day-to-day management.

6. Other forms of ownership include limited liability partnership, joint venture, S-corporation, limited liability company, nonprofit corporation, cooperative, and franchise.

5-3 Organizational Structure for Businesses
7. Successful businesses have an effective organizational structure. A mission statement, goals, policies, and procedures guide them.

8. The specific structure of a business can be illustrated with an organizational chart. Traditionally, businesses have used a functional structure but now many are using a matrix organizational structure.

Communicate Business Concepts

1. What are some rapidly growing employment opportunities? What types of jobs are declining in numbers? How can you predict what job categories may grow or decline in the future?

2. Why do most businesses have no employees other than the owner? Do you believe most of those business owners earn their entire income from that business? Why or why not?

3. Identify several businesses from your community that fit within each of the three categories of businesses listed in Lesson 5.1. Do you believe your community has more producers, intermediaries, or service businesses? Justify your answer.

4. Would you like to start and own your own business? Why or why not? What do you believe are the risks and benefits you would face if you decided to start a business?

5. Julie states that she wants to be her own boss. If she starts a business, it will be a
proprietorship rather than a partnership or corporation. Explain to Julie why she might want to consider another ownership form. Is it possible for her to be her own boss and yet not use the proprietorship form of ownership?

6. Use a business directory to identify several nonprofit corporations in your area. What public service is each providing? Why do you think each is a public rather than a private corporation?

7. “An effective organizational structure is as important to a business as the quality of its products and services.” Do you agree or disagree with that statement? Discuss your beliefs with another student who has the opposing view.

8. You are starting a shopping service for elderly people in your community who cannot leave their homes. Write a mission statement that clearly communicates the purpose of your business.

9. How will the appearance of an organizational chart for a business using a functional organizational structure be different from one using a matrix organizational structure? What should you be able to learn about a business by studying its organizational chart?

>> Develop Your Business Language

Match the terms listed with the definitions.

10. A business owned and controlled by two or more people who have entered into a written agreement.
11. A short, specific written statement of the reason a business exists and what it wants to accomplish.
12. One who has no explicit or implicit contract for long-term employment.
13. Descriptions of the way work is to be done.
14. A specific statement of results the business expects to achieve.
15. A written legal document that identifies ownership and operating procedures and conditions for the business.
16. Businesses involved in selling the goods and services of producers to consumers and other businesses.
17. A separate legal entity, formed by documents filed with the state, which is owned by one or more shareholders and managed by a board of directors.
18. A written contract granting permission to operate a business to sell products and services in a prescribed way.
19. Businesses that complete activities that are consumed by customers rather than offering products for sale.
20. A business owned and controlled by just one person.
21. A written agreement among all owners that specifies the rules and procedures that guide ownership and operations.
22. Guidelines used in making consistent decisions.
23. A diagram that shows the structure of an organization, classifications of jobs, and the relationships among those classifications.

Key Terms

a. articles of incorporation
b. contingent worker
c. corporation
d. franchise
e. goal
f. intermediaries
g. mission statement
h. organization chart
i. partnership
j. partnership agreement
k. proprietorship
l. policies
m. procedures
n. service business
CHAPTER 5  Business Organization

Decision-Making Strategies

Sonja Bartholomew started a lawn mowing service. She could not charge as much as she needed to make the profit she desired. Her competitors only charged $15 per lawn while she charged $20, but she did a superior job cutting lawns. Still, potential customers did not want to pay the extra $5.

A friend, Eduardo Guadalupe, suggested that they work together. He was good at trimming shrubs and had ideas for improving landscapes with flowers and lawn ornaments. They would offer a unique service when they combined their businesses. They could charge an amount that would result in a good profit for both of them. They would seek out homes in neighborhoods with above-average income levels.

24. What will be special about the services that Sonja and Eduardo can offer together? What other services might they include?

25. Why would they target above-average income levels?

26. Should Sonja continue to run her business as a proprietorship and hire Eduardo as an employee? If not, what other form of business ownership would you recommend? Justify your choice.

Make Academic Connections

27. **MATH** To provide additional employment and add to its tax base from businesses, Yorktowne’s city council opened a business park on the edge of the city. After five years, they had attracted two new manufacturers and four supporting service businesses to the park. The total value of the property of all six businesses was $15,825,500. The companies paid $0.78 per $1,000 of property value each year as property tax. In addition, the businesses employed 328 people at an average salary of $36,000. Each person paid a 1% city income tax each year.
   a. What is the total amount of taxes the city collected as a result of opening the business park?
   b. In addition to the tax dollars, what other benefits might the city receive from opening the business park?

28. **TECHNOLOGY** Use a spreadsheet and graphics program to make a chart or graph showing one of the following sets of data: (a) the five largest employers in the world and the number of employees for each, (b) the composition of the U.S. workforce by the age of employees, (c) the average size of U.S. business by annual sales revenues.

29. **COMMUNICATION** The DECA chapter in your school is planning to open a school store to sell school supplies, school-related apparel, and spirit items before and after school. Prepare a mission statement for the store. Write one goal that identifies a specific result the store should achieve. Write a policy statement for accepting returns of merchandise purchased by customers.

30. **SCIENCE** Identify five types of natural resources that are extracted in the United States for use in manufacturing. For each, identify the leading states where the natural resources are extracted and important products for which the natural resource is needed.

31. **PUBLIC SERVICE** Most communities have nonprofit corporations that support education. Find out if one or more organizations is working to support your school. If so, contact a leader of the organization. Determine how the organization is structured, if it has articles of incorporation and bylaws, and its purpose. Find out how students in your school can support the organization through volunteer activities.
> > Linking School and Home

Identify people in your family and neighborhood who have ownership in a corporation through the purchase of stock. Interview them to determine why they decided to purchase stock, how they selected the stock they purchased, and what they do on a regular basis to check the performance of their company. Ask them what types of communication they receive from the company. Ask them to provide recommendations for students in your class about stock ownership.

> > Portfolio Activity

To provide tangible evidence of your learning about business organization, do the following:

**COLLECT** advertisements or other visual images of businesses that represent the various categories of businesses in the economy. Organize the advertisements into categories to demonstrate your understanding of each type.

**CREATE** a visual to show the variety of businesses in the U.S. and international economies. The visual should illustrate the importance of the various ownership structures of businesses.

**CONNECT** your visual to other items already in your class portfolio, or relate it to an important concept you learned in another class. Make the connection by preparing a one-minute presentation to explain the variety of types and ownership structures of businesses in the economy.

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**Prepared Speech Event**

Small businesses hire the greatest number of employees in the United States. Entrepreneurship and small business ownership have made the United States great.

You have decided to run for Congress. One of the hottest topics in your Congressional district is support for small business ownership. Your constituents want to know your plan to stimulate and support small business ownership. You must come up with a specific plan to encourage more minority and female business ownership. You are also challenged to develop a strategy to bring business back to the inner city. Entrepreneurs want to know the incentives for taking the risk of starting businesses in your Congressional district.

You will have three to five minutes to present your plan to strengthen and encourage small business ownership. Audiovisual equipment and visual aids may be used in this presentation.

**Performance Indicators Evaluated**

- Define demographics of your Congressional district.
- Explain the importance of small business ownership.
- Describe strategies to encourage/support increased small business ownership.
- Outline the greatest obstacles for small businesses to overcome.
- Explain how government assistance to small businesses will be monitored and improved.

You will be evaluated for your:

- Knowledge of the topic
- Organized presentation of the topic
- Confidence, quality of voice, and eye contact
- Relationship of the topic to business strategy

*For more detailed information about performance indicators, go to the BPA web site.*

**Think Critically**

1. Why is small business ownership important in the U.S?
2. What types of government programs or assistance will encourage more small business ownership?
3. Why is it important to meet with community and Congressional district leaders to develop a strategy that enhances small business ownership?

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http://www.bpa.org/
Chapter 6

Entrepreneurship and Small Business Management

6-1 Becoming an Entrepreneur
6-2 Small Business Basics
6-3 Starting a Small Business
Planning a Career in... Consulting

When businesses face unique problems or undertake major changes, they often turn to consultants for advice and help. Consultants are not long-term employees of a company, but are hired to complete a specific task or to focus on an important challenge facing the business. Consultants may be self-employed and work independently, or they may be part of a large consulting business that employs many specialists. Large companies often form teams of specialists to work with a client.

Consultants bring expertise to a business that may not exist among its employees and that would be difficult to develop quickly enough to solve a current problem. Consultants also may be more objective about the business than people who are working there. The primary work of consultants is to conduct research and complete other types of analysis that help businesses address important challenges they are facing. The consultant will often prepare written reports and plans, will provide advice to decision-makers, and may even offer help in reorganizing the company and redirecting its efforts.

Employment Outlook

- The employment outlook for business consultants varies by industry, but is generally growing at a better than average rate.
- Employment demand is based on the expertise and reputation of the individual consultant and the consulting business.
- Most consultants have expertise in organizational change, finance, technology, and management.

Job Titles

- Business Analyst
- Management Consultant
- Performance Consultant

Needed Skills

- Ability to problem-solve with innovative solutions
- Research and analytical skills
- Specialization in specific aspects of business operations and management
- Effective written and oral communication skills

What’s it like to work in... Consulting

Erin Gerrard works as a Small Business Consultant for Security Savings Bank. The bank is committed to strengthening its services to small businesses. Security employs a ten-person team to support its small business customers.

Erin has a degree in accounting, worked five years for a major accounting business, and then operated her own accounting service for five years. The bank asked her to work for them as a small business consultant because of her accounting expertise and reputation in the community. She decided the consulting opportunity would be an interesting challenge.

This morning, Erin is meeting with Dawn Perrot, who is planning to open a florist shop. Dawn has submitted a business plan, but the financial plan is incomplete. Erin is looking forward to helping Dawn gather information and develop a complete picture of the financial needs of her business. At 1 p.m., Erin and the bank’s information management specialist are visiting The Sherron Company to help them plan a new computerized payroll system.

What about you? How do you believe Erin’s work as a consultant is similar to and different from the work she did as the owner of a small accounting business?
An entrepreneur is someone who takes a risk in starting a business to earn a profit. Some key factors in starting your own business are having a real desire to be your own boss and developing a good initial plan. Having special skills and abilities and coming up with innovative ideas are also important.

Can you think of some service or product that is not being offered at this time but that could be in demand? Is there some service or product that you could offer more efficiently than others are doing now? Is there some special talent you have that could become the starting point for a business of your own? If so, you have the basis for a new business enterprise. There are good opportunities for entrepreneurship through small business ownership. Entrepreneurship is the process of starting, organizing, managing, and assuming the responsibility for a business. Here are some real-life examples of young entrepreneurs.

Entrepreneurs in Action
Pankaj Arora is a high school student from Rochester, Minnesota. He has a busy schedule of schoolwork and after-school activities. He also runs two business ventures. Using his advanced computer skills, Pankaj creates and
distributes software through his company, Pankaj Arora Software. He uses his second company, paWare, to design web sites and custom-build computers.

Rich Stachowski of Moraga, California, is an avid scuba diver. While enjoying his hobby, he recognized that he was unable to talk to others who were snorkeling with him. He put his imagination to work and invented Water Talkies™. These walkie-talkies can be used under water. Rich worked with a family friend who developed the manufacturing process. He then opened a business to make and sell his product before he was even a teenager. His Short Stack line of water toys is now sold by 100 chain retailers in the U.S. and several other countries.

Like many other teens in their Brooklyn, New York, neighborhood, Jeffrey Rodriguez and John Serrano enjoyed “graffiti art” that often appears on roadside sound barriers and building walls. Instead of painting their neighborhood, they combined their artistic abilities and business interests to open Latin Artist, a custom art studio. They use their airbrush equipment to create unique artwork for clothing, banners, building signs, and even automobiles. They now use part of their building space for a community art center. They allow local artists to display and sell their artwork.

Sometimes ideas for new products come from problems in daily life. Abbey Fleck was watching her father use a microwave oven to cook bacon one morning in their White Bear Lake, Minnesota, home. The bacon came out soaked in grease. Abbey had an idea to develop a pan that would cook the bacon while letting the grease drain out below. She and her father tested several designs that resulted in the Makin Bacon® microwave bacon tray. They were able to convince the producers of Armour brand bacon to sell the tray with an advertisement and order form printed on each package of bacon. The product was an instant hit. Abbey’s company, A de F, Inc., now sells over 600,000 Makin Bacon® trays each year.

The U.S. government is taking steps to support the more than 6 million women who own their own businesses. One of the resources is a new web site, Women Entrepreneurship in the 21st Century. Access businessxtra.swlearning.com and click on the link for Chapter 6. Read the latest news on women’s entrepreneurship. Review the types of resources that can be accessed through the web site. Locate other government web sites that provide information and help for people wanting to starting their own businesses.
The experiences of these entrepreneurs are examples of the thousands of young people who have creative ideas and turn them into businesses each year. Not all ideas lead to successful businesses, but each provides evidence of the opportunities that exist for people who believe they can turn their idea into a profitable business.

**What Does It Take?**

Not all people who own or manage a business are entrepreneurs. It takes unique skills and personal characteristics to develop a new idea for a product or service. A person must also have both the confidence and capability to turn it into a business.

Entrepreneurs come from all age categories and racial and ethnic groups. They represent both genders as well as varied amounts and types of education. Many entrepreneurs own their first business while in their teens. Others do not take the step until retirement. More business owners are male, but young entrepreneurs are more equally divided between male and female.

It is important to have an understanding of business operations and management. This understanding does not always come from getting a business degree in college. People learn how to run a business in many ways. They may work in a business or ask for help and advice from an experienced business owner. They may read and study on their own as well as in school.

There are personal traits that are common to successful entrepreneurs, as shown in Figure 6-1. While some people already have many of these qualities, others do not. If you have a desire to become an entrepreneur, you can work to develop these characteristics.

**Figure 6-1**

Do you believe you have the characteristics needed to be a successful entrepreneur?

<table>
<thead>
<tr>
<th>Personal Characteristics of Successful Entrepreneurs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Entrepreneurs are more</td>
</tr>
<tr>
<td>• persistent</td>
</tr>
<tr>
<td>• inquisitive</td>
</tr>
<tr>
<td>• energetic</td>
</tr>
<tr>
<td>• goal oriented</td>
</tr>
<tr>
<td>• independent</td>
</tr>
<tr>
<td>• self-confident</td>
</tr>
<tr>
<td>• creative</td>
</tr>
<tr>
<td>• reliable</td>
</tr>
<tr>
<td>• competitive</td>
</tr>
</tbody>
</table>
Entrepreneurship is a key part of the U.S. economy. Nearly one in ten of all Americans 18–64 years old is involved in some type of entrepreneurship activity. Over 500,000 new businesses are created annually. Entrepreneurship is also risky. Nearly as many small businesses close as begin each year.

Employment
About 40 percent of new business owners run their own businesses with no help. The other 60 percent have one or more employees. The number of employees in new businesses is shown in Figure 6-2.

Financing
Most of the money needed to start a new business comes from the entrepreneur and his or her family and friends. One in five Americans has invested in a business of someone they know well. Over 50 percent lend financial support for the business of a family member or relative. Twenty nine percent give money to neighbors and friends. Eight percent invest in businesses started by work colleagues. Family and friends invest over $100 billion in new businesses each year.

Another source of money for some new businesses is venture capital. Venture capital is money provided by large investors to finance new products and new businesses that have a good chance to be very profitable. In the late 1990s, many venture capital companies were formed. They supplied over $100 billion each year to new businesses.

Many of the businesses receiving those funds were e-commerce and high tech start-ups. When many of those businesses failed, the amount of venture capital declined to less than $20 billion in 2003. Over 2,000 companies receive venture capital each year. That shows that many people think new businesses provide a good investment opportunity. The other sources of financing for new businesses are loans from banks and financial institutions and credit given by businesses that sell products and services to the new business.

Productivity
New and small businesses produce a large volume of goods and services for the economy. Businesses with just a single owner and no staff account for over $600 billion in sales annually. Small businesses are responsible for nearly half of the U.S. gross domestic product each year. They account for 55 percent of all innovative products and services developed.

**Figure 6-2**
Almost half of new businesses have no employees.

<table>
<thead>
<tr>
<th>Number of Employees in New Businesses</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
</tr>
<tr>
<td>1–5</td>
</tr>
<tr>
<td>6–9</td>
</tr>
<tr>
<td>20 or more</td>
</tr>
</tbody>
</table>

> Recognize the importance of entrepreneurship in the economy.

**Checkpoint**
What personal characteristic are common to most successful entrepreneurs?

**Checkpoint**
What are the sources of financing that entrepreneurs use for their new businesses?
Describe opportunities and risks of entrepreneurship.

OPPORTUNITIES AND RISKS

When Jerelyn Frank was deciding whether she would open her own personal fitness business, she had to think about both the opportunities and the risks. Giving up a regular job and stable income is a difficult choice. As benefits, she will have personal control over her own business. She can take personal satisfaction if her idea develops into a successful, profitable company.

New Business Opportunities

The American private enterprise economy promotes innovation and new business development. Individuals are able to take the risk to start a new business. They can compete with other businesses to sell their products and services and make a profit. Consumers are always looking for new and better choices to meet their wants and needs.

Many opportunities are open to prospective entrepreneurs. The opportunities begin with the creation of new or improved products and services. An innovation is an invention or creation that is brand new. An improvement is a designed change that increases the usefulness of a product, service, or process.

Inventors often develop innovations. Those inventions may become the basis for a new business. The inventor may sell them to another company for development and sale. Examples of well-known innovations include the Apple personal computer developed by Steven Jobs and Stephen Wozniak and Post-it Notes created by Arthur Fry and Spencer Silver. Recent innovations that may become successful products include a miniaturized artificial heart, a virtual computer keyboard, and an optical camouflage system that allows people wearing a special reflective material to seem to disappear.

In addition to inventions, innovators create new services that become the basis for a business. Frederick Smith envisioned an economical worldwide system for quickly and efficiently shipping packages. The creation of FedEx was the result. After graduating from college, Paul Orfalea developed neighborhood walk-in photocopying centers known as Kinko’s. When the Internal Revenue Service no longer prepared individual tax returns for free, two brothers, Henry and Richard Bloch, created the H & R Block Company. They trained people to provide efficient low-cost tax preparation services to individual taxpayers.

Not all entrepreneurship opportunities emerge from those types of inventions and innovations. Many come from an improved design, more effective procedures, or greater attention to quality. Entrepreneurs are creative problem-solvers. Those traits lead to ideas for improved products and services.

Recognizing Risks

Many successful entrepreneurs and their businesses are well known. Their success encourages others to think about starting a new business. Developing a successful new business is not easy. Many more new businesses fail than succeed. The time and energy required of new business owners is much higher than most people expect.

The National Federation of Independent Business reports that of all new businesses, about one-third are profitable, one-third do not make a
Entrepreneurs need to be aware of the many risks they may face and prepare for them. Most entrepreneurs are willing to face risks. They will work hard to make their businesses succeed. However, many entrepreneurs have seen one or more of their business ideas fail before they are able to grow a successful company.

CHECKPOINT
Where do entrepreneurship opportunities begin?

6-1 Assessment

>> Key Concepts
Determine the best answer.

1. True or False. Everyone who owns or manages a business is an entrepreneur.

2. Which of the following is not a characteristic of entrepreneurship in the U.S.?
   a. About three percent of people aged 18–64 are involved in entrepreneurship activity.
   b. About 500,000 new businesses are created each year.
   c. Forty percent of new businesses have no employees.
   d. One in every five Americans has invested in a business of someone who they know well.

3. Money provided by large investors to finance new products and new businesses that have a good chance to be very profitable is known as
   a. a loan  b. credit  c. venture capital  d. start-up funding

4. True or False. The primary reason that businesses started by entrepreneurs close is disagreements with business partners.

>> Make Academic Connections
5. Math Ronaldo Jacarda is opening a manufacturing business. It will produce a new type of USB flash storage card for cell phones and digital cameras. He has several sources for the money needed to start his business. Those sources and amounts are personal savings, $56,500; loans from family and friends, $38,000; venture capital investment, $128,000; bank loan, $22,500. Determine the total amount of capital he has accumulated and the percentage of that total from each of the sources. Prepare a pie chart that illustrates the answers.

6. History Use the Internet to identify important inventions and innovations developed in the past fifty years. Select the five you believe have had the greatest business success. Now select the five you believe have been most important in improving society. Prepare a short report in which you identify and briefly describe each of the inventions and innovations you selected and justifications for your choices.
Small Business Basics

Goals

> Identify important characteristics of small businesses.
> Recognize the competitive advantages of small businesses.
> Identify problems faced by many small businesses.

Key Terms

small business
Small Business Administration (SBA)

Focus on Real Life

During dinner, Jasmine excitedly told her family what happened in her Intro to Business class. The class had spent the time thinking about opportunities for owning a small business. Jasmine knew that is what she wanted to do.

Jasmine’s grandfather said, “Did you know I ran a small business for almost ten years when I was young? I was as excited as you are about starting a business when I graduated from high school. I went to work for the owner of a small hardware store. I hoped that I could save enough money to open my own store. Luckily, after eight years, he decided to retire. We worked out an arrangement where I could buy the store from him over a number of years.”

“What happened to the business?” Jasmine asked.

“Being a small business owner is exciting, but it is a difficult life,” explained her grandfather. “As the bigger stores moved in, I found it more and more difficult to attract customers. I decided to sell the business. I’m excited for you, but I want you to know that your goals will be a challenge to achieve.”

SMALL BUSINESS OWNERSHIP

Business is often viewed as very large corporations. These companies employ thousands of people with locations all over the country and the world. That is not the true picture of most businesses. By far the greatest percentage of businesses in the United States is small businesses. Most people are employed by a small business.

You may be surprised by the definition of small business used by the federal government. According to the Small Business Administration (SBA), a small business is an independent business with fewer than 500 employees. Using that standard, 99.7 percent of the roughly 24 million U.S. businesses are small businesses.

A more specific description is

• The owner is usually the manager.
• It operates in one or very few locations.
• It typically serves a small market.
• It is not dominant in its field.

Most people would probably not consider businesses with 500 employees to be small. Even if you use a standard of fewer than 100 employees, 23 million businesses fit that description. Nearly 17.6 million businesses have no staff other than the owner. Many of those businesses are run on a part-time basis from the owner’s home. Fifteen million businesses are set up as proprietorships. No matter how you identify small businesses, they are by far the greatest number of businesses operating today.
Small Business Employment

Small businesses employ nearly 50 percent of all U.S. workers. On average, small businesses are responsible for creating 60–80 percent of all new jobs. Figure 6-3 shows some of the common types of small business. It is not surprising that there are a large number of service businesses. Many small business services are professional and technical. Many construction companies operate as small businesses.

Ownership Diversity

Women own over one-fourth of all small businesses. Over 16 percent of small businesses have African-American, Asian-American, or Hispanic-American ownership. The majority of small business owners are over 40 years old, but nearly 20 percent are under 25. Today, almost all people starting small businesses have at least a high school diploma. Nearly 30 percent have finished some college work.

Half of all small businesses are home-based businesses. Because many businesses are part-time ventures or service businesses, the owners report that

Why are so many small businesses in services and retailing?

Figure 6-3

Common Types of Small Businesses
on average they needed $5,000 or less to start that type of business. Full-time businesses with buildings, equipment, and employees may require well over $100,000 of initial capital.

**SMALL BUSINESS ADVANTAGES**

You need someone to mow your lawn, make a gourmet meal in your home for a few close friends, build a custom display case for a model train, or repair hardware on your home computer. Where would you turn for help? It’s not likely that you will find a large business for any of those services.

**Meeting Customer Needs**

Small businesses play a vital role in the economy. They often serve customers where the number of products and services needed is small or the requirements are too specialized for large businesses to make a profit. It is easier for a small business to meet the precise needs of customers than a large business. Even though a large business has more resources, to operate efficiently it must focus on products and services that meet the needs of a large group of customers. That makes it harder to satisfy the unique needs of single customers.

Small businesses often are not able to match the lower operating costs of larger businesses. They can compete by paying attention to their customers. Small businesses serve fewer customers and usually have more frequent contact with those customers than large businesses. They are more likely to be located close to the customer. They depend less on other businesses to distribute or service their products.

Large businesses often rely on consumer research to gather information. Small businesses usually get direct information from their customers about what they like and dislike.

**Providing Unique Services**

Small businesses are especially suited to provide unique services for customers. They may plan a wedding or design a customized sound system for your home. Providing those types of services means that business representatives must take a special interest in the customer. They spend time determining needs and discussing alternatives. They

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**CHECKPOINT**

What percentage of employees in the U.S. work for small businesses?

How do small businesses provide unique services that large businesses cannot?
have the expertise to plan and deliver the services that satisfy the customer. Large businesses may not find it profitable to spend that much time with each customer. Each employee that works with customers may not have the expertise to design the needed service.

Big business has a clear advantage when a large number of customers are willing to buy standard products and prefer low cost and efficient delivery. Small businesses gain an advantage when customers have unique needs, want more individual attention, and are willing to pay a bit more for the product or service to obtain what they really want. When asked, “What businesses do you believe are most concerned about you as a customer?,” the majority of consumers identify small businesses.

COMMON SMALL BUSINESS PROBLEMS
Not all small businesses succeed. In fact, their failure rate is much higher than larger businesses. Many failures result from the inability to pay expenses. The business is then forced to close. Some companies quietly go out of business when the owner believes that he or she is not doing well enough to continue. The owner may also get tired of the long hours and hard work.

Reasons for Failure
The following are the most common reasons for small business failure:
• Not keeping adequate records
• Not having enough start-up money
• Lack of management experience
• Lack of experience with the type of business
• Not controlling operating expenses
• Poor location for the business
• Failure to manage credit offered to customers

Work as a Group
Identify two or three small businesses in your community that have been successful for many years. As a group, discuss what you think they do that allows them to compete successfully with other small and large businesses.

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Small Business Assistance

With the right kind of assistance, small businesses can overcome each of the causes of failure listed above. Small-business owners can get help from a number of sources. Universities and colleges often have persons on their faculties who can give advice and support to people who are starting or have started their own businesses. Local groups of businesspeople, such as Chambers of Commerce, have members who can help others with business problems.

The Small Business Administration (SBA) is a government agency that helps small business owners develop business plans and obtain financing and other support for their companies. Information about the SBA and its services can be obtained by visiting www.sba.gov.

The SBA offers information, publications, counseling, and many other forms of support. The SBA sponsors the Service Corps of Retired Executives (SCORE). Members of SCORE are retired local businesspeople who volunteer their services to counsel and mentor new business owners.

Checkpoint

List common reasons for small business failure.

6-2 Assessment

Key Concepts

Determine the best answer.

1. The Small Business Administration considers a business small if it employs fewer than _?_.
   a. 5   b. 20   c. 100   d. 500

2. A competitive advantage that small businesses have over larger businesses is
   a. lower costs
   b. more consumer research
   c. lower prices
   d. attention to unique customer needs

3. Which of the following is not one of the reasons small business fail?
   a. poor customer credit practices
   b. the owner does not have adequate experience
   c. a poor business location
   d. not enough employees to do the work

Make Academic Connections

4. Technology eBay has become the home of many small businesses. Thousands of small business owners earn an excellent income by selling their products using the online auction services provided by eBay. Visit the eBay website and identify three ways a small business can use the web site to support its operations.

5. Communication Interview a small business owner who has operated his or her business for at least three years. Determine the factors that have contributed to success as well as the major challenges that have been faced. Prepare an audio or video “news report” on your interview.

6. Research Interview ten people who have recently purchased products or services from a small business. Ask them to list the top three reasons they made the purchase from a small business rather than a large business. Summarize the results from your interviews and present your findings in a table or chart.
Sharpen Your Life Skills

Writing with Technology

Today’s technology allows written communication to be exchanged at a much faster pace. Traditional forms of written communication, including letters, reports, and brochures, have not changed. However, when composed and completed, they can be sent to recipients in minutes using the Internet. Many uses of traditional written communication have been replaced by instantaneous informal communications including text messaging, instant messaging, and e-mail. The immediate nature of the technology as well as the informal approach to composing those messages often result in poor communication or even miscommunication. When you use technology for written communication, especially in business, a few basic rules will demonstrate to your recipients that they are important and you want to communicate effectively.

The two primary types of instant communication used in business are memos and e-mail messages. Memos are formal and used to convey more complex information. E-mail is more informal and used for direct and brief communication. Here are some important guidelines.

When Composing a Memo

1. **Know your audience.** Direct your memo to one person or a small group of people. Who needs the information? What do they need to know?
2. **Focus on one specific subject.** Make sure the subject is important to the audience. Specifically identify the subject of the memo. Do not stray into other topics.
3. **Select your words carefully.** Use language appropriate for the organization and understandable to your audience. Be clear, direct, and objective.
4. **Start strong.** Have an attention-getting first sentence. Focus the attention of the reader and get to the point.
5. **Provide only needed information.** Keep the memo brief, usually less than two pages, so it can be read in a few minutes. Before you end, be sure the information is complete.
6. **End effectively.** Identify any action needed and emphasize the importance of the information.

When Composing an E-mail Message

1. **Send only to the people who need the information.** Do not “reply to all” or use a mass e-mail list. Use e-mail for more individualized and specific messages.
2. **Use a specific subject line.** People get many e-mails. They can read and respond more efficiently if they can identify a clear subject.
3. **Provide a context.** If you are responding to an e-mail, briefly identify the information to which you are responding. Provide any information needed by the reader to understand your message.
4. **Don’t get caught up in the technology.** Avoid “flaming” with all caps or inserting emoticons, flashing text, or other gimmicks that detract from the information.
5. **Keep the message short.** An e-mail should be read in about a minute. If the message is longer, send it in a different format or add an attachment or link.
6. **Don’t write in haste.** You may regret an emotional message sent in haste. Consider the effect your message may have on the recipient.
7. **Even when informal, use effective writing skills.** Write in complete, active sentences, organize using paragraphs, and check your spelling.

Think Critically

1. When should you send a memo rather than an e-mail?
2. What are the communication problems that are most likely to occur when using instant communication methods?
Starting a Small Business

The Business Decision

Many people think about starting a business. Few actually do. The procedures followed to start a business often determine whether it will be successful. The process begins with an idea and concludes with a careful study of information to establish whether the idea can be successful.

An Idea Plus Experience

Every business begins with an idea. Business ideas come from many sources. Hobbies, interests, and business experiences often give people ideas for new businesses. Books and magazines suggest new business opportunities, including available franchises. Few people should think about starting a business without working for some time in a small business. Several years of training in a range of business operations will prepare you for the role of owner. Having responsibility for decisions and opportunities to manage people is a key part of that experience.

Right Place and Time

Putting your business idea into action means finding the right place to open the business. Most retail businesses need good customer traffic. If the business is not easy to find or requires a great deal of travel time, many potential customers will stay away. A wholesaler needs easy access to manufacturers where products are obtained for resale to other businesses.

Focus on Real Life

Jermaine Anderson turned his baseball card hobby into a business. He had a small store in a mall where he bought and sold collectors’ baseball cards and other baseball memorabilia. Jermaine began his business with a small loan from the bank and money saved from working while in college.

The business grew steadily each year. Jermaine prepared a specific budget at the beginning of each year. He was able to spend his money wisely on new inventory, advertising, and improvements to his store.

This year he used the same budgeting process that he had for the past four years. Based on last year’s results, he estimated that sales would increase 8 percent. He planned to increase expenses accordingly. Even with the increased expenses, the budget projected another nice profit.

The first two months of the year went well. Then the economy slipped into a recession. Customers cut back on their spending at his store. Jermaine’s sales were declining while his expenses continued to increase. Jermaine studied his budget to determine why he had problems in the fifth year when his planning had been so successful in the past.
Manufacturers must be located in an area with access to the raw materials used in manufacturing. Transportation systems must also be easy to reach for distributing finished products. Timing is another key factor in starting a business. Most successful businesses start during a period when customer demand for certain products or services is high.

**Team Approach**

Many small business owners are quite independent. They started their businesses because they do not want to take direction from other people. A business is not easy to start without the help of others. Even the smallest businesses need a few full- or part-time employees. The employees must be chosen carefully for their ability to work as a team. Choosing the “team” members becomes one of the most important initial business decisions.

In addition to employees, small business owners will need assistance from people with specialized business knowledge. These include bankers, lawyers, and accountants. If possible, the new owner should identify business professionals who focus on working with small businesses.

**Preparation and Research**

The most important step in starting a business is preparation. Preparation includes having enough information to make good decisions about the business. Time spent gathering and studying information before the business is started will save time and avoid later problems.

Information is needed about customers, competitors, important operations, government regulations, and many other topics. This information is available through libraries, colleges or universities, and small business assistance centers. At times, the new business owner will have to do further research to gather more current data. Information will help to make sure that decisions are made objectively.

**Work as a Group**

You are planning to open a small business that will rent bicycles, rollerblades, push scooters, and electric scooters by the hour for people to use for relaxation and exercise. As a group, identify three possible business locations in your community and discuss which location would be best for the business.
DEVELOPING A BUSINESS PLAN

When successful businesses are compared with those that failed, one factor stands out as the most important difference. The owners of successful businesses develop and follow a business plan. The owners of businesses that fail often do not have a business plan.

What Is a Business Plan?

A business plan is a written description of the business idea and how it will be carried out, including all major business activities. Key features of a business plan are a general description of the company, the credentials of the owner(s), a description of the product or service, an analysis of the market (demand, customers, and competition), and a financial plan. Most business plans are developed for one year and then updated for the next year. If the business owner needs help from others, especially for financing the new business, a business plan will usually be required. Figure 6-4 is an outline of the sections of a business plan.

Figure 6-4

Why are each of these elements important when planning a new business?

Elements of a Business Plan

Description of the Business
- the business idea
- major products and services
- ownership structure
- strengths/weaknesses
- long- and short-term goals

Description of Competition
- characteristics of the industry
- condition of the economy
- strengths and weaknesses of major competitors

Customer Analysis
- description of customers
- location, number, and resources of customers
- sales forecasts

Operations Plan
- organization of the company
- description of major operations
- analysis of resources needed
- human resource plans

Marketing Plan
- description of major marketing activities
- description of resources needed
- schedule of marketing activities

Financial Plans
- start-up costs
- short- and long-term financial needs
- sources of financing
- budgets and financial statements
Even if help is not needed, a business plan must be developed. By developing a plan, the owner is forced to think about important activities, the amount of time they will take, and their cost. That process may identify potential problems. The plan also serves as a guide to keep the business on track.

**Steps in Developing the Business Plan**

The business owner is in charge of developing the business plan. The most popular use of business plans is to persuade lenders and investors to finance the venture. A well-developed plan will lay out an idea and will require an owner to analyze his or her concept and make decisions about key business activities such as production, marketing, staffing, and financing.

Some owners hire someone to write the plan. Others get help from a bank or a local office of the Small Business Administration. Even if others are involved in developing the plan, the owner must be familiar with all of the information and make the major decisions for the plan.

The first step in developing the business plan is to gather and review information. If possible, the owner should review other business plans and study information on the activities and financial performance of similar businesses, especially potential competitors.

Next, the owner should develop the “game plan.” Alternative plans for production, marketing, staffing, and financing should be studied and identified.

The owner can select the best choices from the alternatives.

Finally, each section of the business plan should be written. A plan devotes sections to a general description of the business. The sections include the basic legal form of the organization and major products or services. Other sections detail the competition, potential customers, operations, marketing, and finances. Before the plan is completed, the owner should have other business experts review the plan and give their advice about its strengths and weaknesses.

**CHECKPOINT**

What is the “game plan” in a business plan?
FINANCING THE SMALL BUSINESS

A new business with a good product or service may run out of money before it can become profitable. Several years of operation are required before most new businesses earn a profit. Finding adequate financing is a key step in starting and running a new business.

Types of Financing

Three types of financing must be considered. **Start-up financing** is the amount of money needed to open the business. It includes the cost of buildings, equipment, inventory (products or raw materials on hand), supplies, licenses, and the like. **Short-term financing** is the money needed to pay for the current operating activities of a business. Short-term financing is obtained for a period of less than a year and often for one or two months. **Long-term financing** is money needed for the main resources of a business (such as land, buildings, and equipment) that will last for many years. These resources usually require large amounts of money and will be paid for over many years.

Sources of Financing

Finding the needed money may be the most difficult part of starting a business. The money required to start and operate a new business usually comes from a mixture of owner-supplied and borrowed funds. The source of owner-supplied money depends on the ownership structure.

E-Commerce in Action

Niche Marketing

The Internet provides an effective way for large companies to efficiently reach millions of customers. Retailers such as Walmart, Target, and Amazon and manufacturers like Dell Computer, Toshiba, and Symantec use their web sites to provide product information and take product orders from thousands of people each day.

The Internet is also valuable for companies that offer very specialized products that may attract only a few hundred or thousand customers. Those companies use niche marketing in which they appeal to customers with very specific and narrow interests.

They might not be able to be profitable if they had to rely on customers visiting their business location to make purchases. By using the Internet, those companies can reach worldwide to any customer seeking a unique product.

One such category of niche marketer is the bookstore. A number of bookstore web sites exist to serve people looking for very rare and out-of-print books. If you are seeking a signed copy of John Steinbeck’s *The Grapes of Wrath* or even a rare first edition copy of Dr. Seuss’ *The Cat in the Hat*, it can be located through the Internet. Be prepared to pay over $10,000 for either of these books.

**Think Critically**

1. Find and visit a bookseller’s web site. Use the search feature to locate a rare book title. List the title, author, and selling price as well as the name and location of the company offering the book.

2. Identify a business in your community that you would consider a niche marketer. What products do they offer, and who are the customers to whom they appeal?
In a proprietorship, one person will supply the money. In a partnership, the partners will each be expected to contribute. A corporation is owned and financed by the shareholders. Borrowed funds are obtained through loans from banks and other financial institutions or through funding provided by other people, such as family and friends. Often companies that sell equipment, materials, or inventory to a business will offer credit if the business does not have financial problems. A new business owner should be careful about accepting credit. The owner must take into account the cost of the credit and when payments are due.

>> CHECKPOINT
In addition to owner-supplied capital, what are several other sources of financing for a small business?

### 6-3 Assessment

#### >> Key Concepts

Determine the best answer.

1. Every business begins with a(n)
   a. customer   b. profit   c. idea   d. invention

2. True or False. Most small business owners enjoy being part of a team.

3. True or False. A business plan does not have to be written since the business owner is well aware of the information in the plan.

4. Money needed for the important resources of a business (such as land, buildings, and equipment) that will last for many years is called
   a. start-up financing
   b. short-term financing
   c. long-term financing
   d. credit

#### >> Make Academic Connections

5. **Technology** Locate an outline for a business plan on the Internet. Compare the sections of the plan you found with those in Figure 6-4. Develop a final outline using both resources. Write a two-sentence statement for each section of the outline describing why that section is important to a successful small business.

6. **Math** Gwen Osterhaus and Portia Juarez have formed a partnership to open a garden coffee cafe in Central Park. Gwen invests $23,000 and Portia invests $31,000. They get a micro loan from the Small Business Administration for $18,500. They have $9,000 of credit from the Bean Machine Company that sold them some of their equipment. Calculate the total amount of start-up financing available to the partnership. Make a pie chart that shows the percentage of total financing that is provided from each source. How much of the financing is owner supplied and how much is borrowed?
>> Business Notes

6-1 Becoming an Entrepreneur
1. Successful entrepreneurs have a real desire to be their own boss. They use special skills and abilities to come up with innovative ideas and then develop a good initial plan for a business. Entrepreneurs come from all age categories, racial and ethnic groups, and both genders, as well as varied educational levels.

2. Entrepreneurship is a key part of the U.S. economy. Money needed to start a new business may come from the owner, family, friends, or venture capital. Other sources of financing are loans from banks and financial institutions and credit given by other businesses. Small businesses are responsible for nearly half of the U.S. gross domestic product each year and 55 percent of all innovative products and services developed.

3. Opportunities open to entrepreneurs include the creation of new or improved products and services, an improved design, more effective procedures, or greater attention to quality. Risks include lack of adequate capital, low sales, higher than expected expenses, competitive pressure, an owner unprepared to manage a growing business, and operations that require more time than the owner is willing to commit.

6-2 Small Business Basics
4. In a small business, the owner is usually the manager, it operates in one or very few locations, it typically serves a small market, and it is not dominant in its field of operation.

5. Small businesses play an important role in the economy. They often serve customers where the number of products and services needed is small or the requirements are too specialized for large businesses to be profitable.

6. The most common reasons for small business failure are not keeping adequate records, not having enough start-up money, lack of management experience, lack of experience with the type of business, not controlling operating expenses, poor location for the business, and failure to manage customer credit.

6-3 Starting a Small Business
7. Factors that lead to a successful new business are an idea plus experience, the right time and place, a team approach, and preparation and research.

8. By developing a written business plan, the owner will think about important activities, the amount of time they will take, and their cost. The plan also serves as a guide to keep the business on track.

9. Obtaining adequate financing is an important step in starting and operating a new business. Three types of financing to be considered are start-up, short-term, and long-term financing. The money required to start and operate a new business usually comes from a mixture of owner-supplied and borrowed funds.

>> Communicate Business Concepts

1. What is a new product or service that could become the basis for a new business that fits your interests, hobbies, or special skills and abilities? What are some reasons you would be interested or not interested in becoming an entrepreneur?

2. Why do you believe that small businesses contribute more of the new jobs to the economy than large established businesses?

3. What are factors that you believe contributed to the success of the young entrepreneurs described in Lesson 6.1? Do you believe the idea for their product or service was more or less important than their personal characteristics?
4. How is the Internet changing the characteristics of small businesses? Do you believe the Internet can make small businesses more competitive with large businesses? Why?

5. Freddie is thinking about starting a small business and has come to you for advice. Using the reasons that most small businesses fail listed in Lesson 6.2, what would you tell Freddie that will help him increase his chances for being successful?

6. In most communities, there are several locations where retail businesses locate but soon fail. They are followed by other businesses that also fail. People say the pattern of failure is because of a poor location. Do you agree that the location is the most likely reason that the businesses fail? Why would a new business consider a location where a previous business has already failed?

7. Identify the three types of people you believe would be the most important to assist a new small business owner. Justify each of your choices.

8. If you were a banker reviewing a business plan to determine if you will provide financing, what information would be most important in determining if you would support the small business or not?

9. What are the advantages and disadvantages of hiring another experienced person to develop and write the business plan for the owner of a new business?

> > Develop Your Business Language

Match the terms listed with the definitions.

10. A government agency that helps small business owners develop business plans and obtain financing and other support for their companies.

11. Money provided by large investors to finance new products and new businesses that have a good chance to be very profitable.

12. The money needed to pay for the current operating activities of a business.

13. The amount of money needed to open the business.

14. An invention or creation that is brand new.

15. Someone who takes a risk in starting a business to earn a profit.

16. A written description of the business idea and how it will be carried out, including all major business activities.

17. Money needed for the important resources of a business (such as land, buildings, and equipment) that will last for many years.

18. An independent business with fewer than 500 employees.

19. A designed change that increases the usefulness of a product, service, or process.

20. The process of starting, organizing, managing, and assuming the responsibility for a business.

Key Terms

a. business plan
b. entrepreneur
c. entrepreneurship
d. improvement
e. innovation
f. long-term financing
g. short-term financing
h. small business
i. Small Business Administration (SBA)
j. start-up financing
k. venture capital
Decision-Making Strategies

David Obolski completed a community college program in Small Business Management. He now wanted to own his own florist business. He had worked for Flower-a-Bunda during high school and college. In addition, he was able to save almost $20,000 toward starting his own business. However, he knew that he would need more than $20,000 to buy a florist shop. He would need almost double that amount to qualify for the necessary loans to start up the business. David studied three ways he might start his business.

a. He could find a partner to provide the additional cash.

b. He could work for the owner of Flower-a-Bunda until she retired in seven years and buy the business with his accumulated savings.

c. He could purchase a franchise for an investment of $20,000. However, David would have to pay a franchise fee of 6 percent of total sales each year to the franchisor.

21. What are the advantages and disadvantages of each route to small business ownership for David?

22. If you were David, which choice would you make? Why?

Make Academic Connections

23. TECHNOLOGY Use the Internet to identify the number of small business owners by race or by age. Then enter the information in a spreadsheet program and calculate the percentage of all small business owners represented by each race or age classification. Then use the graphing function to create a chart or graph illustrating the results.

24. COMMUNICATION Many small business owners obtain some of their start-up financing from family members and friends. Assume you are starting a small Internet business that will develop and maintain low-cost web sites for local organizations, clubs, and nonprofit groups. You have $2,500 of your own money to invest and need to raise an additional $5,000. Develop a letter or one-page brochure that you can use to interest family and friends in investing $500 or more in your new business. Make sure it is persuasive and tells them what benefits they will receive from their investment.

25. PERSONAL DEVELOPMENT The characteristics common to most entrepreneurs are listed in Figure 6-1. Create a table with three columns. In the first column, list each of the characteristics. In the middle column, describe things you have done (hobbies, work, projects, activities) that provide evidence of each characteristic. In the final column, list additional things you can do in the next five years to further develop the characteristic.

26. GOVERNMENT The federal government and most state governments provide many resources as well as financial support for small businesses. Use the Internet to locate two agencies of the federal government that provide services developed specifically for small businesses. Then search the web site for your state’s government and locate one state agency that provides small business services. Prepare a three-paragraph report on each of the agencies you identified in which you describe the agency, the services provided, and how a new business can qualify for the services.

27. ECONOMICS The U.S. Census Bureau maintains information on the number of businesses and amount of business activity in every county of each state. Use the Internet to visit the U.S. Census Bureau web site (www.census.gov). Use the search engine on their web site to locate “County Business Patterns.” When you have accessed that web page, enter the name of your state and then the county in which you live. Find data on the number of businesses with one to four employees in your county. List the total number of businesses of that size, the five industries with the most businesses employing fewer than five employees, and the total number of establishments in each of those industries.
> > Linking School and Home

Select five family members or neighbors and meet with each person to compare their experiences as consumers with small businesses and large businesses. Ask them to describe the reasons they prefer to buy from small businesses and the reasons they prefer to buy from large businesses. Then ask them to describe the disadvantages of each. Summarize the results of your discussions in a chart or short written report.

> > Portfolio Activity

To provide tangible evidence of your learning about entrepreneurship and small business management:

**COLLECT** data and other information that describe the role of entrepreneurship and small businesses in the economy.

**CREATE** a visual to illustrate the contributions small businesses make to the economy and to communities.

**CONNECT** your visual to other items already in your class portfolio, or relate it to an important concept you learned in another class. Make the connection by preparing a one-minute presentation on the importance, benefits, and risks of small business ownership.

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**American Enterprise Project**

The United States takes great pride in the American enterprise system, which encourages individuals to take the risk of starting a business.

Consumers play an important role in the American enterprise system. Their demand for goods and services influences which businesses will be successful. Business success depends upon paying attention to consumer demand.

Your team of three individuals has been challenged to design a presentation that teaches elementary students about the American enterprise system. Your presentation should teach students about supply and demand and the American dream of owning a business. The presentation should include active participation of the elementary students.

You will create a business report with substantiated statements in a clear and concise format. Creativity through design and use of meaningful graphics is encouraged. The report should be a clear presentation about the American enterprise system and your strategy for teaching elementary students key concepts. The report should include the following parts: Purpose of project, Research into school and/or community needs, Description of project, Uniqueness of project, and Evaluation and results. The format of your report will be evaluated for clear and concise presentation with logical arrangements of information; creativity in presentation; and correct grammar, punctuation, spelling, and acceptable business style.

**Performance Indicators Evaluated**

- Understand the major concepts about the American enterprise system.
- Present an effective lesson to elementary students.
- Highlight measurable results from the American Enterprise Project.
- Reach goals for the American Enterprise Project.

For more detailed information about performance indicators, go to the FBLA web site.

**Think Critically**

1. Why is it important for young Americans to understand the American enterprise system?
2. List two strategies to use during the presentation that will hold the attention of elementary students.
3. List five major concepts that elementary students must understand about the American enterprise system.
4. What would be a good joint project between FBLA/BPA members and elementary students to strengthen understanding about the American Enterprise System?

http://www.fbla-pbl.org/
Chapter 7

Management and Leadership

7-1 Management
7-2 Leadership
7-3 Ethical Management
Planning a Career in...

Management

Management is the goal of most people who enter business careers. The chance to move up in a business and contribute to major decisions is viewed as a challenging goal for many people. Managers are key to the success of a company. Management opportunities are vast. They exist in all companies and every part of a business. Whether your interests are in finance, marketing, information management, engineering, or human resources, you can become a manager. You can begin a management career as a team leader, supervisor, or assistant manager after only a few years of experience. You can move up in the company to become a mid- or top-level manager with additional experience and education. Your career advancement will be based on your performance as a manager and your contribution to the business’ success.

Employment Outlook

• The employment outlook for management jobs is varied, with some high-growth areas and other areas facing increasing competition.
• Mid-level management jobs are more competitive as companies reduce the levels of management and move more decision-making and responsibility to employees.
• Entry-level management positions as supervisors or assistant managers are plentiful but often low paying. They usually combine limited management responsibilities with regular job duties.

Job Titles

• Assistant
• Coordinator
• Leader
• Supervisor
• Department Head

Needed Skills

• Financial and data analysis skills
• Oral and written communication, listening, and human relations skills
• Leadership and decision-making skills
• Understanding and use of technology with expertise in standard business software

What’s it like to work in...

Management

Frank faced a number of challenges as he sat at his workstation Monday morning. He is the supervisor of a production line at the Emprex Corporation. Frank had to interview nine people to fill three full-time jobs and one part-time job. He had to meet with his team to let them know they would have to work at least 10 hours of overtime each week for the next two months to meet their quota. He knew they would be happy with the extra money but would be giving up a lot of free time. Frank was also challenged by some budget problems. While he didn’t have full authority over the budget, his manager had warned him that costs were going up, which meant every supervisor had to find ways to reduce. Frank knew that some employees wasted supplies and materials and would have to be watched more carefully. Finally, Frank had to complete one of his least favorite duties. An employee had not met expectations and had to be fired. Frank had a meeting scheduled at 3 p.m. with the employee to break the news.

What about you? What would you find the most and least enjoyable about Frank’s work?
ROLE AND WORK OF MANAGERS
Managers are responsible for the success or failure of a business. Managers will receive recognition and other rewards if the business meets its goals. They will also be held accountable if those goals are not met. People who want to experience the risks and rewards of business become managers.

Who Is a Manager?
Management is the process of accomplishing the goals of an organization through the effective use of people and other resources. Managers make things happen in business. The entrepreneur who develops the idea for a new business is a manager. The chief executive of an established firm who decides how to compete in a changing international market is a manager. Supervisors with responsibility for the work of a small number of employees are managers, as are vice presidents with more than 100 employees reporting to them.

What Do Managers Do?
Every manager has specific job duties. Managers must complete similar activities no matter what the size or type of business. Managers’ work can be organized within five functions. Those functions are planning, organizing, staffing, implementing, and controlling.

- **Planning** involves analyzing information, setting goals, and making decisions about what needs to be done.
- **Organizing** means identifying and arranging the work and resources needed to achieve the goals that have been set.
- **Staffing** includes all of the activities involved in obtaining, preparing, and compensating the employees of a business.
- **Implementing** is the effort to direct and lead people to accomplish the planned work of the organization.
Controlling determines to what extent the business is accomplishing the goals it set out to reach in the planning stage.

Large corporations have many managers. Duties for specific management functions are assigned to each manager. Often, due to the size of a business, several managers may have individual responsibilities within just one of the functions. The management functions are usually divided among the owners of a partnership. Each owner works with functions he or she enjoys and performs well. In a new small business, the owner usually is responsible for all of the management functions. As the business grows, other employees will be moved into management positions. They will be assigned one or more of the management functions to complete.

Managing a business or even a part of a business is a very complex process. Managers must make decisions, solve problems, respond to competition, and develop new strategies. Decisions made to complete one management function affect all other functions. The efforts of each manager impact the work of others and the results achieved by the business. Effective managers motivate employees to do their best work. They also use the money and other resources of the business wisely. Successful businesses have managers who are able to complete each of the management functions well.

MANAGEMENT LEVELS

Unless a business is very small, there will be several managers with responsibilities for leading the business. Every manager completes all of the management functions and has authority over other people and their work. Not every manager gives the same amount of attention and time to each of the functions. Most organizations have three levels of managers—executives, mid-managers, and supervisors.

Top Management

Executives are top-level managers with responsibilities for the direction and success of the entire business. They set long-term direction and plans. They are held accountable for the profitability of the business.
and success of the business. Job titles of executives include chief executive officer, president, chief operating officer, and vice president.

Executives spend most of their time on planning and controlling activities. They study the economy and competition. They are responsible for all major business communications. All other managers report to executives.

Mid-Management

Mid-managers are specialists with responsibilities for specific parts of a company’s operations. Examples of mid-management jobs are marketing manager, information technology manager, customer service manager, operations manager, and human resources manager. They take the business plans developed by executives and prepare specific plans for their part of the business. They must coordinate their work with other managers. Much of their time is devoted to the organizing, staffing, and implementing functions.

Supervisors

Supervisors are the first level of management in a business. They are responsible for the work of a group of employees. Supervisors often have non-management duties in addition to their management work. They plan the day-to-day work of the employees they supervise. They make sure that needed resources are available and used wisely. Supervisors often evaluate the work of their employees and solve problems that occur in their area. Supervisors spend most of their time implementing the plans of executives and mid-managers.

Management by Others

Employees who are not managers complete work that seems to be a part of one of the management functions. Employees plan and organize their work. They might take part in hiring and training new employees. They may evaluate the quality of the work they complete. Managers are responsible for the work of others and have authority over those employees. Without that authority and responsibility, the work of an employee is not considered part of management.

Some experienced employees are asked to serve as leaders for their work group. They may be asked to lead a particular project or supervise the work of a new employee.

Many companies are now organizing work teams. They are giving the teams both authority and responsibility for much of their work. The team meets to make plans, determine how work will be completed, and divide the work among the team members. The team is responsible for meeting objectives and may even have some control over their budget. The team will still report to a manager and can ask for that person’s assistance when needed.

Both work group leaders and employee teams are completing a limited number of management activities. Both of those situations are an effective way for employees to have experience with several management activities. They can develop the skills needed by managers and decide whether they are interested in a management career.

FYI

The glass ceiling for women in management still exists when it comes to leading large corporations. As of 2000, only eight women headed Fortune 1000 companies, with four women leading Fortune 500 businesses. Carly Fiorina was named CEO of Hewlett Packard in 1998, making her the first female to lead a Fortune 50 company.

CHECKPOINT

What are the differences among the three levels of management?
MANAGEMENT STYLES
Managing a group of people is a very difficult job. It is not easy to get people with different backgrounds, personalities, and experience to work well together. Have you been a part of an athletic team or musical group? If so, you can remember how hard it was at first to coordinate the talents of each group member so the team or group performed well.

Managers approach the task of directing a group in different ways based on their management style. Management style is the way a manager treats and involves employees. Two very different styles often used by managers are tactical management and strategic management.

Sometimes a management style is chosen based on the characteristics of the employees being managed. At other times, the choice is based on the work assignment. Figure 7-1 describes situations where each style will be more effective. Experienced and effective managers can change their management style. It should be based on the urgency of the work to be done and the confidence the manager has in the employees.

Tactical Management Sometimes managers are faced with a crisis. They feel they don’t have time to let the group decide how to complete the task. In other situations, a manager may be working with a group of new employees or may have work for which the members have no previous experience. In those situations, the manager should use tactical management. Tactical management is a style in which the manager is more directive and controlling. The manager will make the major decisions and stay in close contact with employees while they work to make sure the work is done well.

Strategic Management When a group of employees is experienced and work well together, a manager does not

<table>
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<tr>
<th>Choosing a Management Style</th>
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<tr>
<td>A manager should use tactical management when</td>
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<tr>
<td>- Working with part-time or temporary employees</td>
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<td>- Working with employees who are not motivated</td>
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<td>- Working under tight time pressures</td>
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<td>- Assigning a new task for which employees are not experienced</td>
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<td>- Employees prefer not to be involved in decision-making</td>
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> Discuss when to use the two management styles.
have to be as directive and controlling. If there is enough time to bring a team together to help plan a work assignment, team members will usually prefer being involved in the decision-making process. These are examples of strategic management. Strategic management is a style in which managers are less directive and involve employees in decision-making. A manager using a strategic style will trust employees to work without direct supervision and will seek their advice on important decisions.

**Mixed Management** Which of the two management styles would you prefer if you were an employee? If you were a manager, which of the styles would you use? Do you believe everyone would answer those two questions the same way? In the past, many managers used the tactical style of management. They believed they were responsible for getting work done and thus needed to be directive and controlling. That often led to employee frustration because they felt their manager did not trust them. Some employees prefer that the manager make day-to-day decisions. Other employees are not experienced enough to work without close supervision. As a result, effective managers are prepared to use both styles. The combined use of tactical and strategic management is known as mixed management.

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**Assessment**

**Key Concepts**

Determine the best answer.

1. True or False. An entrepreneur who starts a new business is not considered to be a manager.

2. Which of the following is not one of the five functions of management?
   a. planning
   b. implementing
   c. producing
   d. controlling

3. Which level of management spends most of its time completing planning and controlling activities?
   a. top management
   b. mid-management
   c. supervisors
   d. team management

4. True or False. Effective managers should use strategic management rather than tactical management.

**Make Academic Connections**

5. **Research** Use the Internet or library to identify and gather information on the top executive of a large corporation or an entrepreneur. Prepare a report on the manager, describing the person’s career path to his or her current position. Identify the important responsibilities of the executive in leading the company.

6. **Careers** Study the classified advertising section of a newspaper or an employment web site. Identify three management job listings. One of the listings should describe a top management position, another a mid-management position, and the third a supervisor position. Develop a table that lists the main duties the person in each position needs to perform. Classify those duties within the five management functions.

7. **Critical Thinking** Imagine you are managing a team of students that is running the snack bar at a basketball game to raise money for your DECA chapter. List two situations that could occur for which a tactical management style would be most appropriate and two other situations when a strategic style would be most appropriate. Discuss the situations with other students and see whether they agree with your decisions.

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**CHECKPOINT**

How is tactical management different from strategic management?
In 1994, South Africa celebrated the arrival of democracy. After decades of apartheid, the government policy that separated blacks and other non-whites from the dominant whites, voting rights were extended to all citizens. Today, the country is often seen as a model for developing economies and emerging markets.

South Africa supplies two-thirds of the electricity used on the African continent. The country has modern seaports, roads, and airports, and is one of the fastest growing countries for mobile communications. This infrastructure makes South Africa one of the best locations for business activity.

The African Growth and Opportunity Act (AGOA) has provided South Africa and other African countries with expanded trade with the United States. AGOA reduces many import taxes and offers incentives for U.S. companies to invest in Africa.

In a business meeting, expect a slow process as you gain the confidence of local businesspeople. While South Africa has eleven official languages, English is most widely used in business activities. The different languages reflect many cultures. Some decision makers may consult with family members before finalizing an agreement. When negotiating, don’t be too pushy. Hard-nosed bargaining is not a part of most South African cultures.

Meals at home and away are often a sociable and shared occasion. The foods of South Africa are influenced by the many local, European, and Asian cultures that are part of the country’s heritage. A traditional dish is a vegetable and beef stew with a tomato base that may also include pumpkin or cabbage. European foods include a prego roll, a steak sandwich in crispy Portuguese-style bread. Indian and Chinese foods can be found in immigrant communities of people from those countries.

Think Critically
1. What elements of the South African economy make it an attractive location for trade and foreign investment?
2. How does culture affect business activities in South Africa?
3. Conduct library or Internet research to obtain additional information about the history and economic activities of South Africa.
WHAT IS A LEADER?
A business uses many resources to accomplish its work and make a profit. Those resources include buildings, equipment, money, materials, supplies, and people. One of the most important responsibilities is managing people. Managers have often been very good at managing things but not as good at managing people. Because people are often the most important resource of a business, managers who can effectively manage people are in high demand.

Need for Leadership
The management of people has changed in recent years. In the past, it was thought that if the manager wanted something done, he or she just had to tell the employees and they would do as they were told. Experience has shown differently. When employees feel that they are not involved in decisions and are not valued by the business, they will not be as committed to the work.

It is often said that people are the most important resource of a business. The cost of hiring, training, and paying employees is usually one of a business’...
highest expenses. If employees are not satisfied, they might not perform the work correctly, may not treat customers well, or may quit. That will require the company to hire and train new employees. Today, managers are expected to do more than just give orders. They must involve employees and find ways to meet employee needs as well as business needs. Managers must be effective leaders.

**Leadership** is the ability to motivate individuals and groups to accomplish important goals. When a manager can get individual employees and groups to work well together to accomplish objectives, she or he is an effective leader.

**Leadership Characteristics**

Leadership is much more than just being friendly with employees. It takes skill to get people with different backgrounds and personalities to work well together and do the work needed by the business. The characteristics of effective leaders are listed in Figure 7-2.

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**FYI**

According to the Conference Board, the four things that most often result in leadership failure are unwillingness to take risks, being arrogant and insensitive, using a controlling style, and avoiding difficult people issues.

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You may have heard, “Leaders are born and not made.” However, most leaders report that they did not always have the characteristics needed for success. Rather, they worked hard over many years to develop them.

It is harder for some people to develop leadership skills. You may be shy and find it hard to work with others. You may prefer to let others make decisions while you work to make those decisions successful. On the other hand, you may have friends who seem to have already mastered many leadership characteristics. They always seem to be willing to take control, take a risk, or make a hard decision. Others look to them for direction and ideas.

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Can you identify people who have most of these leadership characteristics?

<table>
<thead>
<tr>
<th>Characteristic</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Understanding</td>
<td>Respecting the feelings and needs of the people they work with.</td>
</tr>
<tr>
<td>Initiative</td>
<td>Having the ambition and motivation to get work done without being asked.</td>
</tr>
<tr>
<td>Dependability</td>
<td>Following through on commitments.</td>
</tr>
<tr>
<td>Judgment</td>
<td>Making decisions carefully.</td>
</tr>
<tr>
<td>Objectivity</td>
<td>Looking at all sides of an issue before making a decision.</td>
</tr>
<tr>
<td>Confidence</td>
<td>Being willing to make decisions and take responsibility for the results.</td>
</tr>
<tr>
<td>Stability</td>
<td>Not being too emotional or unpredictable.</td>
</tr>
<tr>
<td>Cooperation</td>
<td>Working well with others, recognizing others’ strengths, and helping to develop effective group relationships.</td>
</tr>
<tr>
<td>Honesty</td>
<td>Being ethical in decision-making and treatment of others.</td>
</tr>
<tr>
<td>Courage</td>
<td>Willing to take reasonable risks and make unpopular decisions.</td>
</tr>
<tr>
<td>Communication</td>
<td>Able to listen, speak, and write effectively.</td>
</tr>
<tr>
<td>Intelligence</td>
<td>Having the knowledge and understanding needed to perform well.</td>
</tr>
</tbody>
</table>
Preparing to Be a Leader

You do not have to be a manager to be a leader. You don’t have to wait until you become a manager to develop leadership skills. There are several ways you can develop them, including:

• **Study leadership.** Many books on the subject of leadership and leadership skills can help you understand what it takes to be a leader. You can also take courses to develop specific leadership skills.

• **Participate in organizations and activities.** Clubs, teams, and organizations offer occasions to develop leadership skills.

• **Practice leadership at work.** If you have a part-time job, you can develop leadership skills as you help customers, complete work assignments, take initiative to solve problems, and demonstrate dependability and honesty.

• **Observe leaders.** Every day you can observe people in leadership positions. Some are effective, while others are not.

• **Work with a mentor.** An older brother or sister, a trusted adult, a teacher or coach, or your supervisor at work may be willing to help you learn about leadership skills.

• **Do a self-analysis and ask for feedback.** Find opportunities to show leadership characteristics. Review the results to identify what you did well and what you can improve. Ask others for constructive feedback.

**checkpoint**

What are several ways to develop leadership skills?

**Importance of Human Relations**

Managers and leaders must be able to work well with other people. Surveys show that for many managers, more than half of their time is spent interacting with people. They work with employees, customers, people from other businesses, and other managers in their own organizations. Human relations largely determines whether a manager is successful or not. **Human relations** is the way people get along with each other.

**Human Relations Skills**

Effective managers and leaders must be able to get along well with all of the people with whom they work. In addition, they must help their employees develop effective human relations skills. The important human relations skills needed by leaders and managers are 1) self understanding, 2) understanding others, 3) communication, 4) team building, and 5) developing job satisfaction.

**Self Understanding** To be able to meet the expectations of others, leaders must first understand their own strengths and weaknesses. A manager
cannot always do exactly what employees would prefer or make decisions with which every employee agrees. In addition, a manager cannot be viewed as either unpredictable or unfair. To improve your human relations skills, study how you get along with others. Try to recognize the ways you communicate and work with others individually and in groups. It is important to understand how you make decisions. You must learn which decisions were effective and which were not so you can improve your decision-making ability over time.

Understanding Others Leaders recognize that people in a business often are more alike than different. Recognizing those similarities will help develop a stronger team. Differences can also improve a business. If everyone thought and acted the same, there would seldom be new ideas or anyone to question a decision in order to improve it. An effective leader gets to know each person’s skills and abilities as well as strengths and weaknesses. The leader will not treat everyone alike, but will attempt to involve each person in the way that is most beneficial to the business and that employee.

Work as a Group

List the five human relations skills and rank them 1–5 in the order you believe is most important to effective management. Now compare your rankings with those of your team members. As a group, agree on a final ranking of the skills. When you are finished, discuss whether the process used to agree on rankings demonstrated effective human relations skills or not.

Technology Topics

Assistive Technology for Disabilities

People with physical disabilities face special challenges when completing many personal and job functions. Today, assistive technologies are making many tasks possible that previously were difficult or impossible to complete. Assistive technology is any unique equipment, modification, or special design used to increase, maintain, or improve the capabilities of persons with disabilities. Companies benefit when providing assistive technology for disabled employees. The technology allows the employee to be productive, often at a level equal to non-disabled employees.

The computer industry has developed unique applications so that individuals with disabilities can use computers. For blind persons, software is available that gives audio signals for on-screen images such as windows, menus, icons, and cursor location. A computer can also become a translator for the blind by converting printed pages to speech or Braille. Touch-sensitive Braille displays mechanically lift small rounded plastic or metal pins as needed to form Braille characters. The user reads a line of Braille letters with his or her fingers and then refreshes the display to read the next line. In the same way, a device can monitor computer sounds and alert a deaf computer user with light signals.

Special applications have been designed for people with other physical disabilities. Low-pressure, touch-sensitive keyboards can make typing easier, and special seven-key keyboards are designed primarily for one-handed typists. Special keyboard designs can customize each key’s size, position, and function. Switch-operated or on-screen keyboards allow typing with almost any part of the body. In addition, joysticks, writing pads, and even remote-controlled mice can replace the standard mouse when the physical disability requires it.

Think Critically

1. In what ways does a company benefit when it provides assistive technologies for employees with disabilities?
2. What other uses can you see for the technologies described in addition to benefiting physically disabled employees?
Communication

Communication is very important in business. Managers must have effective communication skills. Various types of communication can be classified as follows:

- **Formal or informal** Formal communications methods have been established and approved by the organization. Informal communications are common but unofficial ways that information moves in an organization.

- **Internal or external** Internal communications occur between managers, employees, and work groups. External communications occur between those inside the organization and outsiders such as customers, suppliers, and other businesses.

- **Vertical or horizontal** Vertical communications move up or down in an organization between management and employees. Horizontal communications move across the organization at the same level—employee to employee or manager to manager.

- **Oral or written** Oral communications are word-of-mouth. Written communications include notes, letters, reports, and e-mail messages.

Managers need to recognize the many ways that communication occurs in the business. They must be able to use all types of communication effectively. Communication must use words that are understandable and meaningful to the people receiving the communications. They must be specific. An effective communicator must be a good listener as well as skilled at providing information. Listening helps managers understand employees and demonstrates that the manager respects their ideas.

**Team Building** Businesses are made up of groups and teams, not individuals. The combined skills of the people in a team are greater than that of individuals working alone. On the other hand, if there are problems in the team and members cannot get along, the team will not be effective. Managers need team-building skills to help people understand each other and their responsibilities. Managers should be able to identify any problems within the group and help solve the problems quickly.

**Developing Job Satisfaction** Most people are more satisfied than dissatisfied with their work because they have jobs that use their skills and interests. The jobs also provide needed income and benefits. Managers can influence how employees feel about their jobs on a daily basis. Sources of dissatisfaction include assignments employees do not like, poor working conditions, ineffective communication, and lack of recognition. Daily difficulties can lead to long-term dissatisfaction. On the other hand, when a manager pays attention to the needs and concerns of individual employees, they appreciate that effort.
INFLUENCING PEOPLE

Have you been a part of a group that seldom agrees on what should be done and spends a long time making decisions? It is interesting to see what the leader of a group does when the group is not working well. Some leaders will complain and criticize group members. Others will give up on the group and attempt to do the work themselves. Neither of those responses improves the group’s effectiveness. Effective leaders must be able to influence members. Influence enables a person to affect the actions of others.

Kinds of Influence

There are several kinds of influence a leader can use. Position influence is the ability to get others to accomplish tasks because of the position the leader holds. If the leader can influence an employee’s job rating, wages, and chances for promotion, it is likely that the employee will respond to the leader’s requests.

Reward influence results from the leader’s ability to give or withhold rewards. Rewards may be in the form of money or job benefits. Rewards can be non-monetary, such as recognition and praise. Leaders can use rewards in a negative way by requiring people to work overtime or by criticizing rather than praising employees.

Expert influence arises when group members recognize that the leader has special expertise in the area. Suppose a group of inexperienced salespeople have a manager with years of successful selling experience. They will likely look to the manager for guidance.

Identity influence stems from the personal trust and respect members have for the leader. If the leader is well liked and is thought to have the best interests of the group in mind, members are likely to support the leader.

The influence of leaders is not always positive. It may not be effective for a long period. If a manager is not viewed as an expert and is not well liked, he or she will have to rely on position and reward influence. It is not easy to continue to get people to do things for you just because you are their manager. They will probably do just enough to get by, get a reward, or avoid punishment. Most leaders try to develop expert and identity influence.

Formal and Informal Influence

How does a person influence a group to accomplish important goals? It may depend on whether you are a manager or not. Managers have formal influence. Others in the organization can have informal influence.

Think of a manager, coach, or teacher you’ve enjoyed working with. What characteristics made it easy to follow his or her lead?
What happens when your teacher assigns a group project and the team members get together for the first time? Usually one or two people emerge as leaders to help get the group focused and organized. That is known as informal influence because the leadership role is not part of a formal structure. Consider another situation where members of Student Council meet for the first time. There are bylaws that call for the election of officers. The person elected president has formal influence because the leadership position is part of the organization’s structure.

Often in organizations, both formal and informal influence will operate at the same time. One person will be the manager and have formal influence. There may be a well-liked and respected employee in the group. That person will have informal influence. If there is a conflict between the formal and informal influence, the group will probably not work effectively. Group members will have difficulty deciding whose influence to follow. Effective managers recognize informal influence and work closely with the informal leaders to gain their support and avoid conflicts.

**Assessment**

**Key Concepts**

Determine the best answer.

1. It is often said that the most important resource of a business is
   a. cash  
   b. technology  
   c. customers  
   d. people

2. True or False. Research has proven that effective leaders are born and not made.

3. The way people get along with each other is known as
   a. human relations  
   b. influence  
   c. management style  
   d. communications

4. A person who is not a manager but is still able to get a group focused and organized is using
   a. tactical management  
   b. strategic management  
   c. formal influence  
   d. informal influence

**Make Academic Connections**

5. **Technology** Virtual teams are groups that complete a project by communicating using technology rather than meeting face to face. Complete Internet research on virtual teams. Prepare a report that describes a project completed by a virtual team. Discuss how technology was used to support communication among team members and successful completion of the project.

6. **Communication** You are the supervisor of a new employee having difficulty completing some tasks. You believe the new employee may be reluctant to ask questions of experienced employees. You encourage your employees to help each other when asked. You want to meet with the new employee to discuss the situation and want the discussion to be positive and result in improved performance. Role-play the discussion with another student using effective oral communication.

7. **Math** A survey of one company’s employees asked them to identify which type of influence their managers used most often. Seven hundred employees responded with the following results: Position influence, 305 responses; reward influence, 80 responses; expert influence, 120 responses; identity influence, 195 responses. Prepare a chart that illustrates the percentage of managers using each of the types of influence the most often.
Ethical Management

Goals
> Justify the need for ethical management.
> Identify the role of leaders in increasing ethical behavior.

Key Terms
- ethical business practices
- core values

Focus on Real Life

The news has been full of information about corporate executives who acted unethically, resulting in the failure of their businesses, loss of employees’ retirement savings, and millions of dollars in losses for shareholders. These events suggest that the leaders of businesses operate illegally and unethically with no regard for anything except their personal financial success.

Most executives have a strong personal and professional code of ethics. They insist that their companies, managers, and employees reflect those same values.

*Business Ethics* magazine identifies the 100 best corporate citizens each year. Recognition is given to companies that demonstrate a strong commitment to all of their stakeholders—the community, minorities and women, employees, the environment, non-U.S. stakeholders, and customers. Twenty-nine companies have been recognized for five straight years. At the top of the list is Procter & Gamble. Others are Hewlett-Packard, Avon Products, Timberland, and Starbucks.

**IMPORTANCE OF ETHICAL BEHAVIOR**

Would you copy a paper from the Internet and submit it to your teacher as your own work? Would you cheat on a test to ensure a higher grade? Is it okay for an employee to call in sick to justify a day off from work or to take office supplies from the company for use at home? Do you believe a manager should ever lie to an employee or ignore unsafe working conditions in order to save money or speed production?

Each of those situations describes an ethical decision you and others may face in your personal life and in business. Not everyone will have the same belief about what is ethical and what is not ethical. It is important for businesses and those who work in business to develop agreement on behaviors that are acceptable and unacceptable.

> Justify the need for ethical management.

Name a behavior you would want your employer to discourage.
Individuals and organizations develop reputations based on their actions and the decisions they make. You can identify people who are not trustworthy and companies that do not compete fairly. When an individual or a company develops that reputation, others will be reluctant to trust them or work with them. Once that reputation is lost, it will be difficult to recover it and build a reputation of honesty and integrity. It is important for an organization to develop a clear view of what is acceptable business behavior and what is not.

**What Is Ethical Behavior?**

*Ethics* are the principles of conduct governing an individual or a group. Ethical business practices ensure that the highest standards of conduct are observed in a company’s relationships with everyone who is a part of the business or is affected by the business’ activities. Ethical behavior is not just the decisions and actions of a company’s executives and managers. It involves the actions of every employee.

Ethical behavior is made up of two parts: the actions of individuals and groups and the results of those actions. When considering whether behavior is ethical or not, both the actions taken and the results of those actions should be considered. Ethical behavior meets several standards:

- It is lawful.
- It is consistent with company values and policies.
- It does not harm some while benefiting others.
- If the actions and results become public, it will not embarrass the company.

**Ethical Management**

Managers are responsible for the success or failure of a business. Success or failure is not just determined by results, such as sales and profits or losses. It is also determined by the actions and activities of the business. Are the actions legal, honest, and ethical? Are people and other companies treated fairly? Does the work of the company improve the communities and countries in which it operates? Does the company work to
Ethical Management

Most organizations have a mission statement. A *mission statement* describes the reason a business exists and what it wants to accomplish. To make ethical behavior a part of a company’s mission, many businesses develop a statement of core values. *Core values* are the important principles that will guide decisions and actions in the company. Figure 7-3 shows the core values statement of the Rite Aid Company. As a part of the planning process, managers should work with employees to develop core values that emphasize ethical behavior.

The staffing function offers another chance for managers to emphasize the importance of ethical behavior. The company’s commitment to ethical behavior should be made clear when each new employee is hired. In employment interviews, prospective employees should be questioned about ethics and asked to describe how they would...
handle problems involving ethical behavior. New employee training should include information about the company’s commitment to ethics and values.

In the day-to-day operations of the business, managers and supervisors should often stress the importance of ethics. They should look for situations that might encourage employees to act unethically. Individual employees and work teams should be encouraged to develop ethical solutions to problems.

Ethical behavior should be a part of employee evaluations and promotions. Managers and supervisors should recognize and reward employees who display high ethical standards. They also need to be quick to identify and correct ethical problems if they occur.

Many important business decisions have both positive and negative results. The effects of international outsourcing challenge United States businesses and the U.S. economy.

International outsourcing is a business decision to transfer jobs from the United States to other countries. In an era of international business and the implementation of free trade agreements among many countries, the concept of outsourcing seems to make sense. U.S. companies want to expand their international business and at the same time reduce costs wherever possible. By shifting jobs from the United States to countries where wage rates are much lower, companies can greatly reduce their costs, providing a higher profit for executives and shareholders.

A negative result of outsourcing decisions is that U.S. workers are displaced from their jobs. Forrester Research, Inc. estimates that nearly 1 million jobs have already been lost to outsourcing and that, by 2015, up to 3.4 million U.S. workers will be affected by outsourcing. Lost jobs are found in almost all job categories, from manufacturing and service jobs to high-tech computer and data management jobs. Some suggest that other problems result from outsourcing. Companies are not held to the same strict regulations as when they operate in the U.S. That can mean lower environmental standards and poorer working conditions for employees. One of the major issues being raised is the privacy and security of personal consumer data that is transferred from a U.S. company to be handled by unknown employees in other countries.

Those who are in favor of outsourcing argue that in the long run, the movement of jobs to other countries will increase the standard of living for those employees, making them better markets for U.S. products. Opponents say that unless all countries have the same rules and regulations for business operations, U.S. employees do not have a fair playing field and cannot be competitive. The decline in U.S. employment in the past few years combined with increasing profits for many companies has only made the debate more intense.

Think Critically
1. How should companies balance the issue of increasing profits available from outsourcing and the resulting loss of jobs for U.S. companies?
2. Should the U.S. government take action to protect U.S. jobs even if it means that businesses will have lower profits?
Modeling Ethical Behavior

The most important action leaders can take to emphasize the importance of ethical behavior in an organization is to always act ethically. It is said that actions speak louder than words. If employees read the core values of a company but do not see managers living up to those values, it will be clear that ethics are not that important. On the other hand, if employees see their manager taking actions that demonstrate the company’s values, they will be encouraged to act ethically as well.

When managers treat each employee in a respectful way, it demonstrates that everyone is valued in the organization. When a manager rejects a decision that is illegal or would damage the reputation of the company even though it would be profitable, employees learn that ethical behavior is a basic value of the organization. Being an ethical role model inspires others to do the same.

Assessment

1. Which of the following is not a standard of ethical behavior?
   a. It should be lawful.
   b. It should not benefit some while harming others.
   c. It should not give the company a competitive advantage.
   d. It should not result in embarrassment for the company.

2. True or False. Managers are responsible for the ethical actions of a business.

3. Important principles that guide decisions and actions in a company are known as
   a. a mission statement
   b. a business plan
   c. ethical behavior
   d. core values

4. Research Use the Internet to locate a news report on a business charged with unethical or illegal activities. Gather information to identify the unethical actions taken, the impact of those actions on individuals inside and outside of the company, and the effect of the actions on the image of the company. Prepare a written report on what you learned.

5. Debate Form two debate teams. Assign each team the pro or con position on the following statement: “Managers must be responsible for the ethical behavior of every employee.” Each team will have five minutes to present their arguments and then two minutes of rebuttal time. At the end of the debate, have class members vote on which team made the most convincing argument.

Think of a time when you were faced with an ethical dilemma. How did you handle it?

What are the core values of an organization?

>> CHECKPOINT

THINKSTOCK

>> KEY CONCEPTS

Determine the best answer.

4. Research Use the Internet to locate a news report on a business charged with unethical or illegal activities. Gather information to identify the unethical actions taken, the impact of those actions on individuals inside and outside of the company, and the effect of the actions on the image of the company. Prepare a written report on what you learned.

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> Business Notes

7-1 Management

1. Managers’ work can be organized within five functions: planning, organizing, staffing, implementing, and controlling. Not every manager devotes the same amount of attention and time to each of the functions.

2. Most organizations have three levels of managers. Executives are top-level managers with responsibilities for the direction and success of the entire business. Mid-managers are specialists with responsibilities for specific parts of a company’s operations. Supervisors are the first level of management in a business and are responsible for the work of a group of employees.

3. A manager should use tactical management when working with part-time or temporary employees, working with employees who are not motivated, working under tight time pressures, assigning a new task for which employees are not experienced, or when employees prefer not to be involved in decision-making. A manager should use strategic management when employees are skilled and experienced, the work is routine with few new challenges, employees are doing work they enjoy, the manager wants to improve group relationships, or when employees are willing to take responsibility for the results of their work.

7-2 Leadership

4. Leadership takes skill to get people with different backgrounds and personalities to work well together and do the work needed by the business. The characteristics of an effective leader are understanding, initiative, dependability, judgment, objectivity, confidence, stability, cooperation, honesty, courage, communication, and intelligence.

5. The important human relations skills needed by leaders and managers are 1) self-understanding, 2) understanding others, 3) communication, 4) team building, and 5) developing job satisfaction.

6. Position influence is the ability to get others to accomplish tasks because of the position the leader holds. Reward influence results from the leader’s ability to give or withhold rewards. Expert influence arises when group members recognize that the leader has special expertise. Identity influence stems from the personal trust and respect members have for the leader.

7-3 Ethical Management

7. When an individual or a company develops an unethical reputation, others will be reluctant to trust them or work with them. It is important for an organization to develop a clear view of what is acceptable business behavior and what is not.

8. It is the responsibility of managers to establish an atmosphere in which all employees know they are expected to act ethically and believe they will be supported when they make the right decision.

> Communicate Business Concepts

1. How are the work of an entrepreneur and the top executive of a large corporation similar? How are they different? What do you believe are the most important management skills both types of managers need for their companies to be successful?

2. Describe a specific activity a manager might complete that illustrates each of the five management functions.

3. The number of mid-managers has been declining in many businesses as companies cut personnel and give employees more
responsible. In your opinion, what are the advantages and disadvantages of that change for businesses? How will the skills needed by employees change when there are fewer mid-managers?

4. Which type of management style would you personally prefer a manager you work for to have? Why? What would you have to do to successfully work for a manager who used the other style?

5. You have been assigned to be the team leader of a work group that must complete a very important project. What are the first things you would do to inspire and motivate the individuals to work well as a team to complete the assignment?

6. Review the list of leadership characteristics in Figure 7-2. Which three characteristics do you believe are the most important to managers? Which three do you believe are least important? Justify your choices. Compare your decisions with those of other students.

7. To demonstrate your self-understanding, what do you believe are your human relations strengths? What are your current weaknesses? Describe some examples of situations where you get along well with others.

8. In your school or another organization, identify a person that illustrates each of the four kinds of influence. Prepare an example of how each person uses their influence to accomplish the work of the organization.

9. Do you believe the ethical behavior that a person demonstrates in his or her personal life will be the same as the person’s ethical behavior in business? Why or why not?

10. As an employee, what would you do if you saw the following individuals behaving unethically: a coworker, a customer, a competitor, the top executive of your company?

>> Develop Your Business Language

Match the terms listed with the definitions.

11. The leadership role is part of the organization’s structure.

12. The important principles that will guide decisions and actions in the company.

13. The effort to direct and lead people to accomplish the planned work of the organization.

14. All of the activities involved in obtaining, preparing, and compensating the employees of a business.

15. Enables a person to affect the actions of others.

16. Ensure that the highest standards of conduct are observed in a company’s relationships with everyone who is a part of the business or affected by the business’ activities.

17. The process of accomplishing the goals of an organization through the effective use of people and other resources.

18. The way people get along with each other.

19. The effort to inspire and motivate individuals and groups to accomplish important goals.

20. Determines to what extent the business is accomplishing the goals it set out to reach in the planning stage.

21. Analyzing information, setting goals, and making decisions about what needs to be done.

22. The way a manager treats and involves employees.

23. Identifying and arranging the work and resources needed to achieve the goals that have been set.

24. The leadership role is not part of a formal structure.

Key Terms

a. controlling
b. core values
c. ethical business practices
d. formal influence
e. human relations
f. implementing
g. influence
h. informal influence
i. leadership
j. management
k. management style
l. organizing
m. planning
n. staffing
Decision-Making Strategies

Valencia Price has just become a supervisor in the Roxbury Manufacturing Company, where she has worked for eleven years. She had often heard employees complain that their supervisors were not interested in employees’ ideas and did not involve them in decision-making. As a result, Valencia felt it was important to avoid using power and reward influence and to try to adopt a strategic leadership style. From the first day of work as a supervisor, Valencia asked employees to discuss how the work could be improved. She knew that the other employees respected Manny, a long-time member of the work team. She would often ask Manny to lead the discussion when she wanted the team to make a decision so the employees would not think she was trying to influence them. After a month, Valencia started to hear that employees believed she could not make a decision on her own and wasted too much time in meetings. Several even suggested that maybe Manny should be the supervisor. They said that if Valencia had to ask Manny to run her meetings, she must not have any confidence in her own supervisory skills.

25. What principles of effective leadership was Valencia demonstrating as a supervisor?

26. Why were the employees not satisfied with the way Valencia was leading? What would you recommend she do?

Make Academic Connections

27. JOURNALISM Identify a manager of a local business who has at least five years of management experience. Prepare five questions about the person’s career and current work that would be of interest to others. Arrange a face-to-face or telephone interview with the person. If possible, record or take notes on the person’s comments. Prepare a 200-word article on the manager that could be published in a local newspaper.

28. COMMUNICATION Managers are responsible for establishing the importance of ethical behavior in a business. You are the CEO of a company that has a reputation of being a very ethical business. Prepare a two-minute speech that you will give to a group of newly hired employees that identifies the importance of that reputation and encourages each person to act ethically in all they do.

29. PERSONAL DEVELOPMENT The characteristics of effective leaders are shown in Figure 7-2. Create a three-column table. In the first column, list the characteristics from the figure. In the middle column, describe things you have done (hobbies, work, projects) that give evidence of each leadership characteristic. In the final column, list other things you can do in the next five years to further develop your capabilities as a leader.

<table>
<thead>
<tr>
<th>Planning</th>
<th>Organizing</th>
<th>Staffing</th>
<th>Implementing</th>
<th>Controlling</th>
</tr>
</thead>
<tbody>
<tr>
<td>Executives</td>
<td>22</td>
<td>6</td>
<td>2</td>
<td>4</td>
</tr>
<tr>
<td>Mid-Managers</td>
<td>10</td>
<td>12</td>
<td>7</td>
<td>14</td>
</tr>
<tr>
<td>Supervisors</td>
<td>5</td>
<td>8</td>
<td>3</td>
<td>20</td>
</tr>
</tbody>
</table>

30. GOVERNMENT The U.S. Department of Labor publishes the Occupational Outlook Handbook each year. Find the most recent edition of the Handbook on the Internet. Locate the section that reports on management occupations. Select a category that interests you. Identify five important job duties, the range of salaries paid, and the employment outlook for jobs in the category selected.

31. ECONOMICS Some people believe that ethical behavior and a company’s profitability do not go hand in hand. Use the Internet to locate research on the relationship between ethics and profits. Develop a one-page report on your findings. In the report, indicate whether you believe an ethical company can be profitable.

32. MATH The three levels of management spend different amounts of time on the five management functions. The records of one company show the average amount of time their managers spent on each function in a week. The results are shown in the table below. Calculate the total time spent per week by all levels of management for each of the five functions. Develop a graph that shows the percentage of the total hours each group devotes to each of the management functions during their workweek.
Linking School and Home

There are many opportunities in your community to develop skills that will help you become an effective business leader. Select five of the leadership characteristics shown in Figure 7-2 that you would like to develop. For each characteristic selected, identify a community activity in which you can participate that will help you develop the characteristic. List the community group or organization that offers the activity and the requirements to participate in the activity.

Portfolio Activity

To provide tangible evidence of your learning about entrepreneurship and small business management, do the following:

**COLLECT** information on several current and historic leaders from business, politics, sports, or other areas. **CREATE** a visual to illustrate the leadership characteristics demonstrated by the people you studied. **CONNECT** what you learned about leadership to an important concept you learned in another class. Make the connection by preparing a one-minute presentation on effective leadership.

Partnership With Business Project

Networking with leaders in the business community contributes to success. You may shadow business leaders and develop positive relationships within the business community. FBLA members can benefit greatly by forming positive relationships with business leaders.

This event recognizes FBLA chapters that develop and implement the most innovative, creative, and effective partnership plan for increasing sustained communication and interaction with the business community.

This class project will be performed by teams of two or three members. Each team must propose a Partnership with Business Project for the FBLA Chapter to consider.

The report you prepare will include Development (description of the goals, planning activities, and roles of business leaders and chapter members), Implementation (description of the activities implemented to learn concepts of business operations, level of involvement from business leaders, and roles of business leaders and chapter members in implementing the project), Results (description of concepts learned from the project and the impact of the project), Degree of Involvement (hours spent, personal contact, executives, and department heads contacted), and Evidence of Publicity (examples of publicity and recognition received from the partnership).

The format of the report should be clear and concise with logical arrangements of information. The written presentation should use a creative design with graphics.

**Performance Indicators Evaluated**

- Understand the importance of the business partnership.
- Demonstrate creative strategy for networking in the business community.
- Demonstrate a relationship that is important to the business and FBLA members.

You will be evaluated for

- Creativity and variety of partnership activities.
- Organization of your oral presentation.
- Outcome from the partnership between the business and FBLA.

For more detailed information about performance indicators, go to the FBLA web site.

**Think Critically**

1. What is the definition for professional networking?
2. Successful partnerships must provide a win-win situation for all participants. What does this mean?
3. List two types of activities that FBLA members can participate in with a business partner that are beneficial to both parties.

http://www.fbla-pbl.org/
Chapter 8

Human Resources, Culture, and Diversity

8-1 Human Resources Basics

8-2 Managing Human Resources

8-3 Organizational Culture and Workforce Diversity
Planning a Career in...  
**Human Resources**

Today’s businesses recognize the importance of their employees to the company’s success. A highly skilled, motivated workforce is a key competitive edge. Companies usually spend more money on their personnel than on any other resource. With that large investment, they need professional human resources personnel to recruit, train, motivate, and compensate employees.

The goal of human resources is to hire the best people, make sure they stay with the company, and continue to improve their skills to meet today’s and tomorrow’s job requirements.

Large human resources departments are made up of a number of specialists. They work closely with managers and employees. They ensure that employees are skilled, motivated, and rewarded for their work.

**Employment Outlook**

- There are many jobs in human resources, but also high interest in those jobs from college graduates and people with experience in industry.
- People with abilities in a specialized area of human resources are in greater demand than generalists.
- Job opportunities exist from entry-level clerks and assistants to the vice president of human resources.

**Job Titles**

- Director of Human Resources
- Benefits Specialist
- Employment Recruiter
- Training Specialist
- Job Analyst
- EEO/Affirmative Action Representative
- Employee Relations Representative
- Mediator
- Placement Specialist

**Needed Skills**

- A college degree with broad preparation in business, social, and behavioral sciences
- Specialized preparation in one or more specific areas of human resources management
- Ability to work with people at all levels of an organization
- Skill in problem solving, negotiations, and conflict resolution
- Ability to deal with detailed information while maintaining confidentiality

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**What’s it like to work as a... Corporate Trainer**

Emiko is a lead trainer for the Orbis Company. She has had an interesting career path, starting as a high school science teacher, followed by five years as a laboratory specialist in industry. Last month, she applied to fill an open training position in the company. The new job allowed her to combine her passions for teaching, science, and helping her coworkers.

As a lead trainer, Emiko meets with managers to identify training needs. Those needs might be helping new employees learn their jobs, preparing experienced employees for new processes, or developing a teamwork course. Emiko works with instructional designers and media specialists to prepare training materials. She must stay up to date with the latest educational technology since training is often delivered using computers and the Web.

**What about you?** Why is Emiko’s position so important to the success of the Orbis Company? Would you be interested in a career as a corporate trainer?
THE CHANGING WORKFORCE

The workforce is made up of all the people 16 years and older who are employed or who are looking for a job. More than 140 million people have full-time or part-time jobs in the United States workforce.

Most jobs today require at least a high school education. They often require some special training. Some jobs require only basic skills and a willingness to work hard, but those jobs are becoming scarce. Some jobs are high paying and some are low paying. Some involve working mainly with machines and technology. Others involve working mainly with people and information.

Types of Jobs

The business world consists of hundreds of thousands of companies. These companies provide a wide variety of jobs. The jobs in the business world may be arranged in many ways. The Bureau of Labor Statistics (BLS) is part of the U.S. Department of Labor. It researches thousands of different jobs. The BLS publishes many useful materials about the workforce. The Occupational Outlook Handbook is one of these. It offers up-to-date information about the U.S. workforce.

There are two major types of industries analyzed in The Occupational Outlook Handbook. The service-producing industries include businesses that perform services that satisfy the needs of other businesses and consumers. Service companies include health care facilities, insurance companies, retail stores, and transportation businesses. Goods-producing industries include businesses that produce or manufacture products used by other businesses or purchased by...
final consumers. These companies are involved in construction, manufacturing, mining, and agriculture. Figure 8-1 highlights the industry categories from the *Occupational Outlook Handbook*.

The U.S. economy has experienced a change. It has moved from an emphasis on goods-producing businesses to service-producing businesses. The BLS estimates that nearly all job growth over the next ten years will occur in service businesses. Four out of five workers will be employed in those businesses.

Another way of looking at the workforce is to think about groups of occupations. Occupations are affected by industry trends and current developments in certain types of businesses. Occupations in groups are affected differently. Twelve occupational groups used by the BLS, along with future employment prospects for each group, are shown in Figure 8-2.

Occupations also are referred to in terms of two very broad types of workers: white-collar and blue-collar. A

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**Figure 8-1**

**Industry Categories**

<table>
<thead>
<tr>
<th>Service-Producing Industries</th>
<th>Goods-Producing Industries</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Personal and business services</td>
<td>• Construction</td>
</tr>
<tr>
<td>• Retail and wholesale trade</td>
<td>• Manufacturing</td>
</tr>
<tr>
<td>• Finance, insurance, and real estate</td>
<td>• Mining</td>
</tr>
<tr>
<td>• Government</td>
<td>• Agriculture</td>
</tr>
<tr>
<td>• Transportation, communications, and public utilities</td>
<td></td>
</tr>
</tbody>
</table>

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**Figure 8-2**

**Employment Projections for Occupational Categories**

<table>
<thead>
<tr>
<th>Occupational Category</th>
<th>Percentage Change in Employment, 2002–2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Professional</td>
<td>23.3</td>
</tr>
<tr>
<td>Business and financial operations</td>
<td>21.3</td>
</tr>
<tr>
<td>Service</td>
<td>20.1</td>
</tr>
<tr>
<td>Construction and extraction</td>
<td>15.0</td>
</tr>
<tr>
<td>Installation, maintenance, and repair</td>
<td>13.6</td>
</tr>
<tr>
<td>Transportation and material moving</td>
<td>13.1</td>
</tr>
<tr>
<td>Sales and marketing</td>
<td>12.9</td>
</tr>
<tr>
<td>Management</td>
<td>12.1</td>
</tr>
<tr>
<td>Office and administrative support</td>
<td>6.8</td>
</tr>
<tr>
<td>Farming, fishing, and forestry</td>
<td>3.3</td>
</tr>
<tr>
<td>Production</td>
<td>3.2</td>
</tr>
</tbody>
</table>

---
A white-collar worker is one whose work is more mental than physical and involves the handling and processing of information. Most white-collar workers are employed in offices, stores, and professional services businesses. They include professional, managerial, and clerical workers. A blue-collar worker is one whose job involves a great deal of manual work, including the operation of machinery and equipment or other production activities. Blue-collar workers are employed in factories, on construction sites, and on farms.

### Changing Job Requirements

White-collar and blue-collar workers are equally important in the workforce. Increased use of computers and information technology in factories and construction is changing the nature of both types of work. It is resulting in a need for higher levels of education and training. Both types of workers are needed to satisfy economic needs and wants.

The jobs in the workforce are subject to a variety of factors that can cause the need for these jobs to change. Some of these influences may cause jobs to be eliminated. Others will cause the work to be modified. Changes may require employees to develop new skills and get different training. Consumer preferences, economic conditions, new technology, and business competition are strong influences on the workforce.

### Consumer Preferences

Consumers regularly cast their “dollar votes” in the marketplace. Preferences by consumers have an important effect on available jobs. Jobs are affected by consumer demand for a product or service. Sometimes new products entering the market make those already available obsolete. Workers making the old product may find that their jobs will be eliminated. New jobs would be created by the demand for the new products.

### Business Cycles

Stages of the business cycle affect job opportunities. When businesses expand and consumers buy more goods and services, new jobs are created to meet the growing demand. More workers are employed and earn more money. In turn, they spend more on goods and services that they need and want. The growing demand continues.

High prices cause consumers to decrease their buying. When interest rates increase, both businesses and consumers find it difficult to borrow money. Demand for goods and services decreases. As a result, jobs may be eliminated.

### Name ways in which computers could change the way an industry operates.

Each year, Fortune magazine identifies the “Best Companies to Work For” based on high rankings from each company’s employees. In your group, make a list of things a company can do that you believe would help it make that list.

**Work as a Group**
eliminated or the number of workers reduced. Consumer spending and demand is decreased even more.

**New Technologies** Technology refers to the use of automated machinery, electronic equipment, and integrated computer systems to help increase the efficiency of producing goods and services. Technology is important in the workplace. It improves efficiency so that businesses may stay competitive in international markets. Computerized systems and robots have greatly reduced the need for production workers in some manufacturing industries. These include steel, autos, tires, and farm equipment. Sophisticated computer and communications systems have also reduced the need for office employees such as typists, bookkeepers, and clerks. New technology continues to change the types of jobs in production and manufacturing. It has also changed how office workers and professionals perform their jobs.

**Business Competition** Companies must be competitive to stay in business. Costs are a major factor. The cost of running a business affects jobs and workers. When costs begin to increase, the business must look for ways to stay profitable. Installing new equipment and streamlining processes make workers more productive. Businesses may also decide to downsize. **Downsizing** is a planned reduction in the number of employees needed in a firm in order to reduce costs and make the business more efficient. **Outsourcing** removes work from one company and sends it to another company that can complete it at a lower cost. Today, many U.S. jobs are being outsourced to companies in other countries that pay much lower wage rates.

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**CHECKPOINT**

What are several strong influences on changes in the workforce?

Think of the places you frequent every day. What types of workers are visible? Are there “behind the scenes” employees?
resources. Managing human resources is one of the most important responsibilities of a business. Most medium- to large-sized businesses have a department devoted to human resources management and activities. The owner of a small business will be responsible for managing human resources or will hire others to complete the work.

Human Resources Goals
Human resources are different than almost every other resource needed by businesses. Each person is different. They bring varied knowledge, skills, experience, and motivation to their jobs. People are used in different ways in a company. Some will be required to do hard, physical labor. Others will operate sophisticated equipment. Some employees will work in groups where they must have effective interpersonal skills and demonstrate teamwork. Others will work independently, relying on their own abilities. Managers will direct the work of others and make long-term plans that affect the entire company. New employees must be willing to follow directions and will have few decision-making responsibilities at first.

Human resources must be able to work with the vast differences and unique capabilities of each employee and develop a workforce that is productive and efficient. The major goals of human resources are to

1. Identify the personnel needs of the company.
2. Maintain an adequate supply of people to fill those needs.
3. Match abilities and interests with specific jobs.
4. Provide training and development to prepare people for their jobs and to improve their capabilities as job requirements change.
5. Develop plans to compensate personnel for their work.
6. Protect the health and well-being of employees.
7. Maintain a satisfying work environment.

Human Resources Activities
Managing human resources involves four broad categories of activities. The categories are planning and staffing, performance management, compensation and benefits, and employee relations. Specific human resources activities for each of the categories are listed in Figure 8-3.

Planning and staffing activities are directed at identifying and filling all of the jobs in the company with qualified people. Performance management involves evaluating the work of employees and improving performance through training and development. Compensation and benefits is responsible for
planning and managing payroll, personnel records, and benefits programs. Employee relations is responsible for maintaining a safe, healthy, and productive work environment for all employees.

### 8-1 Assessment

<table>
<thead>
<tr>
<th>Key Concepts</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Determine the best answer.</strong></td>
</tr>
</tbody>
</table>

1. The U.S. workforce is made up of about ___?___ people.  
   a. 80 million  
   b. 100 million  
   c. 140 million  
   d. 190 million

2. The Bureau of Labor Statistics publication that provides detailed and up-to-date information about the U.S. workforce is the  
   a. Occupational Outlook Handbook  
   b. IRS Publication 15  
   c. Congressional Record  
   d. Business Report

3. A person whose work is more mental than physical and involves the handling and processing of information is a  
   a. blue-collar worker  
   b. human resource manager  
   c. white-collar worker  
   d. service employee

<table>
<thead>
<tr>
<th>Make Academic Connections</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Math</strong> The population of the United States is approximately 294,500,000. If 150,000,000 people are not employed, what percentage of the total population is not currently working? What accounts for the difference in that percentage and the approximate five percent unemployment rate that is typically reported?</td>
</tr>
</tbody>
</table>

5. **Art** Create a collage on poster board that illustrates the many activities that are a part of human resources. Clip pictures from newspapers and magazines that represent the four broad categories of activities. Show your collage to other students and describe the activities you have illustrated.
Managing Human Resources

Goals
- Identify important planning and staffing activities.
- Describe compensation and benefits plans.
- Recognize the goals of performance management.

Key Terms
- job analysis
- compensation
- salary and wages
- benefits
- incentive systems
- promotion
- transfer
- termination

Focus on Real Life
Jaqueline Perez had come to the end of a busy week as she locked the door to her bookkeeping service. She knew her work wasn’t finished. For the third time this year, she was going to have to replace one of her best employees who had resigned to take a position with a larger competitor. She owned a small company of 15 full-time and 12 part-time employees. The business had been more successful than she had hoped in its first three years, but the personnel problems were challenging.

Jaqueline had tried to support her employees with a good work environment. She even gave them time off from work to get advanced training. Because of it, the employees had become very skilled at using computer systems for maintaining business records. But it seemed that just as an employee got to the point where he or she was really doing a good job, the employee would be hired by a larger business paying higher wages or offering better benefits. Jaqueline wondered what she could do as a small-business owner to compete with the economic advantages offered by larger businesses.

HUMAN RESOURCES PLANNING AND STAFFING
Human resources management ensures that needed employees are available, productive, paid, and satisfied with their work. If human resources management does its job well, the company will have employees who do their jobs well. This will result in a successful, profitable business.

Planning and Job Analysis
Human resources management begins by analyzing where the business currently is in terms of its personnel and where it wants to be. The decision to hire people must be made carefully.

Once an employee is hired, the person’s salary must be paid whether the company is profitable or not. An employee should be hired when the work of that employee will add more to the company’s profitability than it will cost.

Classifying Employees The company must decide whether the person to be hired will be permanent or temporary. A permanent employee is one to whom the company makes a long-term commitment. It is expected that the employee will work for the business as long as the business is profitable and the employee’s performance is satisfactory. A temporary employee is one hired for a specific time or to complete a specific assignment.
Whether permanent or temporary, employees can be hired full-time or part-time. A *full-time employee* regularly works a schedule of 30 hours or more a week. A *part-time employee* has a shorter work schedule with either fewer hours each day or fewer days each week. Because permanent employees feel that they are a part of the business, they are often more productive than temporary employees. On the other hand, there is more control over the company’s resources when temporary employees are hired. The employee is paid only until the temporary assignment ends. Temporary employees are usually hired during a busy time for the business or when a special task needs to be done.

**Determining Job Requirements**

Before starting the hiring process, human resources staff studies the work that must be done in the job. Specific information about each job is needed in order to hire people with the right skills. That information is often collected by completing a job analysis. A *job analysis* is a specific study of a job to identify in detail the job duties and skill requirements.

First, human resources staff reviews the current job in detail. They identify all important job duties, as well as the knowledge and skills required to successfully complete the job. Next, they add any new activities planned for that job to the analysis. The job analysis will help determine if the needs of the business can best be met with temporary, permanent, part-time, or full-time employees.

**Recruiting and Hiring**

Once the specific need and skill requirements are determined, prospective employees meeting the requirements must be located. If this search is not done carefully, an employer may spend a great deal of time and expense and an appropriate employee may still not be found. Several good sources of prospective employees exist and are identified in Figure 8-4. Businesses should use sources that will provide

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**Figure 8-4**

*Which sources would you most likely use to look for a job?*

<table>
<thead>
<tr>
<th>Effective Sources for Locating Prospective Employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Newspaper classified advertising</td>
</tr>
<tr>
<td>• Public and private employment agencies</td>
</tr>
<tr>
<td>• High school and college placement offices</td>
</tr>
<tr>
<td>• Job and career fairs</td>
</tr>
<tr>
<td>• Referrals by employees</td>
</tr>
<tr>
<td>• Internet career services</td>
</tr>
<tr>
<td>• Radio and television advertising</td>
</tr>
<tr>
<td>• Industry publications</td>
</tr>
<tr>
<td>• Company web sites</td>
</tr>
<tr>
<td>• Company employment office</td>
</tr>
</tbody>
</table>
an adequate number of candidates for the position. The candidates must have the skills required for the job and an interest in working for the business.

**The Application Process** Most companies ask prospective applicants to fill out an employment application. The application gathers personal information, information on education, and work experience history. It may also ask for specific skills related to the job and names of people who can serve as references. For career-level jobs, the applicant may be asked to submit an application letter and a resume as well. Applications are used to remove people who are clearly not qualified for the job and to identify those who appear to be especially qualified.

Once applications have been reviewed, the top applicants are studied more carefully. Information is checked for accuracy. References are contacted. The employer selects a few applicants to interview. The applicant may be asked to complete special tests related to needed job knowledge and skills. During the interview, the applicant will be introduced to the work area, managers, and coworkers. The applicant will be given more detailed information about the company and the job. Finally, the most qualified applicant will be offered the job.

**New Employee Orientation** The final step in the hiring process is to help the new employee get a good start in the company. As a part of the orientation, the new employee will meet with human resources professionals. If you were a busy manager, how would you like to have an assistant available 24 hours a day? When you are leaving work for the evening, you can give the assistant a stack of work that will be completed and ready for you when you walk in the office the next morning. If you have a special research project, your assistant can visit a large library and gather the information you want. If you have a meeting with clients in another country, your assistant will be there to organize the materials and greet your visitors in their own language.

Is this a realistic scenario? Yes, if you hire virtual professionals. Virtual means that the work is completed somewhere other than your office using computer technology. Communications occur via the Internet, telephone, fax, or mail. Professional means that you can hire a person to whom you can assign a variety of business responsibilities from clerical and administrative duties to research, report preparation, or meeting planning. Virtual professionals are independent businesspeople or employees of business services firms. They are hired on a part-time basis for either permanent or temporary work. They may be located at their home, in another office building across town, across the country, or even in another country. They might work the same hours you do or, when in a different time zone, at times when you are not at work.

A manager may hire one or several virtual professionals and employ them for the length of time needed to complete the required work. The person can be used for occasional overflow projects, regular weekly or monthly tasks, or even to staff a part-time office in the city of important customers. Will you miss the face-to-face communication? Not with the technology tools available. Video-conferencing, audio and video e-mails, voice mail, and instant messaging link people more efficiently than walking to the next office even when they are halfway around the world.

**Think Critically**
1. What are the advantages and disadvantages of working virtually rather than in the same location as your manager and coworkers?
2. What other jobs could be completed virtually using the types of technology described?
resources specialists to complete all of the paperwork needed to receive pay and benefits. In turn, the company will have a complete employee record. There will usually be at least several days of training. The employee may be paired with an experienced coworker, or mentor. The mentor answers questions and helps the new employee solve problems and build confidence for the new job. The company may have a probationary period of several weeks to several months. At the end of that time, the new employee is evaluated to be sure job performance is meeting the company’s expectations.

**CHECKPOINT**

Why do human resources personnel need to study jobs before beginning the hiring process?

**COMPENSATION AND BENEFITS**

One of the reasons people work is to earn money. **Compensation** is the amount of money paid to an employee for work performed. Compensation is made up of two parts. **Salary and wages** are direct payment of money to an employee for work completed. Compensation in forms other than direct payment is known as **benefits**. Examples of benefits are insurance, vacations, low-cost food service, and health and fitness programs.

**Compensation Methods**

A **time wage** pays the employee a specific amount of money for each hour worked. A **straight salary** pays a specific amount of money for each week or month worked. Neither of these types of compensation are based on the amount or quality of work done, but are determined by the amount of time spent on the job. For that reason, it is a simple system to manage. The business just has to keep records on the amount of time each employee works.

**Incentive systems** connect the amount of compensation to the quality or quantity of an employee’s performance. Some businesses pay a **commission** in which an employee is paid a percentage of sales for which he or she is responsible. Salespeople are often compensated with commissions. Another pay-for-performance plan is known as a **piece rate**. An employee receives a specific amount for each unit of work produced. Piece rates are most often used in factories and data processing or telephone call centers.

Some companies use a **base plus incentive** compensation system. This system combines a wage or salary with

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**Work as a Group**

Automobile dealerships often paid their salespeople with a straight commission. Now many pay each salesperson a salary and an incentive based on customer satisfaction surveys. In your group, discuss how that change might affect the performance of the salespeople and why the dealerships have chosen to make the change.
an additional amount based on the employee’s performance. One type of base plus incentive plan is profit sharing. With profit sharing, employees receive their regular compensation plus a share of the profits earned by a company. This system encourages a commitment to the company, teamwork, and effective customer service so that profits will be high.

**Employee Benefits**

Employee benefits can be an expensive addition to the cost of compensation. On average for all businesses, an additional 20 to 40 percent of an employee’s wages is spent on benefits. If an employee earns $7.00 an hour, 30 percent added for benefits increases the hourly cost to $9.10. If the employee works 40 hours a week for 50 weeks, the additional cost to the company is $4,200.

State and federal laws require some benefits. Most new businesses must offer and pay the cost of benefits. Benefits include compensation for overtime hours worked, social security, Medicare, and contributions to funds for injured employees and for unemployed workers. Full-time employees may expect companies to offer insurance plans including health, life, dental, and disability insurance. Many companies, especially small businesses, cannot afford the cost of all of those types of insurance. Insurance costs in particular have been rising rapidly. As a result, many companies are reducing that benefit. They may also require employees to pay a large part of the monthly insurance premiums.

Time off for vacations is another popular benefit for employees. Paid vacations are a costly benefit since employees are being paid for time when they will not be working. On the other hand, the time off may result in a more content and productive employee. Other benefits offered by businesses include retirement programs, employee savings plans, personal or sick days off, and flexible work schedules.

The costs of benefits programs are very high and continue to increase. Each employee may prefer different benefits. As a result, human resources departments have developed cafeteria plans. A cafeteria plan allocates a certain amount of money to each employee that can be spent on benefits. The employee selects the preferred benefits. If the cost of the benefits does not use all of the allocated money, the employee can receive the difference in additional pay. If the costs are higher, the employee must pay the difference.

**CHECKPOINT**

List three types of incentive systems for employee compensation.

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**FYI**

At any time, about 68 percent of the U.S. population is working. Five to eight percent are unemployed but looking for work. Others who are not employed are students, parents who choose not to hold a job, people who are sick or disabled, and those who have retired.
**PERFORMANCE MANAGEMENT**

Managers work closely with their employees to make sure work is being finished as planned. Every employee is expected to meet quality standards as well as work efficiently. In addition, employees must demonstrate effective working relationships with coworkers, managers, and customers. As jobs change, new equipment and procedures will be introduced. Employees must upgrade their skills to meet the changing job requirements. Most companies offer training and development programs to help employees perform their work well.

**Employee Evaluation**

The manager evaluates the work of all employees on a regular basis. The human resources department is in charge of developing the evaluation procedures and forms. Managers will be trained to complete objective evaluations and hold evaluation conferences with employees. Human resources maintains the results of employee evaluations in the employee’s personnel file.

**The Evaluation Process**

Performance evaluations focus on the specific job duties of each employee. They also review the important work qualities expected of all employees. Those qualities include factors such as communication, interpersonal relationships, quality and quantity of work, and ethical behavior.

Managers are given evaluation forms to complete. Evaluation decisions are based on observations of the employee’s performance and evaluation of the quality of the work produced. Some companies ask coworkers to provide feedback that is considered in the evaluation process. Using the evaluation form, the manager identifies each employee’s strengths and areas that need improvement.

**The Evaluation Conference**

After the manager completes the evaluation form, a conference is scheduled with the employee. The purpose of the conference is to review and discuss the results of the evaluation and to plan for any needed performance improvement. Often, both the manager and employee are concerned about the conference. They might not be comfortable with a specific discussion of performance. Human resources personnel should work with all employees to help them prepare for evaluation conferences. The conference should be meaningful and positive. The conference should result in reasonable agreement on the employee’s performance, goals, and plans for the future. It should detail the support the employee can expect from the manager and the company in order to improve performance.

**Promotions, Transfers, and Terminations**

Employees expect that if they work for a company for a long time and perform well, they should be rewarded with
increased pay and the chance of promotion. A **promotion** is the advancement of an employee to a position with greater responsibility. Companies want to keep good employees. They want to place good employees in positions where they can provide the most benefit to the company. When possible, companies should fill open positions with current employees. Those employees are familiar with the company and will view the promotion as a reward. They will be motivated to continue to work for the company and continue to work effectively.

In some cases, promotional opportunities do not exist, but employees want to change jobs. It is not unusual for some jobs in a company to be cut due to changes in competition while other jobs are created. In that case, employees may accept a job transfer. A **transfer** is the assignment of an employee to another job in the company with a similar level of responsibility. The job may provide a new challenge for the employee or may be a better match with the person’s skills.

If performance does not meet the company’s expectations or if jobs are being reduced, the company may have to terminate the employee. A **termination** ends the employment relationship between a company and an employee. The termination may be a **discharge** that ends employment due to inappropriate work behavior. Another type of termination is a **layoff**, which is a temporary or permanent reduction in the number of employees due to changing business conditions. The company should complete all terminations carefully. The terminations must meet legal requirements and be as helpful as possible to the employee who is asked to leave the business.

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**Assessment**

**Key Concepts**

Determine the best answer.

1. An employee to whom a company makes a long-term commitment is considered to be
   a. full-time  
   b. part-time  
   c. permanent  
   d. temporary

2. True or False. Companies should interview all prospective employees who apply for a job.

3. On average, the percentage of employees’ wages spent on benefits is
   a. under 5%  
   b. 10%–20%  
   c. 20%–40%  
   d. over 50%

4. The employment relationship between a company and an employee is ended with a (an)
   a. termination  
   b. interview  
   c. evaluation  
   d. lawsuit

**Make Academic Connections**

5. **Math** Augusta is paid $3,100 a month and a commission of 2% on all sales. She also is given a yearly bonus of $4,500. If Augusta’s sales for the year are $186,200, what is her total salary for the year?

6. **Research** Use the Internet to locate four different sources of current job opportunities. Develop a table that compares the sites in terms of their effectiveness in providing information about the job, the company, and the procedure applicants should follow in applying for a job.

7. **Critical Thinking** You are a human resources specialist giving advice to a new supervisor on how to conduct a performance evaluation conference with an employee. List three recommendations you would make to the supervisor that would result in an effective conference.

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**CHECKPOINT**

What is the purpose of an evaluation conference?
8-3  Organizational Culture and Workforce Diversity

Goals
> Recognize factors that contribute to an effective organizational culture.
> Describe the benefits of diversity to an organization, individuals, and society.

Key Terms
organizational culture
work environment
labor union
diversity
glass ceiling

Focus on Real Life

“Three years of related experience required.”
“Must be very energetic and eager.”
“Requires heavy lifting.”

Each of these statements is from employment advertisements. Do the statements reflect important qualifications for a job? On the other hand, are the requirements designed to eliminate certain people as job applicants? Lack of related work experience excludes many high school students and recent graduates. A requirement of high energy or stamina might discourage older workers from applying. Women might avoid applying for a position when heavy lifting is a job requirement. Job recruitment should focus on the job. It should not focus on the type of person thought to be best qualified to fill the position. If a manager believes a female is most appropriate for the job, the requirements stated to fill the position will often reflect that belief. If physically disabled people are viewed as unsuitable for a job, those applicants will seldom be considered. Businesses should avoid any employment practice that discourages or eliminates applicants who may actually be effective employees.

DEVELOPING AN EFFECTIVE CULTURE

Businesses today are far different from those of the past century. Some of the changes that have occurred are obvious. Technology has reduced the need for low-skilled employees and demanded that current workers have much greater skills. The Internet has changed the way you communicate, share information, and shop. Globalization of business has resulted in greater competition. It has also resulted in more opportunities for every business to reach many new customers.

Other changes are just as important but not as clear. The workforce is more diverse, with growth among both younger and older workers. Jobs are changing, with a larger temporary and part-time workforce and a rise in entrepreneurship. Jobs are being shifted to other countries in an effort by businesses to cut costs. The number of manufacturing jobs is declining. Service jobs are growing at a rapid pace. Some of the service jobs are low skill. Others are professional-level jobs or require a great deal of technical knowledge.

Businesses have to respond to all of the changes and maintain a positive organizational culture. An organizational culture is the environment in which people work, made up of the atmosphere, behaviors, beliefs, and relationships. An organizational culture shows people how they will be treated and
how they are expected to treat others. It identifies what is acceptable behavior and what is not. If a company has a positive organizational culture, employees enjoy going to work. They have positive working relations with coworkers and managers. They believe the company values them and their work. They are motivated to do a good job for the company.

Work Environment
The work environment is the physical conditions and the psychological atmosphere in which employees work. The physical conditions are the work area, offices, break rooms, storage areas, and all other spaces where employees spend time while at work. Tools and equipment, lighting, temperature, and air quality are also a part of the physical work environment. The physical conditions must be safe and healthy. That is certainly a legal requirement of businesses. It is also important in assuring employees that the company has their best interests at heart. If employees believe the physical environment is unsafe or unhealthy, they will likely look for another job.

In addition to the physical conditions, companies need to provide a positive psychological atmosphere. Employees do not want to work in a place where they feel they are mistreated or where their work and ideas are not valued. An atmosphere of mistrust or fear is likely to result in low morale and poor performance among employees.

Not all jobs can be physically comfortable. Some require people to work outside in very hot or cold conditions. Other jobs require a great deal of physical effort or can be quite hazardous. Even in those jobs, the business needs to find ways to provide as much physical comfort as possible. They should offer protective clothing and equipment, allow needed breaks, and ensure that every employee receives adequate safety training.

Offering a positive psychological environment means that managers are trained in effective communications and interpersonal skills. They are honest, fair, and ethical in their treatment of each employee. Employees get important information from their managers rather than from rumors through the grapevine. They believe their work is important and valued. They are recognized and rewarded for their contributions to the company.

FYI
The average job in the U.S. pays $17 per hour and provides some health insurance and retirement benefits. Still, over 2.5 million Americans hold temporary jobs that average below $12 per hour with no health insurance or retirement benefits.
Work-Life Relationships

People seem to be working more days and longer days. Some people hold two jobs. There are many two-career families. Balancing work and personal life is a very important issue for most employees. A recent survey revealed that a majority of people would give up additional income to be able to spend more time with their families.

A positive organizational culture is one that respects the demands on employees from outside of the job. It offers ways for employees to meet those demands while also fulfilling the requirements of the job. Some of those ways include personal time, family leave, flextime, job sharing, and flexplace.

Many companies now offer personal time for employees to complete non-job activities that can only be done on work time. It is hard to schedule a dental or medical appointment, visit a child’s school, or renew a driver’s license while working. Personal time is a few hours each month that can be scheduled for non-job activities. Some companies even offer paid employee time to volunteer at schools or other community organizations.

Family leave policies allow employees to take a leave of absence for the birth or adoption of a child, to care for a sick family member, or for other personal emergencies. In 1993, the U.S. Congress passed the Family and Medical Leave Act. It requires companies employing 50 or more people to provide up to 12 weeks of unpaid leave for employees who face specific family or personal circumstances.

Flextime allows employees some choice in how their work days and work hours are arranged. Some employees may start and end their work day earlier or later than normal. They may be able to work a longer day and thereby work fewer days each week. Job sharing offers one job to two people. Each person works a part-time schedule. They share the work space and duties of the job. Flexplace means that some employees can complete part or all of their work away from the business site. Telecommuting is becoming increasingly popular. Employees who primarily use personal computers and other technology can work from home. They communicate with managers, coworkers, and customers using the Internet, telephone, and fax machine.

Some of the strategies for improving work-life relationships cost companies very little. Others do have a cost but often result in reduced absenteeism, lower employee turnover, and happier and more productive employees.

The Family and Medical Leave Act has limits on who may benefit—only 45% of Americans are eligible*. Are there other ways an employee might negotiate time with family?

*Economic Opportunity Institute
Employer-Employee Relations

Both managers and employees want their business to succeed. Unprofitable businesses have to reduce the number of employees they hire. They must limit salary and benefit increases. If everyone can work together to make the business successful, all should benefit. Managers and employees do not always have the same immediate goals. Managers must make sure that a company makes a profit. They try to get more work done at a lower cost. Employees are most concerned about pay, working conditions, and job security.

Many years ago, a boss made all of the important decisions and told employees what to do. This characterized employer-employee relations. Employees had little input as to what they did or how they did it. Each person was assigned a specific job. They often had little interaction with other employees while they worked.

That approach often left employees thinking that their ideas were not welcome or appreciated. They believed they knew a great deal about their jobs and the business and could offer suggestions to improve the way work was done. Those differences led to disagreements and conflicts between many employers and their employees.

Much is often made of the differences between management and employees. Still, there may be more things that are alike than different between the two groups. Managers and employees have discovered that as they work together, they find ways to accomplish the goals of both the organization and the individuals who work for it. Managers who involve employees in decision-making find that better decisions are made. Employees are more likely to support those decisions. Employees discover that when they cooperate with management, managers have a better understanding of their needs and expectations. Both groups benefit through cooperation.

Employer-employee relations are governed by a number of federal laws administered by the Department of Labor. Those laws relate to wages and salaries, benefits, employment age, health and safety, and many other issues. Access businessxtra.swlearning.com and click on the link for Chapter 8. Identify five different employment laws that would apply specifically to you and your classmates if you held a part-time job. Prepare a brief description of each law and what an employee or employer must do to comply with the law.
Labor Unions

Early in the 20th century, many U.S. businesses did not treat their employees well. Low wages and poor working conditions caused employees to band together and form labor unions. A labor union is an organized group of employees who negotiate with employers about issues, such as wages and working conditions. Unions can be effective because they represent large numbers of employees. The popularity of labor unions peaked in the 1940s and 1950s when more than one-third of the U.S. labor force was unionized. That percentage has been steadily declining since the 1960s and is now less than 15%.

Occupations with strong union membership today include police and firefighters, government employees, communications workers, transportation workers, construction trades, manufacturing occupations, and utilities employees. Unions and management resolve issues through collective bargaining, which is formal negotiation between members of both groups. When agreement is reached, both groups sign a written labor contract. There are also federal and state laws that regulate the relationships of businesses and unions.

Relationships between many companies and their unions are very positive today. They work together on issues that affect the success of the business and the work life of employees such as job training to keep employee skills up to date, employee assistance if a business site closes, and how to improve product quality to make businesses more competitive.

WORKFORCE DIVERSITY

Imagine a world where everyone looked, thought, and acted alike. The world is diverse, and the United States is the most diverse country in the world. That diversity continues to grow. Not all businesses reflect that diversity. Even in companies with a diverse workforce, that diversity is not always reflected in various job categories or in management positions.

Prospective employees and customers are attracted to work and shop in businesses where the employees are similar to themselves. When people with diverse backgrounds and characteristics are promoted into leadership and management positions, it will encourage others like them to work hard to achieve that same success.

How might a company recruiter ensure diversity in the workplace? What if only one type of person applies for positions?
Benefits of Diversity

Workplace diversity has many definitions. The basic definition of **diversity**, as it applies to businesses and organizations, is the comprehensive inclusion of people with differences in personal characteristics and attributes. The federal government has recognized important personal characteristics in equal employment legislation. Those laws are identified in Figure 8-5. Today, businesses working to build a diverse workforce use a much broader view of diversity. They try to build a broad workforce that reflects the communities in which they operate and the markets they want to serve. Diversity includes race, ethnicity, gender, age, and disability. It also includes socio-economic status, culture, religion, and even personal interests, abilities, and values.

When people in an organization are more alike than different, there is often reduced creativity and innovation. There will be limited understanding of people who are different including their attitudes, experiences, and needs. It will be difficult to recognize and plan for those differences when developing products and services for customers who are different from the people in the company. Companies that build a diverse workforce see several benefits. The benefits can be classified as organizational, individual, and societal.

**Organizational Benefits**

Prospective employees and managers are drawn from the broadest possible employment pool. The greatest increase in the labor force in the future will be women, ethnic and racial minorities, and immigrants. If people from those groups are not considered, the company will have fewer and fewer employees from which to choose.

The company will have a broader base of knowledge and understanding when making decisions. People with very different backgrounds, experiences, and even ways of thinking and planning will be a part of the organization. They will bring new ideas on how to design processes, plan products, work and communicate with others, and provide leadership.

Prospective customers will have a more positive image of the company. Customers with diverse characteristics will see a company that values that diversity. They will have a greater level of respect and trust for the company and its products. They will see a company that has their interests at heart. They will see that their views and interests are represented within the company.

The company will be better at serving diverse markets. The company will understand similarities and differences
in needs, decision-making processes, and communication strategies among diverse customer groups. Traditional stereotypes that upset consumers will no longer be used.

*Global business strategies will improve.* The U.S. is the most diverse country in the world and a country of immigrants. That offers American businesses a unique advantage to recognize and understand global needs and differences. They can do this much easier than companies from countries with limited diversity.

**Individual Benefits** Each employee will have the opportunity to develop to their full ability. In the past, women and other minority employees have faced a glass ceiling. A *glass ceiling* is an artificial limit placed on minority groups moving into positions of authority and decision-making. Businesses that value diversity remove those obstacles so everyone has an opportunity to advance based on their ability and performance.

*Individuals will feel they are respected and supported despite their differences.* Employees who are different from the typical employee do not have to hide those differences. They do not have to be uncomfortable because they are different. Individual differences will be expected and viewed as a valuable part of the organization. Employees can comfortably represent their uniqueness when participating in planning and decision-making.

**Societal Benefits** Prejudice and discrimination will be reduced as a societal problem. People involved in diverse organizations learn to recognize and value diversity. This is true for neighborhoods, schools, and businesses alike. They lose their stereotypes and recognize the strength that comes from the full participation of every person.

The country has a more talented, experienced, economically successful workforce. Diversity opens more job opportunities for everyone. It allows people to develop and use all of their abilities. It increases access to higher-paying jobs. Diversity in business leads to greater opportunities in society.

**Developing a Diverse Organization**

An organization’s culture develops over many years. Employees and managers become comfortable with the way things have always been done. It may be hard to recognize all of the ways that an organization makes it difficult for people from diverse backgrounds to be successful in the organization. The whole organization will need to be committed to diversity in order for the necessary changes to occur. An example of a written commitment to diversity is shown in Figure 8-6.

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**Figure 8-6**

Would you include anything else?

**Abbott Laboratories Diversity Statement**

At Abbott, we know that every employee—no matter what role they play or how long they’ve been with the company—is essential to our continued success. We count on having a variety of perspectives to foster the innovation we need to bring our science and company to a higher level of performance.

Abbott is committed to the principle of equal opportunities for everyone, and in nurturing an atmosphere in which creative thinking thrives and employees develop to their full potential. We believe the simple reason that any organization—or individual—realizes its full potential is because diversity is understood, appreciated, and supported.

Abbott offers more than just a job. We offer unlimited career opportunities, the ability for employees to build long-term financial stability and serve their commitments both on the job and in their personal lives.

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The following steps have been used successfully in a number of businesses and other organizations to develop diversity.

1. **Develop a written commitment to diversity.** Prepare a mission statement that clearly communicates the company’s values.

2. **Have the full support of top executives.** The top managers in the business must make diversity a priority in their written and oral communications and in their actions.

3. **Review evidence of diversity in the company.** Gather data on the diversity characteristics of all employees, managers, and companies. If any part of the organization does not reflect the diversity expectations, determine what is standing in the way and make changes.

4. **Update policies and procedures.** Make sure that recruiting, hiring, performance evaluation, and promotion practices encourage diversity.

5. **Provide continuing diversity education.** All managers and employees should participate in programs to increase their understanding of inclusion and diversity and to prepare them to work effectively in a diverse organization.

6. **Recognize and celebrate diversity.** Make diversity a part of the organization’s culture. Have visible evidence of the variety of languages, music, art, celebrations, and customs of employees and customers.

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**CHECKPOINT**

Identify several organizational, individual, and societal benefits of diversity.

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**Assessment**

**Key Concepts**

Determine the best answer.

1. **True or False.** There are greater numbers of both younger and older employees in the workforce today than in the past.

2. Some employees can complete part or all of their work away from the business site under
   a. flextime
   b. flexplace
   c. job sharing
   d. personal time

3. The term most closely related to diversity is
   a. affirmative action
   b. discrimination
   c. minority
   d. inclusion

**Make Academic Connections**

4. **Sociology** Use the Internet to identify data that describes the changing characteristics of the U.S. population in terms of age, gender, race, religion, and immigration status. Develop a written report of your findings. Include at least five tables and charts to support your written report.

5. **Art** Working with other students in your class, create a bulletin board, exhibit, or display that illustrates the diversity in your school and community.

6. **Journalism** Select a business in your community and contact a company executive to schedule an interview. Prepare several questions on the steps the company has taken to increase diversity and the results of those steps. Record your interview. Use the information to prepare an 800-to-1,000-word feature for a newspaper.
Coffee and a Conscience

In 1981, while on a skiing trip in Vermont, Robert Stiller stopped at a coffee shop for a cup of coffee. He liked the coffee so much that he decided to buy the business. Green Mountain Coffee is no longer a small-town coffee shop. It has expanded to become a major wholesaler of specialty coffees with a large direct-mail business and an e-commerce site. The company has been recognized by Forbes magazine as one of the best 200 small companies in America and by Business Week and Fortune as one of the fastest-growing small businesses.

Mr. Stiller was not only interested in developing a successful business. He had a belief that a company can be profitable and still have a social conscience. He wanted to operate a company that demonstrated a concern for the environment, for the people who grow and supply the coffee, and for the local and global community. Green Mountain Coffee is a partner and advocate in Businesses for Social Responsibility and the Fair Trade Partners.

Most coffee growers are small family farmers who are at the mercy of large coffee companies. Those companies had pushed the price paid for coffee beans to less than 70 cents a pound. The result was a drop in the income of small farmers to a level that didn't allow them to maintain their families' nutrition, health care, or education. Fair Trade Partners guarantee a minimum fair price when they purchase a farmer’s coffee beans, as much as $1.40 per pound. In return, they ask the farmers to use farming practices that result in high-quality products and that protect the environment.

Another program supported by Green Mountain is Coffee Kids, a nonprofit international organization. It is committed to improving the lives of children and families in the small mountain towns of coffee-growing regions around the world. The organization offers health care, nutrition training, educational scholarships, and money for local schools to improve the lives of children living in poverty. In 2001, Green Mountain employees personally donated over $100,000 to Coffee Kids.

Through the Community Action For Employees (CAFÉ) program, Green Mountain encourages employees to perform volunteer work while on company time. Employees average 6.5 work days a year of community service.

Social responsibility is an ongoing focus and commitment of the company. Among Green Mountain’s principles are Ethics Do the right thing. Integrity is the foundation of all our decisions, actions, and relationships.

Sustainability Pathway to our future. We use resources wisely and make decisions that take into account the well-being of people, profit, and the planet.

World Benefit Creating positive change. We are a force for good in the world. We celebrate and support the power of businesses and individuals to bring about positive changes, locally and globally.

Think Critically
1. Why would Green Mountain be willing to pay farmers almost twice as much for their coffee beans than the large coffee companies pay?
2. How do you believe social programs, such as those supported by Green Mountain Coffee, affect customers' views of the company? Do you believe it affects the sales of their products? Why or why not?
CHAPTER 8  Human Resources, Culture, and Diversity

>> Business Notes

8-1  Human Resources Basics

1. There are more than 140 million people who have full-time or part-time jobs in the United States workforce. Changes in the economy may require employees to develop new skills and get different training. Consumer preferences, economic conditions, new technology, and business competition are strong influences on the workforce.

2. Human resources are the people who work for a business. The major goals of human resources are to (1) identify the personnel needs, (2) maintain a supply of people to fill needs, (3) match abilities and interests with specific jobs, (4) provide training and development, (5) develop compensation plans, (6) protect the health and well-being of employees, and (7) maintain a satisfying work environment. The activities of human resources are planning and staffing, performance management, compensation and benefits, and employee relations.

8-2  Managing Human Resources

3. Human resources management ensures that needed employees are available and that they are productive, paid, and satisfied with their work. If human resources management does its job well, the company will have employees who do their jobs well, resulting in a successful, profitable business.

4. Compensation is the amount of money paid to an employee for work performed. Compensation is made up of two parts. Salary and wages are direct payment to an employee for work completed. Compensation in forms other than direct payment for work is known as benefits.

5. The manager regularly evaluates the work of all employees. Performance evaluations focus on the specific job duties of each employee as well as the important work qualities expected of all employees.

8-3  Organizational Culture and Workforce Diversity

6. An organizational culture is the environment in which people work, made up of the atmosphere, behaviors, beliefs, and relationships. An organizational culture shows people how they will be treated and how they are expected to treat others. A positive organizational culture is one that respects the demands on employees from outside of the job.

7. Prospective employees and customers are attracted to work and shop in businesses where people like them work. Companies that build a diverse workforce see several benefits. The benefits can be classified as organizational, individual, and societal.

>> Communicate Business Concepts

1. Why are service-producing industries growing more rapidly than goods-producing industries? What effect will this trend have on the skills people need for careers in the next 10 years?

2. Provide several examples of the effect of consumer “dollar votes” on jobs. What are some jobs that have increased and decreased in importance due to those “votes?”

3. Small businesses usually cannot offer the same levels of wages and benefits to employees as large businesses. In what other ways can small businesses compete to hire and retain highly qualified employees?

4. In addition to offering insurance benefits, what types of activities should businesses undertake to protect the health and safety of their employees?
5. What are the advantages and disadvantages for a company in hiring part-time and temporary employees rather than full-time and permanent employees?

6. Use a business directory to identify several nonprofit corporations in your area. What public service is each providing? Why do you think each is a public rather than a private corporation?

7. You are the human resources manager for a company and want to hire several accountants. List three good recruiting sources and justify your choices. If you wanted to hire several web designers, would your sources change? Why or why not?

8. Make a list of three benefits you would like to see a company offer its employees. How do you believe that list would change if you were married with a spouse and young children? If you plan to retire in 10 years?

9. Do you believe the physical conditions or psychological atmosphere of a business are more important to maintaining an effective work environment? Justify your choice.

>> Develop Your Business Language

Match the terms listed with the definitions.

10. Ends the employment relationship between a company and an employee.

11. Removes work from one company and sends it to another company that can complete it at a lower cost.

12. Amount of money paid to an employee for work performed.

13. Environment in which people work, made up of the atmosphere, behaviors, beliefs, and relationships.

14. Compensation in forms other than direct payment for work.

15. The assignment of an employee to another job in the company with a similar level of responsibility.

16. The comprehensive inclusion of people with differences in personal characteristics and attributes.

17. An organized group of employees who negotiate with employers about issues, such as wages and working conditions.

18. All the people 16 years and older who are employed or who are looking for a job.

19. Physical conditions and psychological atmosphere in which employees work.

20. The advancement of an employee to a position with greater responsibility.

21. Connect the amount of compensation to the quality or quantity of an employee’s performance.

22. Direct payment to an employee for work completed.

23. A planned reduction in the number of employees needed in a firm in order to reduce costs and make the business more efficient.

24. A study of a job to identify in detail the specific job duties and skill requirements.

25. An artificial limit placed on minority groups moving into positions of authority and decision-making.

Key Terms

a. benefits  
b. compensation  
c. diversity  
d. downsizing  
e. glass ceiling  
f. incentive systems  
g. job analysis  
h. labor union  
i. organizational culture  
j. outsourcing  
k. promotion  
l. termination  
m. transfer  
n. salary and wages  
o. work environment  
p. workforce
> > Decision-Making Strategies

Arte Malik has operated a lawn care business for many years. The business offers landscaping services including seeding and sodding lawns, applying chemicals and fertilizer, and regular lawn mowing. Mr. Malik has 25 employees. Many of them have worked for him for five to ten years. He usually hires two or three new employees each year. In the past, Arte was not concerned about the skills of new employees. He prefers to find people who are interested in the work and want to learn. Yet the machinery he uses is getting more complex, and employees must know a great deal about safe handling of chemicals, detecting plant diseases, and effective lawn care. The local community college has a two-year degree program in lawn care management. Arte is deciding whether to continue his present hiring procedure of allowing new employees to learn on the job, develop a training program to be offered to all employees, or hire only people who have completed the community college program.

26. What are the advantages and disadvantages of each of the choices Mr. Malik is considering?

27. If you were Mr. Malik’s human resources manager, what choice would you recommend? Why?

> > Make Academic Connections

28. **MATH** A small business budgets $80 per employee per year for training costs. The training cost for new employees is $130 for their first year. Last year the firm had 35 employees and added six new employees. It is considering increasing both parts of the training budget by 10 percent for the next year.
   
a. What was the total training budget for last year?
   
b. What percentage of the budget is spent on new employee training?
   
c. With the proposed increase, how much will be spent for training each experienced employee and each new employee?
   
d. What will be the total new training budget for all employees if four new employees will be hired?

29. **TECHNOLOGY** Use a spreadsheet and graphics program to make a chart or graph showing current data for the U.S. workforce using the following characteristics: (a) part-time versus full-time employees; (b) gender of employees; (c) racial classification of employees.

30. **COMMUNITY SERVICE** Companies participate in community activities to demonstrate that they value diversity. Using your community, develop a written description of a community service project that the employees of a business could complete to demonstrate that value.

31. **ADVERTISING** Use the Internet or a newspaper to locate classified advertising for employment opportunities. Select a job of interest to you and find listings from three different companies for that type of job. Develop a table that compares the three opportunities based on job duties, wages or salary and benefits, and work environment of the company.

32. **MATH** Nicole Miller works for a store that uses an hourly wage of $7 plus a commission of 2% on all sales over $500 per day. Her hours worked and daily sales for the past week are shown in the table.
   
a. How much did Nicole earn in base salary and commission for each of the days she worked?
   
b. How much was the total of her base salary for the week?
   
c. How much was the total of her commissions for the week?
   
d. What were Nicole’s total earnings for the week?

<table>
<thead>
<tr>
<th>Day</th>
<th>Hours</th>
<th>Total Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>Monday</td>
<td>6 hrs</td>
<td>$735 total sales</td>
</tr>
<tr>
<td>Tuesday</td>
<td>4 hrs</td>
<td>$320 total sales</td>
</tr>
<tr>
<td>Wednesday</td>
<td>5 hrs</td>
<td>$570 total sales</td>
</tr>
<tr>
<td>Thursday</td>
<td>3 hrs</td>
<td>$450 total sales</td>
</tr>
<tr>
<td>Friday</td>
<td>0 hrs</td>
<td>$0 total sales</td>
</tr>
<tr>
<td>Saturday</td>
<td>8 hrs</td>
<td>$1,050 total sales</td>
</tr>
</tbody>
</table>
>> Linking School and Home

Identify several people from your family or your neighborhood who work full time. Ask them their views on the importance of maintaining a balance between their work life and their personal life. Have them identify ways they believe the company they work for supports or does not support a balance in work-life relationships. Based on your discussions, do you believe most of the companies are or are not sensitive to work-life relationships?

>> Portfolio Activity

To provide tangible evidence of your learning about human resources, culture, and diversity, do the following:

**COLLECT** information from the web sites of several companies that provide information on their employment policies and ways they try to create a positive work environment for employees.

**CREATE** a visual that illustrates the effective human resources practices you identified.

**CONNECT** your visual to other items already in your class portfolio, or relate it to an important concept you learned in another class. Make the connection by preparing a one-minute presentation explaining the importance of effective human resources practices to the success of a business.

Emerging Business Issues Event

The border between the United States and Mexico has always been a major issue. Illegal workers cross the border to work at better-paying jobs in the U.S. Some Americans believe that it is unfair for non-citizens to be filling jobs in America. Research this issue. Be prepared to argue either to gain stronger control over illegal workers in the U.S. or to develop a process granting Mexican workers legal status or even citizenship in the United States.

Each team of two or three members must conduct research to gather facts to support their stand on the issue. Teams will be permitted to bring prepared materials written/printed on white 8 1/2" by 11" paper or notes written/printed on note cards. One 4" by 6" index card will be given to each participant and may be used during the preparation and performance.

Fifteen minutes before presentation time, team members will draw to determine whether they will present an affirmative or negative argument. Teams will then have 15 minutes to finalize their preparations.

Each presentation may last no more than five minutes. Following each oral presentation, judges/class members may conduct a five-minute question-and-answer period during which the presenters should be prepared to defend their affirmative or negative argument.

**Performance Indicators Evaluated**

- Demonstrate sound research with the information gathered.
- Present the case in a clear, understandable manner.

You will be evaluated for

- Organization of your oral presentation.
- Believability of your presentation.

For more detailed information about performance indicators, go to the FBLA web site.

**Think Critically**

1. How is illegal labor from Mexico beneficial to the United States?
2. Do illegal aliens from Mexico actually take away jobs from Americans?

http://www.fbla-pbl.org/
Chapter 9

Career Planning and Development

9-1 Career Opportunities
9-2 Planning Your Career
9-3 Applying for Employment
9-4 Securing a Job
Planning a Career in...

Employment Assistance

Most jobs involve some aspect of planning, creating, or distributing goods and services. But some jobs involve helping people obtain employment and helping them advance in their careers. The field of employment assistance includes a variety of activities. Some workers are employed by schools and companies to help people explore career options. Others assist people with preparing a resume, writing a cover letter, or practicing interview skills.

Many states have employment bureaus to help workers who have lost their jobs or who require retraining if they are injured on the job. Employment assistance workers are available to help identify, encourage, and plan advanced training for persons who have jobs. The field of career counseling is especially important as employment opportunities change due to technology, global competition, and demographic trends.

Employment Outlook

- Overall employment is expected to grow faster than average for all occupations.
- Employment for counselors in schools will show average growth.
- Career specialists who provide career planning assistance will be in strong demand as economic conditions and technology result in people seeking new employment fields.

Job Titles

- Career Counselor
- Career Placement Advisor
- Career Planning Instructor
- Career Coach
- Resume Writer
- Interviewing Trainer
- Vocational Testing Center Manager

Needed Skills

- School counselors will need a college degree along with state school counseling certification.
- Knowledge of employment trends and job search techniques are fundamental for most careers in this field.
- Communication and human relations skills are important for effective interaction with students and clients who are being served.

What’s it like to work in...

Career Counseling

“You are very capable in mathematics and computer technology. But your interests seem to lie in working with people.” These comments from a career counselor can help people better understand what they do well and what they enjoy doing.

In the next stage of the career search process, a career counselor will provide assistance with developing the content and format for a resume. Then, sample interviews will take place to help the person present a confident and competent appearance.

The counselor’s work doesn’t end when a person gets a job. A desire to advance in a career field can result in additional interaction with a counselor. Or, if a need exists to change careers, the counselor can direct you to needed resources for education and training.

What about you? Have you ever helped someone with finding a job or preparing for an interview? Is this something you enjoy?
THE CAREER PLANNING PROCESS

An occupation is a task or series of tasks that is performed to provide a good or service. People are hired to fill occupations, and they are paid for the work they perform.

A career is a goal for work that is fulfilled through an occupation or series of occupations. You actually have a kind of career goal now: “to complete your schooling and get ready for your future.”

Career planning is the process of studying careers, assessing yourself in terms of careers, and making decisions about a future career. As shown in Figure 9-1 on the next page, this process begins by carrying out a personal assessment. Your interests, values, talents, and abilities provide the basis for a career choice as you develop new interests and abilities.

Your search for the right career could continue for a long time. In the years ahead, some of your values and goals will change. You will develop new interests and abilities.
Your Study of Careers

Too often, a career choice is not made until full-time work begins. This is too late, especially if certain training and education are required.

The study of careers is a continuous process. New career opportunities occur all the time. You do not just decide to study careers for one day or one week. It is important to view learning about careers as a lifelong activity. It is something that continues even after you begin your career.

Your first decision will likely be a tentative career decision—a decision that is subject to change as new information is received. A tentative decision is much better than no decision at all. Your career decision will give you a direction that is needed.

Making initial career decisions while you are in school has many advantages. One is that, in school, you have a lot of information readily on hand. More importantly, early career planning will help you choose the right courses. An early career decision can also encourage you to become involved with organizations such as Future Business Leaders of America (FBLA), DECA, and Junior Achievement (JA). These organizations teach you about business and careers.

Career Training

Many careers require education and training beyond high school. These educational alternatives include:

- Two-year schools, usually called community colleges or junior colleges, offer training in many areas.
- Four-year colleges and universities, both public and private, provide education for many careers and professions.
- Private business schools specialize in specific job training, such as radio and television or computers and other technology.

Consider the cost for further schooling as an investment in your future that will help you earn higher wages and expand your potential. Many ways exist to help finance additional schooling. Most schools have financial aid programs including scholarships, student loans, and work-study opportunities.

Some financial aid programs are based on your academic record. Others are based on financial need. You should assess these methods for financing an education as you continue your career planning and decision-making.

How can you be sure that you are making the best career decision? There is no way to guarantee a perfect decision. Those who follow the right steps generally make good decisions.

STEP 1 Personal Assessment
- Determine interests and values
- Identify talents and abilities

STEP 2 Employment Market Analysis
- Geographic influences
- Business and economic trends

STEP 3 Application Process
- Application form
- Resume and cover letter

STEP 4 Interview Process
- Prepare for interview
- Follow-up activities

STEP 5 Employment Acceptance
- Salary and financial factors
- Organizational environment

STEP 6 Career Development and Advancement
- Practice career success behaviors
- Develop strong work relationships

CHECKPOINT

List the steps in the career planning process.
Many information sources for career planning are easily available. Your school may have a career resource center with magazines, books, videos, and CDs on careers. Some information covers careers in general. Other sources provide specific coverage about occupations and careers in your area.

**Print and Media Sources**

The *Occupational Outlook Quarterly* or other print publications from the Bureau of Labor Statistics can be helpful. *The Occupational Outlook Handbook* gives in-depth information on hundreds of occupations including job duties, working conditions, education and training requirements, advancement possibilities, employment outlook, and earnings. These resources are also available online.

*Career World* magazine publishes information about a variety of careers. It often looks at careers of the future. *The Encyclopedia of Careers and Vocational Guidance* can give you basic information about many occupations.

Newspaper help wanted ads (both in print and online) can be useful in career planning. Reading the help wanted ads in newspapers gives you an idea of what jobs are in demand. The ads help you find out what training and skills are needed. The career and business sections of newspapers publish articles on a range of career planning topics.

**Online Sources**

Web sites are available to help you with career planning. A search may be performed to gather information about “resumes,” “effective interviewing,” and “creating a career portfolio.”

**Informational Interviews**

A very useful method to get career information is with an informational interview. An informational interview is a planned discussion with a worker who is willing to help you find out about the work that a person does, the preparation needed for that career, and the person’s feelings about the career. Informational interviews will help you gain insight into what actually happens in a specific career area.

You will find that most workers like to talk about their career experiences. Be sure to plan your questions for a career information interview. Some suggested questions might include:

Identify the main sources of career information.
• How did you get your current job?
• In what ways do you find your work most satisfying? What are your main frustrations?
• What tasks and activities are required in your work?
• What are the most important qualifications for working in this field?
• What advice would you give a young person who is thinking about this type of work?

Keep notes on what you learn in your informational interviews. The experiences of others can provide key career planning information.

If a specific career interests you, ask your teacher or guidance counselor about the possibility of becoming a job shadow at a company employing workers that reflect your career interest. Job shadowing allows you to spend time with a worker for a day or a week to learn about a certain occupation.

**Work as a Group**

Using Figure 9-2, select three of the career areas listed. For each career area: (1) create a list of additional jobs, and (2) describe various skills that would be necessary to work in this career area.

**Business Contacts**

The process of talking to other people about their jobs is called networking. The advantage of networking is that your contacts are not limited to the people you know personally. Every person you meet is a potential contact for career information. The contacts in your network can provide support when you start work as well as later in life.

**Figure 9-2**

What areas interest you?

<table>
<thead>
<tr>
<th>Career Areas with Greatest Growth Potential</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales and retailing</td>
</tr>
<tr>
<td>marketing representatives and sales managers in the areas of electronics, medical products, financial services</td>
</tr>
<tr>
<td>Business services</td>
</tr>
<tr>
<td>web consultants, foreign language translators, employee benefits managers, data analysts</td>
</tr>
<tr>
<td>Management and human resources</td>
</tr>
<tr>
<td>supervisors, interviewers, employee benefit administrators</td>
</tr>
</tbody>
</table>
GROWTH CAREER AREAS

The life work you choose could be affected by the careers available in a field. Future employment opportunities are influenced by geography and business trends.

Geographic Influences

You may have to decide whether you want to work in the geographic area in which you now live or whether you are willing to move to where the job you really want is located. There may be reasons why you would prefer to live and work near your home. People who successfully pursue the careers of their choice often have mobility. **Mobility** is the willingness and ability of a person to move to where jobs are located.

The lack of mobility can lead to **locational unemployment**. This occurs when jobs are available in one place but go unfilled because those who are qualified to fill those jobs live elsewhere and are not willing to relocate.

Economic and Industry Trends

Career areas with most potential are influenced by economic trends and current business activities. Consumer demand, changing demographic trends, and new technology are factors that often affect career opportunities. As shown in Figure 9-2 on the previous page, service industries are expected to have the greatest employment potential.

While these are fields with strong future demand, do not limit yourself. Every career area will need new employees. Think about your personal interests and abilities in addition to economic and business trends.

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**CHECKPOINT**

What factors affect the career areas that will be in demand in the future?

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**Key Concepts**

Determine the best answer.

1. The first step of the career planning process is to
   a. prepare a resume and cover letter
   b. interview for a job
   c. determine your interests and abilities
   d. obtain career training

2. The purpose of an informational interview is to
   a. obtain information about a career area
   b. apply for a job with a nonprofit organization
   c. research salaries for starting employees
   d. gain career training experience

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**Make Academic Connections**

4. **Geography** Conduct research to identify areas of the country with strong demand for various careers. What factors have affected job opportunities in these geographic regions?

5. **Science** Identify recent scientific developments. Explain how these discoveries might affect (a) the type of career opportunities available in the future and (b) how people work in organizations.
As the country of Ukraine moved from using the Russian ruble to its current currency, the hryvnia, something rather unusual occurred. To prevent a shortage of money, the government issued coupons to use when buying some of the limited food and other products. While the coupons were not intended to become currency, their acceptance grew as the ruble became less attractive. The people of Ukraine desired to separate themselves from their past as a Russian state.

Today, the hryvnia is a fairly strong currency, reflecting an expanding economy and encouraging business investment from around the world. Ukraine’s strategic location, between Europe and Asia, is also attractive. More than 300 U.S. companies have business operations there. Ukraine is also being considered for membership in the European Union in the next few years.

Another change took place in the country’s reputation for corrupt business practices and unfriendliness. Today, visitors to the country often comment on the hospitality and generosity of the Ukrainian people. Ukraine has seen extremes in its history. The country was the major political and cultural center in Eastern Europe until conquered in 1240. More recently, Ukraine was part of the Soviet Union for 70 years. Remember, today Ukraine is not part of Russia despite their years of connection.

Be sure to use formal titles, such as Mr., Mrs., Miss, Ms., or Dr., until you are told to use a first name. When conducting business negotiations, don’t accept the first “no.” This initial “no” may be quick and automatic. Instead, be pleasant and ask again using a different phrasing. In addition, “final offers” may not be final. Be prepared to wait. Ukrainian businesspeople may walk out or shout. While responding in a similar dramatic way might be useful, patience will usually be more effective.

Social events are important in the business process. As you develop trust, acceptance of you will develop. Meetings will usually include highly sweetened coffee or tea along with chocolates or cookies. Some of the most popular dinner foods of Ukrainians include pork, chicken, seafood, potatoes, and many types of bread—white, brown, rolls, bagels, pita, and flat bread.

Think Critically
1. How does Ukraine’s history affect current business and economic activities?
2. What aspects of Ukrainian culture might create difficulties for international companies?
3. Conduct library or Internet research to obtain additional information about business and economic activities in Ukraine.
How can you make sure you select a job you will enjoy and that fits your life situation? Your career planning activities should start with a self-assessment of your interests, values, and abilities. These three areas will help you better understand the careers that will be the best for you. With a thorough self-assessment, you will be more likely to have a satisfying and successful career.

**Interests**

Many resources are available in print and online to determine the activities that give you satisfaction. Your interests provide a basis for your employment goals and possible career paths.

People with strong social tendencies may be best suited for work interacting with people. If you enjoy investigating situations, a career in some type of research should be considered. What are some topics or activities of interest to you?

**Focus on Real Life**

Brianna Bunton learned about career planning in a number of ways. Brianna prepared a career report on becoming a corporate lawyer as a requirement for her Introduction to Business class. She also interviewed the legal counsel for a local corporation. Her report gave her doubts about whether she really wanted to pursue a career in law and whether she could afford the additional schooling.

A course in marketing that Brianna finished in her junior year led her to believe that the marketing field was one that she would like to enter. She did some reading about careers in this area. With her various skills, she was able to get a part-time job as a marketing assistant the following summer. While on the job, she learned about more about the marketing process. Her job gave her a chance to talk to several sales and marketing workers about their careers. When school began again in the fall, she took more courses related to her interest in marketing.
Values
Your values are things that are important to you. You can learn about your values with exercises or activities. These exercises show how you rank items such as prestige, money, power, achievement, independence, security, belonging, or serving others. Each of these may influence you, directly or indirectly, when you select your life’s work.

You can begin to look at your values by answering some questions. Your answers will help you understand what you consider important. Examples of questions include:

• Is it important for me to earn a lot of money?
• Am I mainly interested in work that provides a service for others?
• Is it important for me to have an occupation that others think is important even if I do not really care for it?
• Do I want an occupation that is very challenging and may require additional schooling?
• Would I be willing to start in a job that pays a lower salary than another if that job was more challenging and offered better opportunities for future advancement?
• Do I consider investing money in education or occupational training as important as spending for other things?

Another question to better understand your values is: “What you would do if someone gave you a large sum of money to be used in any way you desire?” Would you start your own business? Would you hire a jet and travel around the world? Would you set up a foundation to support athletics for underprivileged children? Would you buy the trendiest wardrobe ever?

Work as a Group
Prepare a list of common values of people in our society. For each item on your list, describe career situations that would be appropriate for people with this value.

Talents and Abilities
Each of you has certain talents and abilities. A talent is a natural, inborn aptitude to do certain things. People often say someone has a “natural talent.” Ability is the quality of being able to perform a mental or physical task. Your talents and abilities, along with your career goals and interests, are important in career planning.

How can your natural abilities help you get a job?
You can learn about your abilities in a number of ways. Think about the courses you have taken and the grades you have received in school. What kinds of courses have you taken? In which ones have you done your best work? Which courses have been easiest for you? Which have been the most difficult? Which do you like the best? Answers to questions such as these will identify your talents and abilities.

Abilities can be developed, and that is important to keep in mind. If you are weak in a certain area, you may want to take courses that will improve that area. For instance, employers continually report that writing, reading, and computing skills are very important. If you are not strong in preparing reports, take extra courses in English and Business Communication. If reading is a concern, get help in that area. If working with fractions and decimals is not easy for you, more courses in math, including business math, would be desirable. Work to strengthen your weak areas before you go into full-time work. You can plan your courses and future activities to help you grow toward your chosen career.

EMPLOYMENT EXPERIENCE

Most people have more career skills than they realize. Your involvement in a range of school and community activities provides the basis for employment experiences. You can obtain further career-oriented abilities in four main ways: work-study programs, part-time employment, volunteering, and school activities.

A Question of Ethics

Dishonest Hiring Practices

Carl Markus applied for a position as a regional sales manager for a technology company. Although he recently came to the United States, Carl had eight years of computer sales experience in various eastern European countries.

After the interview, Carl was told that other applicants were more qualified. He did not receive the job. While it would be difficult to prove, Carl felt he was a victim of discrimination due to his slight foreign accent. He believes his ability and skills were comparable to others who were hired.

According to the Civil Rights Act and the Americans with Disabilities Act (ADA), it is illegal for employers to make hiring decisions based on personal information such as age, marital status, ethnicity, race, and gender. You can help reduce illegal hiring practices. Be careful of the personal information you include in a resume or cover letter. Never include a picture of yourself on a resume.

Most potential employers do not want to see this personal information related to characteristics that might be a basis for hiring bias. Instead, only offer personal information that is related to the job and your career skills such as hobbies, community activities, memberships, or personal interests.

Think Critically

1. Describe other situations in which a person might be discriminated against when applying for a job.
2. What actions can be taken by companies and workers to eliminate discriminatory hiring practices?
Work-Study Programs
Cooperative education combines school with work-related experience. These programs provide an occasion to develop a variety of on-the-job skills. You will not only learn about technical aspects of the job, but will also learn to interact in work settings.

In a similar way, internships involve work experience in organizations while learning about a career field. Internships for careers in accounting, finance, marketing, and communications are available with many companies and nonprofit organizations.

Applying for an internship is similar to applying for a job. First, identify potential positions. Then prepare a resume and cover letter to communicate your background and interest in participating in an internship.

Part-Time Employment
Summer and part-time work can provide valuable experience. In addition, these work situations will allow you the chance to see if you enjoy a particular career field. Your part-time work experience also helps you make contacts. These people will be able to guide you and offer support throughout your working life.

Volunteer Activities
Involvement in community service can result in gaining career experiences and improving work habits. Volunteering in community organizations also helps you develop organizational skills while making future career contacts.

School Activities
Class assignments can provide work-related experiences. For example, research and communication skills are developed when you prepare reports and oral presentations. Working on team projects offers you a chance to interact with others, a skill vital in every career.

School clubs and organizations can result in a range of valuable skills. Goal setting, planning, supervising, and delegating responsibility are activities needed in many employment settings.

CHECKPOINT
What are methods for obtaining employment experience?

Name some volunteer and part-time activities that could help in a career search.
**SOURCES OF AVAILABLE JOBS**

Finding available positions is a common concern for job hunters. Several sources are often used to obtain leads. Your ability to find job openings is a key part of career planning activities.

**The Media**

The sources you use for information about career planning can help you get job leads, too. Newspaper want ads are a common starting point. Be aware that most available positions are not advertised to the general public. Therefore, other job search actions are very important.

**Personal Contacts**

You need to let as many people as possible know that you are looking for a job. Your school counselors and business teachers can be very helpful. If your school has a placement office, be sure to register with that office. Your relatives, friends, neighbors, and others will be good potential sources of job leads.

**Business Contacts**

You should visit businesses and ask about their openings. Some businesses post help wanted signs in their windows. Getting a job means going out and looking around.

During a visit, you will be able to observe the types of activities performed by employees. You may also be able to make contacts for future career information. Consider calling or visiting before 8 a.m. or after 4 p.m. People are more likely to have time for you than during the main business day. Your professional appearance and actions can create a positive impression of your ability and initiative.

Use phone books, business directories, and websites to find names of organizations that may have unadvertised jobs. Communicating with these companies can produce business contacts that can result in current or future employment opportunities.

**Career Fairs**

Career fairs are often held at schools or community centers. These events allow a chance to contact several prospective employers in a short time. At a career fair, you will be asked a few questions to determine if you qualify for a longer interview.

Get ready for job fairs by being prepared to quickly communicate your potential contributions to an organization. Knowing something about the company will help set you apart from other applicants.
Employment Agencies

Another source of available jobs can be local and state government employment offices. These tax-supported agencies help people find jobs and provide career information.

Employers who need workers often get in touch with government employment offices for help. Employment offices can provide up-to-date information about the job market in your area. They can help you look for part-time, summer, or full-time work.

No one source is necessarily better than others. You need to let as many people as possible know that you are looking for a job. Your relatives, friends, neighbors, and others will be good potential sources of job leads.

**CHECKPOINT**

What are the main sources of information about available jobs?

**Key Concepts**

Determine the best answer.

1. True or False. A person’s values are also called natural talents.
2. True or False. Volunteering experience can result in obtaining career skills.
3. A desire to assist others in your job is an example of your
   a. talents  
   b. interests  
   c. abilities  
   d. values
4. A(n) _?_ is an event that allows a person to contact several prospective employers in a short time.
   a. career fair  
   b. informational interview  
   c. network  
   d. career resource center

**Make Academic Connections**

5. **Research** Use library research or an Internet search to locate a career assessment tool. After answering the questions, describe what you learned about yourself in relation to potential future careers.

6. **Communication** Look at the classified advertising section in your Sunday newspaper. Find three jobs that include an international factor. Prepare a paragraph summary explaining actions a person might take to prepare for these jobs.
Sharpen Your Life Skills

Effective Presentations

“We need you to report to the executive committee about the recent changes in our product line.”

This request and others point out your need to be able to make oral presentations. Your ability to communicate orally is a vital skill that can be enhanced by considering these actions.

Plan Your Presentation

- **Clearly define your purpose.**
  Organize the main sections. Conduct research to get needed information.
- **Plan a creative introduction.**
  Use a story, quote, statistic, or involvement activity to get the audience’s attention and to communicate your main theme.
- **Develop a clear conclusion.**
  Summarize the main ideas and key findings.

Practice Your Presentation

- Prepare an outline of key ideas and main phrases. Do not memorize or read your entire presentation.
- Present your complete presentation several times. Record your presentation to determine areas for improvement.
- Consider using a handout with key ideas, graphs, tables, maps, or other visuals.

Make Your Presentation

- Talk to the audience, don’t read to them. Don’t read from your visuals—posters, slides, or other items.
- Use effective voice projection, expression, and enthusiasm. Avoid repetitious phrases such as “OK,” “you know,” and “like.”
- Look and talk professionally—dress appropriately and stand up straight.

You are likely to make many presentations throughout your life. At first it may seem difficult. As you prepare, practice, and present more talks, your ability and comfort level will increase.

Think Critically

1. What are the main suggestions you should follow for making an effective presentation?
2. Describe some situations in which you may make presentations during your life.
Applying for Employment

**Goals**
- Prepare an application form and a resume.
- Identify the parts of an application cover letter.
- Discuss the online application process.

**Key Terms**
- application form
- resume
- career portfolio
- cover letter

**Focus on Real Life**

Francisca Negalo just graduated from high school. Over the years, she has had various summer jobs and worked part-time during school. Francisca is now ready for full-time employment. Her high school business education program included computer applications and two years of accounting. She has learned a number of computer-based accounting systems.

Francisca plans on continuing her accounting studies in a night school program at a local two-year college. She wants to earn an associate’s degree in accounting. In time, she will transfer to a university and work toward a bachelor’s degree in business administration. For now, she needs to get a job and earn some money.

**APPLICATION ACTIVITIES**

The application process may start in several ways. You might fill out an application form you have received from the employer. You may also apply by submitting a resume and cover letter.

**Personal Data Sheet**

The application process starts by preparing a *personal data sheet*. A personal data sheet is a summary of your important job-related information. It should list your education and work experience, as well as your references. Preparing your personal data sheet will ensure you have all the necessary information to fill out the application form.

**Application Form**

An employer often has each applicant complete an application form. An *application form* asks for information related to employment. The form gives the employer standard information about each job applicant. It becomes part of a permanent file. The form will likely ask for your name, address, social security number, education, work experience, the job for which you are applying, and references.

Filling out the application form should be viewed as your *first job task*. Follow directions carefully. Print answers neatly. Answer all questions completely. Take the assignment seriously. A poorly prepared application form may give a negative impression of you. Study the completed application form in Figure 9-3 on the next page.

> Prepare an application form and a resume.
A **resume** is a tool that provides information about you to a potential employer. Two of the most popular types of resumes are experience-based and qualifications-based. In an experience-based resume, experiences are usually listed in order of work history. In a qualifications-based resume, your abilities and experiences related to the job for which you are applying are highlighted.

As shown in Figure 9-4, a resume usually includes the following sections:

- **Personal information** Name, address, phone, e-mail
Do you see why this information might be helpful to an employer who wants to hire the best person possible?

### Sample Resume

**Francisca Negalo**  
1602 Collegewood Drive  
Madison, WI 53711-2821  
(608) 555-0308  
e-mail: fnegalo@badgernet.com

<table>
<thead>
<tr>
<th>CAREER OBJECTIVE</th>
<th>To use my accounting, business, computer, communication, and interpersonal skills in a challenging position with opportunity for advancement.</th>
</tr>
</thead>
</table>
| EDUCATION         | Four Lakes High School  
Graduated June 10, 20--  
Emphasis: Business Education |
| EXPERIENCE        | • Records Clerk, Tempest Tea Pot Company; one year, cooperative education  
• General Clerk, City Assessor’s Office, summer |
| Relevant Skills and Courses | Proficient with most recent versions of Microsoft Windows and Office, including Word, Excel, Access, and PowerPoint.  
Exelled in the following courses: Introduction to Business, Computer Applications, Accounting I and II. |
| Activities        | • Treasurer, Future Business Leaders of America  
• Member of Pep Club  
• Member of Alpha Chi youth group at First Christian Church  
• Member of East Side YMCA swim team |
| REFERENCES | Will be furnished upon request. |

- **Career objective** Personal employment goal
- **Education** Schools attended, dates, degrees, programs of study
- **Experience** Work and volunteer activities with dates and responsibilities
- **Career-related honors and other activities** Awards, school and community involvement

Be sure your resume is presented in a professional manner—clean, organized, with no errors. Limit your resume to one page. Use a format that highlights how your skills will contribute to the company’s needs.

Remember that resumes are usually skimmed quickly. Some companies even use scanners to check for keywords. Important words to include, as appropriate, are foreign language skills,
computer experience, achievement, research experience, flexible, team projects, overseas study, and international experience.

Use action words that demonstrate what you have achieved. See Figure 9-5 for examples of strong action words.

When preparing your resume, be completely honest about your qualifications. Remember that employers check resume information. Providing false information can cause you to lose a job. False information, found after you have been hired, can lead to your dismissal and long-term career problems.

Many career experts suggest not including a career objective on the resume. Often, a career objective is too vague or too general. Instead, this goal is better addressed in the cover letter when you connect your abilities to the organization’s needs.

References are not usually included on the resume. Have this information on hand when requested by a prospective employer. Prepare a list of people who can give a report about your character, education, and work habits. These individuals may be teachers, previous employers, supervisors, or coworkers. Be sure to obtain permission from the people you plan to use as references.

**Career Portfolio**

Many job applicants prepare a career portfolio. A career portfolio provides tangible evidence of your ability and skills. A career portfolio may include the following items:

- Resume, cover letter, and answers to sample interview questions
- Sample reports, presentation materials, and research findings from school projects
- Web site designs, creative works from school activities or previous employment such as ads, packages, and promotions
- News articles of community activities or other experiences in which you have participated
- Letters of recommendation

A career portfolio can show your abilities in a tangible manner to prospective employers. In addition, these materials will communicate your initiative and uniqueness.

**APPLICATION COVER LETTER**

The application cover letter expresses your interest in a specific job. Think of this as a sales letter for the purpose of obtaining an interview. Like any good sales letter, a cover letter should draw attention and interest. It should build a desire to meet you. Your letter should urge the reader to invite you to come for an interview. Figure 9-6 on the next page shows a cover letter that is neat, courteous, and to the point. A carelessly written letter may cause the employer to think that you will be a careless worker. A cover letter usually involves three main sections: introduction, development, and conclusion.
Introduction
Your cover letter should start by getting the reader’s attention. Next, indicate the reason for writing. Refer to the job or type of employment in which you are interested. Give a brief summary of your experience and qualifications. If applicable, mention the name of the person who referred you to this organization.

Development
This section should highlight your background and experiences that specifically qualify you for the job. Refer the employer to your resume for more details. At this point, summarize information about your experiences and training. Connect your skills and background to specific organizational needs.

Conclusion
The final section is designed to request action—ask for the opportunity to discuss your qualifications in more detail. In other words, request an interview! Include your contact information, telephone numbers, times when you are available, and e-mail address. Make sure your e-mail address is professional. Close the letter with a summary of how you could benefit the organization. Create a personalized cover letter for each position for which you apply.

Targeted Letter
In recent years, more job applicants are using a targeted application letter instead of a resume and cover letter. This letter provides a quick summary of your ability to meet the needs of an organization. A target letter will usually include a list of major skills and competencies. Once again, your goal is to emphasize achievements and skills so you will be invited for an interview.

Sample Cover Letter

1602 Collegewood Drive
Madison, WI 53711-2821
June 25, 20--

Dr. David Haugen
Vice President of Finance
Lakeview Technical College
Madison, WI 53706-3692

Dear Dr. Haugen:
The advertisement in the Daily Chronicle for an accounting clerk describes a position in which I am interested. Please consider me as an applicant for that position.

The ad stated that you are looking for a bright and alert person who is conscientious and interested in long-term employment. My record at Four Lakes High School and part-time employment record will show that I have the qualities you desire. My career goal is to someday become a Certified Public Accountant. An accounting clerk’s position in your office will allow me to get an important start on my career.

My business education program at Four Lakes High School included courses in Introduction to Business, Computer Applications, Office Procedures, and Accounting. I also completed four years of English and three years of math. For each of my last semesters, I was on the honor roll. In our work experience program, I worked ten hours a week during my senior year for the Tempest Tea Pot Company, where I learned a great deal about office work and human relations. My summer job in the city assessor’s office is helping me to work accurately with figures.

Enclosed is a personal data sheet giving my qualifications in more detail. I would appreciate an opportunity to interview with you. I may be reached by telephone at (608) 555-0308 anytime during the day.

Sincerely yours,

Francisca Negalo

Francisca Negalo
Enclosure

CHECKPOINT
What is the purpose of a cover letter?

Work as a Group
Plan an online portfolio. Design a web site that could serve as a career portfolio. Describe the format, elements, graphics, and links of this electronic portfolio. Talk about how an online portfolio could be used when applying for various types of careers.
ONLINE APPLICATION PROCESS

Many people are using the Internet for career planning activities. While researching potential employment is the most common use, job seekers also apply and interview online. Since an Internet resume is less personal, do not overlook other job search methods—phone calls, ads, job fairs, and personal contacts.

Online Applications

Many organizations allow you to apply online. In addition to the basic application, you may also be asked some preliminary questions to determine your suitability for the position available. When posting your resume online or sending it by e-mail, consider the following:

• Use a simple format. Avoid bold, underline, italics, and tabs.
• Do not use attached files that may be difficult to open.

Cyber resumes are posted on various web sites. They are scanned for keywords to identify candidates with the necessary job qualifications. Words and phrases that may impress prospective employers include foreign language skills, computer and e-commerce experience, achievement, research experience, flexible abilities, team projects, and overseas study or experience.

Cyber Interviewing

Many organizations hold screening interviews using video conferencing. Others require that you post preliminary interview responses online. These “e-interviews” may involve questions such as: “Would you rather have structure or flexibility in your work?” and “What approach do you use to solve difficult problems?”

Online interviewing may also be used to test a person’s ability in job-related situations. For example, an applicant may be asked to respond to tasks such as those that a bank teller or retail clerk might encounter.

CHECKPOINT

How is the Internet used in the job application process?

9-3

Assessment

>> Key Concepts

Determine the best answer.

1. The item least likely to be included on a resume is
   a. a school award  
   b. your references  
   c. schools attended  
   d. your work experience

2. The main purpose of a cover letter is to
   a. request an interview  
   b. obtain career information  
   c. ask a person to be a reference  
   d. apply for a government job

>> Make Academic Connections

3. Law Conduct library or online research to obtain information on laws that protect people during the hiring process. What actions are illegal when selecting among various people for a job?

4. Technology Locate an online application form. What types of questions are asked? Are you prepared to answer these questions? How?
Securing a Job

Goals

> Describe activities involved in the interview process.

> Compare factors to consider when accepting a job offer.

> Identify attitudes and actions for success on the job.

Key Terms

employment interview
mentor
exit interview

Focus on Real Life

Barda Yang received a phone call asking her to come in for an interview. She had recently applied for a part-time job to assist the administrator of a child care facility. Barda has always enjoyed working with children. Her volunteer work at the park district, helping to coach soccer, helped her get this interview.

Although this job doesn’t involve working directly with children, she is excited about the opportunity to work in that environment. Barda has not had many interviews in her life, but has practiced answering sample questions with her aunt. This experience has given her more confidence as well as an improved ability to answer unexpected questions.

THE INTERVIEW PROCESS

“We want to meet with you in person.”

This is your goal after submitting an application or resume. An employment interview is a two-way conversation in which the interviewer learns about you and you learn about the job and the company.

Before You Interview

Prepare for an interview by obtaining more information about your prospective employer and the job for which you are applying. Prepare questions to ask in the interview. These might include:

- What training opportunities are available to employees?
- What qualities do your most successful employees possess?
- What new opportunities are your company considering in the next few years?

Successful interviewing requires practice. Record yourself so you will answer questions in a smooth and complete manner. Prepare concise answers for specific questions you might be asked. Ask friends to help you practice your interview skills. Attend workshops on interviewing skills. Work to organize your ideas. Speak clearly and calmly. Be sure to communicate enthusiasm.

What kinds of information can you learn about a position in an interview?
As you prepare for your interview, remember the following:

- Be on time for the appointment.
- Go alone to the interview.
- Dress properly—wear clothing that is not too formal or too informal.

Wear the type of clothing that is appropriate for the company and the job for which you are applying.

**During the Interview**

The person who interviews you wants to find out such things as your appearance, manners, use of language, and general ability for the job. An interviewer may take a number of different approaches. Most interviewers will try to put you at ease when your interview begins. Interviews may include situations or questions to determine how you react under pressure. Answer clearly in a controlled manner. Use of behavioral interviewing is expanding to better evaluate an applicant’s on-the-job potential. Questions typically begin with “describe” or “tell me about...” Some common interview questions are shown in Figure 9-7.

Some employers use pre-employment tests to screen applicants for skills and abilities needed on the job. Examples of pre-employment tests include keyboarding, word processing, calculating, and other skills. The interviewer may review your test results and discuss specific job requirements with you.

Avoid talking too much, but answer each question completely using good eye contact. Stay calm during the interview. Remember, you are being asked questions on a subject about which you are the world’s expert—you! Finally, thank the interviewer for the opportunity to discuss the job and your qualifications.

**FYI**

An interviewer cannot ask
1. Where you were born
2. Your age
3. If you have any disabilities
4. Your marital status
5. Your religion
6. Your responsibility for children

An interviewer can ask
1. If you are a U.S. citizen
2. For proof that you are over 18
3. If you have the physical ability to perform the job
4. If there are any days or times when you can’t work

As you prepare for your interview, remember the following:

- Be on time for the appointment.
- Go alone to the interview.
- Dress properly—wear clothing that is not too formal or too informal.

Wear the type of clothing that is appropriate for the company and the job for which you are applying.

**Figure 9-7**

Think of answers to each question.

**Common Interview Questions**

**Education and Training Questions**

- What qualifies you for this job?
- Why are you interested in this company?
- In addition to school, what activities have helped you to expand your interests and knowledge?

**Work and Other Experience Questions**

- In what situations have you done your best work?
- Describe the supervisors who motivated you most.
- Which of your past accomplishments are you most proud of?
- Describe people with whom you have found it difficult to work.

**Personal Qualities Questions**

- What are your major strengths?
- What are your major weaknesses? What have you done to overcome these?
- What do you plan to be doing five or ten years from now?
- Which individuals have had the greatest influence on you?
After the Interview
Within a day or so, send a follow-up letter to express your appreciation for the opportunity to interview. Even if you don’t get the job, this thank you letter will make a positive impression for future consideration.

Next, do a self-evaluation of your interview performance. Try to remember questions that were different than you expected. Write notes about areas in which you need improvement. The more interviews you have, the better you will present yourself. More interviews will also increase the chance of being offered a job.

Be patient after the interview. It may take several weeks for the company to complete all of its interviews and make its selection.

JOB OFFER COMPARISON
“We’d like you to work for us.” When you hear those words, remember to consider several factors before accepting the position. The financial aspects of a job should be assessed along with some organizational factors.

Salaries and Financial Factors
The type of work and your experience will affect your rate of pay. The position may include employee benefits. While these may be limited for part-time workers, you should still be aware of insurance, retirement, vacations, and special benefits for employees. Many organizations offer recreational facilities, discounts, and other advantages for workers.

Work as a Group
Use Figure 9-7 to ask others sample interview questions. Create follow-up questions based on their answers. Comment on the strong aspects of their answers and suggest improvements.

Organizational Environment
While the financial elements of a job are very important, also consider the working environment. Leadership style, dress code, and the social atmosphere should be explored. Talk with people who have worked in the organization.

Advancement potential might also be assessed. Training programs may be available for students and part-time workers. These opportunities can be very beneficial for your long-term career success.
Attitude can make a big difference in your career success. A positive attitude helps you learn and cooperate with others. Always think, speak, dress, and act to project a positive image. Then, you will likely find your job more satisfying and enjoyable.

Job Success Strategies
As you prepare for your first day of work, remember the following:

- **Ask questions.** If you do not understand directions, have them repeated and listen carefully. You probably will make mistakes when learning your job. Be sure to learn from each mistake and avoid repeating it.
- **Avoid complaining.** If you seem to have more work to do than you can handle, talk with your supervisor.

- **Honor the time for breaks.** Don’t abuse rest periods and lunch breaks by extending the time limit.
- **Consider your appearance.** Dress neatly and be well groomed. Employers often observe that sloppy appearance reflect sloppy work habits.
- **Be on time.** Arriving late or leaving early is a poor practice.
- **Be friendly with everyone.** Respect your coworkers and learn to get along. Each person in an organization is important. Any coworker may be of help to you in the future.
- **Show you are dependable.** Do quality work that is completed on time. Sloppy work or work turned in late affects others. You are part of a team—take pride in that. Pay attention to details. Return phone calls and e-mails promptly to show that you care about your work.
Follow the rules. If a rule seems unfair or unreasonable, discuss it with others and find out why it was created.

Many successful people get assistance from a person with more experience. A mentor is an experienced employee who serves as counselor to a person with less experience. This “career coach” can serve many benefits as you move forward in your working life. For example, your mentor might help you look for future opportunities.

Leaving a Job
At some point in your career, you will have to tell an employer that you are leaving. Departing on good terms is important. The following tips can help you leave a job in an appropriate manner.

- Give at least a two-week notice. Write a short, polite letter of resignation; include the date of the last day you will be working.
- Try to finish all current projects that you have been assigned. If they are not completed, leave a note explaining to the next person where to begin.
- If there is an exit interview, in which your employer asks questions about your work, be constructive and cooperative.
- Let coworkers know that you appreciated the opportunity to work with them.

Leaving on a positive note is good for you and for those you are leaving.

CHECKPOINT
How does a mentor assist less experienced employees?

Key Concepts
Determine the best answer.

1. A commonly suggested action to take after an interview is to
   a. contact the organization about the salary  
   b. evaluate your performance in the interview  
   c. revise your resume  
   d. estimate the cost of career training for the job

2. The _?_ interview occurs when leaving a job.
   a. informational  
   b. exit  
   c. employment  
   d. coaching

Make Academic Connections
3. Communication Work with another person to improve your interview skills. Ask each other some of the questions in Figure 9-7. Describe strengths and needed improvements to each other.

4. Culture Describe questions and actions that might occur in the interview process in different countries. How could body language be interpreted differently in various cultures?
Chapter 9  Career Planning and Development

> > Business Notes

9-1 Career Opportunities
1. The career planning process involves a self-assessment, an analysis of the employment market, application activities, the interview process, a comparison of job offers, and career development activities.
2. Important sources of career information include print and media sources, online sources, informational interviews, and business contacts.
3. Career fields with the most growth potential include computer technology, health care, business services, social services, sales and retailing, education, hospitality and food service, financial services, management, and human resources. Service industries are expected to have the greatest employment potential in the future.

9-2 Planning Your Career
4. Your interests, values, talents, and abilities should be assessed when making a career decision.
5. Employment experience may be obtained through work-study programs, part-time employment, volunteer activities, and school activities.
6. Information sources about available jobs include the media, personal contacts, business contacts, career fairs, and employment agencies.

9-3 Applying for Employment
7. The application process may start with completing an application form or with the use of a resume and cover letter.
8. There are three main parts to an application letter. The introduction gets the reader’s attention. The development highlights your background and the skills that qualify you for the job. The conclusion asks for an interview.
9. Online application activities include the application process, e-resumes, and cyber interviewing.

9-4 Securing a Job
10. The interview process involves preparing for the interview, participating in the interview, and follow-up activities.
11. Factors to consider when accepting a job offer are salary, benefits, leadership style, dress code, social atmosphere, and advancement potential.
12. A positive attitude is the foundation of success on the job. Other success strategies include asking questions, avoiding complaints, giving attention to your appearance, following the rules, and being on time, dependable, and friendly.

> > Communicate Business Concepts

1. Who are some people you know that you might consider for an informational interview?
2. Give examples of how consumer demand, changing demographic trends, and new technology might affect career opportunities.
3. Make a list of your talents and abilities. Specify whether you believe each one is strong or weak. Indicate how you might use your strengths in career planning. Also indicate what actions you might take to improve your weak areas.
4. What actions might a person take when preparing to attend a career fair?
5. Your personal data sheet should list several references. Application forms also ask references to be listed. Make a list of three or more references you could use right now. Then note the type of information each reference could give that would be of help to a potential employer.
6. Prepare a list of items that you might include in a career portfolio when applying for a job.

7. If you were in charge of hiring people, what information would you want to obtain from applicants? How would you go about getting this information? What are some specific questions you would ask if you were to interview the applicants?

8. Job applicants may encounter role-playing situations in an interview. What types of situations may be used to assess the skills and abilities of prospective employees?

9. Information has been received about three job openings in your community. Each is quite different. Assume that you are qualified for only one position. Make up whatever qualifications you think you would like to present to a prospective employer. Then write a letter of application for the position.

   a. Reliable person is needed to handle a variety of responsibilities in a small business office. Must be able to work without supervision and communicate effectively with people who call for information. Word processing and other office skills are desirable. Salary is better than average in this community.

   b. Salespeople are needed for the auto parts and cosmetics departments of a large retail store. Applicants should have some familiarity and/or experience with selling. Hours are flexible, although some evening and weekend work will be required. Benefits are especially attractive; incentive bonus policy can provide a good income for the right person.

   c. Ours is a leading bank in this region. We are in need of capable people who want to begin a career in banking. Our training program starts at the bottom, but provides a great opportunity to learn about the banking industry. Salary is competitive.

10. What kinds of questions would you ask in an exit interview if you were the supervisor interviewing a sales clerk who is leaving?

>> Develop Your Business Language

Match the terms listed with the definitions.

11. A planned discussion with a worker to find out about the work that person does, the preparation necessary for the career, and the person’s feelings about the career.

12. The willingness and ability of a person to move to where jobs are located.

13. The things that are important to you in life.


15. A goal in life that is fulfilled through a job or a series of occupations.

16. The quality of being able to perform mental or physical tasks.

17. A sales letter about an applicant written for the purpose of getting an interview.

18. A summary of job-related information about yourself.

19. An experienced employee who serves as counselor to a person with less experience.

20. A document used by employers that asks for information related to employment.

21. A two-way conversation in which the interviewer learns about you and you learn about the job and the company.

22. An interview in which an employer asks questions about how an employee liked his/her work and inquires about job improvements that might be made.

23. Tangible evidence of your ability and skills provided when applying for a job.

Key Terms

a. ability
b. application form
c. career
d. career portfolio
e. cover letter
f. employment interview
g. exit interview
h. informational interview
i. mentor
j. mobility
k. resume
l. talent
m. values
CHAPTER 9  Career Planning and Development

>> Decision-Making Strategies

Jeff Barbson is looking to his future and wondering what kind of career he should prepare for. His father is the city’s civil engineer. His mother is a buyer in a major department store. Both of his parents are successful and enjoy their careers. Both of them have talked with Jeff about their work. He has visited his father’s office and has worked as a sales clerk in his mother’s store. Jeff’s favorite subjects are computers, economics, and art. He earns his best grades in computers and art. Jeff’s father wants him to be an engineer because there is a need for engineers in their state. His mother wants him to go into retailing. Jeff would like to go to medical school and become a heart specialist.

24. Based on his school record, which of the three career areas do you think he should choose?

25. What advice would you give Jeff regarding career planning?

>> Make Academic Connections

26. ECONOMICS The web site for the Bureau of Labor Statistics (www.bls.gov) presents a wide variety of data on employment and wages. Select a topic area and present a two-paragraph summary. Explain how this information could be useful in your career planning activities.

27. CULTURE Talk to someone who has worked in another country. Obtain information about the application process and hiring activities in a different culture.

28. MATH Nancy Sistrerse attends a college where the tuition and fees amount to $9,500 per year. The books and supplies she buys total $1,200 per year. In addition, she has general living expenses of $11,600 per year. She has three sources of income: financial aid of $3,500 per year, a scholarship that pays one-half of her tuition, and a work-study job from which she earns $5,300 per year.

a. How much income does Nancy receive each year from her three sources of income?

b. How much does it cost Nancy to go to this college each year?

c. What percentage of her annual college costs is covered by her three sources of income? (Round off your answer.)

d. If her uncle David said that he would lend her the money she needs beyond her three sources of income, how much money would Nancy have to borrow each year?

29. COMMUNICATION Prepare an in-class presentation or video with examples of strong and weak interview behaviors.

30. TECHNOLOGY Visit a web site that allows people to post their resumes. Prepare a summary of the procedure, cost (if any), and other information from the web site.

31. MATH Emilie Antoine is a personnel interviewer. On Monday, she interviewed 7 job applicants; on Tuesday, 6 applicants; on Wednesday, 9 applicants; on Thursday, 5 applicants; and on Friday, 8 applicants.

a. How many job applicants did Emilie interview that week? What was the average number per day?

b. On Wednesday, the first interview took 50 minutes; the next 2 each took 40 minutes; the next 4 took 35 minutes each; and the last 2 took 45 minutes each. How many total hours did Emilie spend in these interviews? What was the average length of the interviews?

32. GEOGRAPHY Obtain information about the salaries of workers in different geographic regions of the United States. What factors affect the differences that exist?

33. HISTORY Research a significant world event. Explain how this event affected the location and types of careers available around the world.
Linking School and Home

Talk to two or three people in your home or neighborhood to obtain information about their job search and interviewing experiences. Use the following questions in your discussion with these people:

- What are some ways that you have learned about available jobs?
- What actions did you take to improve your chances of being selected for a job?
- How did you prepare for job interviews?

Prepare a one-page summary of your findings. Which of these ideas did you find most interesting and potentially useful in the future?

Portfolio Activity

Some creative job seekers use job creation techniques, in which they develop and promote a position that matches their skills with the needs of an organization. These jobs could even be positions that do not exist until the person researched the company. To provide tangible evidence of your learning about your ability to serve the needs of an organization, do the following:

**Collect** information about organizations for which you might consider working. This information could be web data, financial reports, advertisements, company catalogs, or product packages.

**Create** two lists: (1) job skills and abilities needed by workers in this company, and (2) your current and future interests and abilities.

**Connect** your two lists by showing how you might serve some of the current and future needs of this organization. Prepare a one-paragraph summary of your potential ability to serve the needs of this organization.

Job Interview Event

You are applying for a position at the Winning Edge Corporation, a large fictional financial corporation headquartered in Washington, DC. Company benefits include paid holidays and vacations, sick leave, a retirement plan, and health insurance. Salary will be based upon experience and education. The event consists of three parts:

- Letter of application and resume
- Job application form
- Interviews

You are required to prepare a one-page letter of application. Your resume should not exceed two pages in length. The resume, letter of application, and job application should be put together in a file folder with the student’s name on the tab of the folder. You will be required to complete a job application form with the use of your resume and a one-page reference sheet. No other reference materials may be used. Your initial interview with a member from the business community will last 10 minutes. Finalists from the first round of interviews will have a 15-minute second interview. Total scores will be calculated for the letter of application, resume, job application, and interview to determine which students will be hired.

Performance Indicators Evaluated

- Understand the importance of a professional portfolio that includes a resume and letter of application.
- Demonstrate strong interviewing skills necessary to earn a job.
- Prepare a business resume and letter of application that generate results.

You will be evaluated for

- Organization of your professional portfolio
- Performance during the interview
- Quality of participation in the interview

For more detailed information about performance indicators, go to the FBLA web site.

Think Critically

1. Why is the letter of application important?
2. Why should you research a company before going on the interview?
3. Give two good examples of questions a candidate can ask the interviewer.
4. List the major sections of the resume.

http://www.fbla-pbl.org/
Global Business Project

Organize International Business Activities

Goals
- Select an organization type that would be most appropriate for an international business setting.
- Outline a business plan for a global entrepreneurial enterprise.
- Identify leadership traits and managerial skills needed when doing business in other countries.
- Research needed training and skills for working in various international settings.
- Prepare a resume, cover letter, and answers to interview questions for an international business employment opportunity.

Activities
Use your textbook, library materials, web sites, interviews with people, and other resources to complete the following:

1. Companies commonly organize as a sole proprietorship, a partnership, or a corporation. Based on the business idea that you developed in the previous unit (or another international business idea), analyze the positive and negative aspects of these three types of business structures.

2. A business plan is vital when starting a new enterprise. Based on your international business idea, obtain information on these business plan components:
   - overview of the business idea
   - main competitors
   - description of customers
   - discussion of the organization’s major operations
   - preliminary marketing activities
   - summary of start-up costs
3. Some leadership skills may be appropriate for several cultural settings. Other career competencies are unique to various regions and industries. Using the country from your portfolio (or select a country), describe two leadership traits unique to the geographic area or business you have chosen.

4. A person’s ability to understand and work with people in different cultures is necessary for international business success. List skills and training that would be of value to a person working for a multinational company.

5. In preparation for a global business career, prepare a list of your current skills and training you hope to obtain in the future. Identify abilities and experiences needed to work in an international business setting.

6. Create a list of questions and preliminary answers that might be the basis of an interview with a multinational company.

**Present**

1. Prepare a portfolio (folder, file, or notebook) to store the information and materials you created in the activities above.

2. Describe in writing or with a visual display the benefits and drawbacks of the three types of business structures when doing business in a foreign country.

3. Create a resume for yourself as it might look in the future. Also, write a cover letter that expresses your interest and ability to work for an international company.

4. Prepare a video (or in-class presentation) showing strong interviewing skills and common job interview weaknesses when applying for a position with an international business organization.
Unit 3

Business Operations and Technology

10 Marketing
11 Business and Technology
12 Financial Management
13 Production and Business Operations
14 Risk Management
Greeting Cards for Late Payers
No one is pleased to receive a late notice from a credit card company. In an effort to reduce the trauma, Discover Card worked with Hallmark Cards to create greeting cards to remind customers of their delinquent account.

This soft-sell approach helps Discover better work with late payers. While the company, of course, wants its money, they also want to communicate that they are willing to work with customers. This strategy has resulted in Discover encouraging people to pay faster and creating a long-term relationship with many customers.

Think Critically
What are some possible messages that might be included in a greeting card from Discover to late payers?

It’s Not a Bank, but...
PayPal handles more than $18 billion of transactions each year. While the online payment service is not a bank, it provides similar services.

The process starts with customers providing details of a credit card or bank account. PayPal, serving as a financial intermediary, verifies the transactions. Then payment amounts are transferred from the buyer to the seller.

Although PayPal mainly serves customers using eBay, other organizations make use of this service. Some local governments are allowing citizens to make tax payments using PayPal. Various charities accept donations through the system.

International expansion is next, with plans for serving customers in Europe and Asia. The global challenges PayPal will face include different regulations in various countries and differing consumer preferences for making payments.

Think Critically
Why is a payment service such as PayPal particularly useful for eBay buyers and sellers?
Chapter 10

Marketing

10-1 Marketing Basics
10-2 Develop Effective Products and Services
10-3 Price and Distribute Products
10-4 Plan Promotion
Planning a Career in...

Marketing

Marketing is a career area that offers a great variety of job opportunities. Entry-level jobs to top management jobs in corporations, high-tech career choices, jobs in international business, and entrepreneurship opportunities all are possible and available if you want to work in marketing. The work of marketers is diverse and exciting. A marketing researcher conducts focus group interviews in a mall or for a political candidate. A marketing team designs a multi-million dollar multimedia advertising campaign for a new product. An international sales representative for a pharmaceutical company travels the world to introduce a life-saving drug. A distribution center manager works to develop plans to reduce the storage time and costs of manufacturers’ products to give them a cost and service advantage over their competitors. Not only are marketing careers available for almost any interest and preparation, they offer some of the highest-paying business careers as well.

Employment Outlook

- The employment outlook for marketing jobs is varied, with some high-growth areas and others facing increasing competition.
- Employment in advertising, marketing, promotions, public relations, and sales is expected to grow faster than the average due to intense domestic and global competition.
- Opportunities in marketing research will be very good but require a masters or PhD degree and strong math and statistics skills.

Job Titles

- Financial Securities Sales Agent
- Merchant Wholesaler
- Marketing Consultant
- Manager of Corporate Brands
- Trade Show and Special Events Coordinator
- Marketing Database Manager
- Media Relations Specialist

Needed Skills

- Creativity, analytical and decision-making skills, effective teaming, communications, and human relations skills
- Many employers prefer people with broad work experience and a liberal arts preparation, but with an understanding of and comfort with technology

What’s it like to work in...

Sales Management

Before Kerri Snodgrass boards flight 699 to Cairo, she returns a call to Ferris Joachum. As vice president of sales, Kerri knows Ferris is in final negotiations with a major customer for a $1.5-million order of environmental monitoring equipment.

Ferris says, “If we can get the order shipped within two weeks and spread the payments over two years, I think I can make the sale.”

Kerri uses the air phone to talk with her company’s production manager and with a loan officer of the international bank they use for customer financing. After several discussions, they get approval on the shipping date and are able to offer free financing for one year or a loan at five percent interest for three years. As she gets off the plane, Kerri receives a text message from Ferris that the sale has been completed and the order has been placed.

As a sales manager, Kerri needs to understand all aspects of her business, gather information, and make quick but effective decisions to support her salespeople and satisfy the customers. Salespeople and sales managers are the face of the company to its customers.

What about you? What skills and personal qualities do you believe make Kerri Snodgrass a successful sales manager?
Marketing Basics

UNDERSTAND MARKETING

Marketing may be the most visible set of business activities to consumers. Yet it may also be the most misunderstood business function. When asked to define marketing, people often use terms such as advertising or selling. While both of these are important, many other activities are a part of effective marketing.

The American Marketing Association’s definition of marketing shows how complex it is. **Marketing** is the process of planning and executing the conception, pricing, promotion, and distribution of ideas, goods, and services to create exchanges that satisfy individual and organizational objectives. Those words describe a complex but key part of every business. Marketing includes a range of activities and a number of businesses in the United States economy.

Marketing Activities

As a consumer you are exposed to marketing activities all of the time. You take part in many of those activities. You see or hear advertisements for products and services. You see the brand names of products on packages and on the clothes that you and your friends wear. You read product descriptions on a company’s web site. You interact with salespeople in your favorite retail store. These are all examples of marketing.

There are less obvious but just as important marketing activities. These include storing products in warehouses and distribution centers and moving those products to the places where they will be sold or used. Establishing and
accepting credit and arranging means of online payment are marketing activities. Businesses use marketing when they gather data on consumer needs, use that information to improve products, and test new products before they are sold.

A great deal of marketing is not even aimed at final consumers. Businesses market products and services to other businesses. These businesses then use the products and services in their own business processes or sell them to final consumers. More time and money is spent in business-to-business marketing than in marketing products and services to final consumers.

**Marketing Businesses**

All businesses must complete some marketing activities even if that is not their focus. Many businesses are directly involved in marketing. Marketing businesses include advertising agencies and marketing research firms. Transportation companies such as trucking, railroad, and air freight move products from producers to consumers. Shipping and delivery companies provide express pickup and delivery of documents and packages. Financial services companies issue and manage credit cards. They can also provide loans to businesses for purchasing raw materials and finished goods. Wholesalers and retailers participate in the distribution, storage, and sale of products to connect manufacturers and their customers. Marketing activities, marketing businesses, and marketing careers are an important part of the U.S. economy.

**Marketing Functions**

Marketing activities can be organized into seven functions as shown in Figure 10-1. Each function occurs every time a product or service is developed and sold. Businesses provide many of the marketing functions. Consumers often take part in one or more of the marketing functions when they make purchases.

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**Work as a Group**

A company in Ft. Lauderdale, Florida, meets fishing boats when they dock. They buy fresh fish caught that day. Have each member of your group identify a marketing activity that must be completed by the company to purchase and then resell the fish to restaurants and supermarkets.

*Product/service management* is designing, developing, maintaining, improving, and acquiring products and services that meet consumer needs. Producers and manufacturers develop new products. Other businesses are also involved in product/service management when they obtain products for resale. Services are created and provided by the employees of service businesses.

*Distribution* involves determining the best ways for customers to locate, obtain, and use the products and services of an organization. Careful shipping, handling, and storing of products are needed for effective distribution.

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Selling is communicating directly with potential customers to determine and satisfy their needs. Selling can be face to face, such as when a customer visits a business or when a salesperson goes to the home or business of a potential customer. Selling is also performed using a telephone or other technology such as instant messaging or videoconferencing to communicate directly with a customer.

Marketing-information management is obtaining, managing, and using market information to improve business decision-making and the performance of marketing activities. Marketing-information management includes marketing research and the development of databases with information about products, customers, and competitors.

Financing is budgeting for marketing activities, obtaining the necessary funds needed for operations, and providing financial assistance to customers so they can purchase the business’ products and services. Customers must have the resources and methods to pay for their purchases. Businesses must receive timely payments so they can continue to operate.

Pricing is setting and communicating the value of products and services. Customers must be able to easily identify the price of items that interest them or they will move on to another choice. Consumers want to know that they are getting a fair value for the money they are spending. Prices must be set low enough that customers are willing to pay but high enough that the business makes a profit.

Promotion is communicating information about products and services to potential customers. Advertising and other promotional methods are used to encourage consumers to buy. Advertising may occur in a variety of ways—television, newspapers, magazines, radio, direct mail, and the Internet. Other methods include contests, product displays, sponsorships, and public relations activities.

**MARKETING STRATEGY**

Marketing is an important and costly part of business operations. Marketing activities often cost 50 percent or more of the selling price of a product or service. In order for a company to make a profit, marketing must be carefully planned. It must be done well, yet at a low cost. Consumers usually have many choices of products and services. If they are not satisfied with the offering of one company, they will look to a competitor to meet their needs. Careful marketing...
will aid a company in understanding and meeting customer needs. Successful marketing results in satisfying exchanges between businesses and consumers. Businesses offer products and services that satisfy their customers’ needs. Customers pay for those products and services, providing the businesses with revenues and profit.

**Marketing Planning**
Marketing planning is aimed at satisfying customer needs better than competitors do, resulting in sales and profits. A company’s plan that identifies how it will use marketing to achieve its goals is called a **marketing strategy**.

Developing a marketing strategy is a two-step process. The first step is to identify a **target market**. A target market is a specific group of consumers that have similar wants and needs. Many companies try to promote their products to a wide audience whose wants and needs are quite varied. It is not easy for the company to meet all of those needs. The result is that many people will not want the company’s products or will be dissatisfied with them. Focusing on a target market makes it easier to develop products and services that those customers want.

The second step in developing a marketing strategy is to create a marketing mix. A marketing mix is the blending of four marketing elements—product, distribution, price, and promotion. A successful marketing mix satisfies the wants and needs of the target market. It also provides a profit for the company.

**Develop a Successful Marketing Strategy**
Many businesspeople believe they know what consumers want. They produce a product and then begin to plan how they will market it to consumers. That approach to marketing typically results in an emphasis on advertising and promotion in order to attract the attention of potential customers and convince them to buy the company’s product. If the product does not appeal to consumers, the business will be forced to cut the price. Lower profits or even losses may be the result.

To increase the chances of developing a product or service that meets customer needs and can be sold at a profit, companies adopt a marketing orientation. A marketing orientation considers the needs of customers when developing a marketing mix. With a marketing orientation, businesspeople don’t assume they know what customers want. They use research to study customers and their needs. The results of that research are used to plan a marketing mix designed to satisfy those needs.

A company that owns a fleet of cruise ships gathers information on people who might consider a cruise as a vacation choice. Families with young children usually will want a different vacation experience than young singles or retirement-age adults. First-time cruisers will need different information...
than experienced cruisers. Menu items, entertainment, travel arrangements to and from the port, and payment options all must be planned to appeal to potential customers.

The company will first study possible customers and the similarities and differences in vacation wants and needs. Then it will select the target market that presents the best opportunity for planning a successful cruise. Using the information gathered about the target market, the company then develops the marketing mix. The product will be an exciting and relaxing cruise experience. There will be enjoyable onboard activities and interesting onshore excursions at cities on the ship’s schedule. Distribution will include providing all of the documents needed by travelers, arranging customer travel to and from the port city, handling baggage, and ensuring effective customer service throughout the process. Pricing decisions provide an affordable cruise with payment options to meet the budgets of the target customers. Promotion offers information to interest prospective customers in the cruise and persuade them to decide it is the best vacation choice.

The cruise company will make each of those marketing mix decisions to meet the specific needs and expectations of their target market. The decisions will be different in many ways than if the cruise was planned for a different group of consumers.

UNDERSTAND CUSTOMERS
Effective marketing begins with customers. Think of a recent product or service you purchased and why you made the choice you did. You likely had several products that would generally meet your needs. You considered those choices and selected the one that you believed would provide the most satisfaction for the money you had to pay.

Many new businesses fail because the owners have an idea for a product but fail to consider customers and their needs. If a product appeals to a group of customers with unsatisfied needs, it has a real chance to succeed. If customers do not see a need for a product or believe they have other choices that are better or less costly, the product will likely not succeed.

Businesses can develop products for two types of consumers. Final consumers are persons who buy products and services mostly for their own use. Business consumers are persons, companies, and organizations that buy products for the operation of a business, for incorporation into other products and services, or for resale to their customers.

Describe the consumer decision-making process.

What information would you need before you decide to purchase a cruise?

CHECKPOINT
What are the two steps in developing a marketing strategy?

> Describe the consumer decision-making process.

What information would you need before you decide to purchase a cruise?
Consumer Decision-Making

The specific sequence of steps consumers follow to make a purchase is known as the consumer decision-making process. Both the steps and the sequence of decisions are the same for all consumers. The length of time taken to complete the process and the information used to complete each step might be quite different from one consumer to the next. The five steps in the consumer decision-making process are shown in Figure 10-2.

Decision-making begins with a need. You may be hungry or thirsty, or you may want to plan an evening’s entertainment with friends. Maybe you need a summer job or are trying to choose a college to attend. If the need is urgent, you will try to satisfy it right away. If it is less important you may put it off or even ignore it. If the need is one that is familiar to you and you have satisfied it before, you will often use that past experience to help make a decision. If it is a new need, you may have a hard time deciding how to make the best choice since you have no similar experience.

People use information to make decisions. You may talk to friends or a trusted adult. An advertisement, magazine article, or Internet site may catch your attention because it provides information related to an important need. You choose sources that you trust and that provide information you understand. Using this information, you will select a very few products that seem to meet your needs. Once the choices are narrowed, you will compare them to determine if one appears to be a better choice or a greater value than the others.

Based on the information you have obtained and the urgency and importance of the need, you will make a decision. The decision is usually to buy the product you have decided is best for you. The decision may be not to buy because you have not found a satisfying choice or you do not have the money you need at the time. You may then go back to a previous step and look at other choices or gather more information.

If you decide to purchase a product, you will complete the purchase and use the product you chose. Based on that experience you will decide if you made a good choice. If you liked the product, you will probably make the same
decision the next time you have the same need. You may also make the decision more quickly and easily. If the product was not what you expected, you will be unlikely to purchase that product again.

**Buying Motives**

Why do you shop in a certain store or choose one brand of a product over another? The reasons consumers decide what products and services to purchase are called **buying motives**. Understanding the motives of consumers helps businesses plan a marketing mix.

Some purchases are guided by emotions. *Emotional buying motives* are reasons to purchase based on feelings, beliefs, and attitudes. If you are concerned about protecting your family and possessions, you may decide to buy a home security system. Gifts and cards on Mothers Day or Valentines Day are triggered by feelings of love and affection.

*Rational buying motives* are guided by facts and logic. You may want the most cost-effective car, so you consider fuel use and repair costs of various models. When choosing a college to attend, you can compare the costs of tuition and the reputation of the college in the major you plan to study.

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**FYI**

Since Fortune magazine began its list of Most Admired Companies in 1997, only four companies have appeared in the top 10 every year. They are Southwest Airlines, Berkshire Hathaway, General Electric, and Microsoft.

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**10-1 Assessment**

**> Key Concepts**

Determine the best answer.

1. The best definition of marketing is
   a. Promotion and selling
   b. Producing and distributing products and services to customers
   c. Finding customers and convincing them to buy your products
   d. None of the above is correct.

2. The two steps in a marketing strategy are
   a. Developing a product and promoting it to consumers
   b. Identifying a target market and developing a marketing mix
   c. Conducting marketing research and planning production
   d. Pricing a product and distributing it to customers

3. Which of the following is an example of a rational buying motive?
   a. Love
   b. Fear
   c. Economy
   d. Self-image

4. **Marketing** List the seven marketing functions. Using a business directory or the Yellow Pages of a telephone book, identify a business that specializes in providing each service for final consumers or other businesses. Briefly describe what the business does and the types of customers it serves.

5. **Critical Thinking** Select one of your recent purchases. Using computer software, develop a chart or illustration that identifies the steps in the decision-making process and how you completed each step to make the purchase decision.
10-2
Develop Effective Products and Services

Goals

> Justify the importance of marketing research.
> Identify the components of a product.
> Describe how services differ from products.

Key Terms
marketing research
product
services
intangible
inseparable
perishable
heterogeneous

Focus on Real Life

CREATE AND IMPROVE PRODUCTS

How do businesses develop new products? In many cases, what are called new products in a company’s advertising are not new at all. Some type of change has been made in the product that may be a major improvement. The change may also be a very minor one that provides little benefit to the customer. The business calls the product new to attract the attention of customers and encourage them to buy.

Totally new products that have never been seen before by customers are not often introduced. What new products can you recall having been introduced during your lifetime? The Internet, airbags in automobiles, scanning equipment used in retail stores, and artificial hearts did not have similar substitutes before they were introduced. They were the result of research by engineers and scientists seeking to find solutions to important problems. Most products you use today are minor or major improvements in existing products. A CD or MP3 player uses new technology to store and replay music. Handheld personal digital assistants are new versions of past computer models. Even cellular phones are improved versions of older wireless telephones. Those and many other product improvements occur through the development of new technology or redesign of current products.

Scientists and other researchers often develop product improvements. Many ideas for product improvements result from the ideas of consumers and from their experience in using current products. Finding solutions to problems through carefully designed studies involving consumers is known as marketing research.

When you go to a store or use a catalog or the Internet to make a purchase, you will usually find several choices of the product you want. What makes the products offered by one company different from those offered by other companies? In some cases, it is little more than the brand name of the product. In other cases, there are many differences in the design of the products, the features, and the options available.

Products can become so specialized that making choices that meet the needs of each customer becomes a very complex process. Companies need to develop tools to help consumers sort through their choices. Purchasing a shirt or pair of slacks on the Internet can involve creating a virtual “model” of your body size and shape and then comparing styles, colors, and fabrics by viewing them on the model. These types of online tools help customers develop a picture of their choices and make complicated decisions easier.

Goals

> Justify the importance of marketing research.
> Identify the components of a product.
> Describe how services differ from products.

Key Terms
marketing research
product
services
intangible
inseparable
perishable
heterogeneous

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10-2 Develop Effective Products and Services
Plan Marketing Research

Many types of research procedures can be used to solve marketing problems. Each type of research follows the scientific problem solving process outlined in Figure 10-3.

**Figure 10-3**

**Steps in Marketing Research**

1. Define the marketing problem.
2. Study the situation.
3. Develop a data collection procedure.
4. Gather and analyze information.
5. Propose a solution.

All marketing research studies involve gathering and analyzing information. A great deal of information about consumers and competitors is available to businesses without doing new studies. Analyzing existing information gathered for another purpose but used to solve a current problem is known as secondary research. Studies carried out to gather new information specifically directed at a current problem is primary research.

**Types of Research Studies**

The most common type of marketing research study involves consumer surveys. Surveys gather information from people using a carefully planned set of questions. The surveys are often sent to consumers through the mail or using the Internet. They can also be conducted over the telephone.

Another less structured way of gathering the ideas, experiences, and opinions of consumers is through focus groups. In this research method, a small number of consumers take part in a group discussion. A focus group leader acts to identify areas of agreement and disagreement and to develop new ideas. Focus group members might discuss their experiences with a product, react to new product ideas, or make suggestions for product improvements.

Observations of consumers provide useful information for marketing researchers. Observations collect information by recording the actions of consumers rather than asking them questions. A store may be interested in how customers study and choose products in a display case or the routes they take through a store when shopping. A product design team may observe any problems consumers have using a product to make design improvements.

A final method of marketing research is conducting experiments. An experiment presents two carefully controlled alternatives to subjects in order to determine which is preferred or has better results. A marketing experiment may compare two sizes of packages to see if one size results in more sales than the other. A study could determine the
Companies try to develop a memorable brand name with an appealing image.

Packaging is a part of many products. **Packaging** provides protection and security for the product before it is used. It also may make product storage and use easier. A new container for ground coffee is created with indentations that allow customers to pick it up easily with one hand. Some customers struggled with handling the original round container. The package is a convenient way to provide information to customers that help them make a purchase decision or explain how to use the product.

A way to build customer confidence in a company’s products is by offering a **guarantee or warranty**. If the product breaks or does not meet customer expectations, the company will repair, replace, or provide a refund.

**Product Planning Procedures**

New product planning is a costly and time-consuming process. It is not unusual for a company to invest several million dollars and spend years to develop a new product. Many people are involved in creating the product idea, determining how it will be produced and marketed, analyzing costs, and predicting sales. When that much money is at stake, companies need a sophisticated planning process.

### Parts of a Product

A **product** is everything a business offers to satisfy a customer’s needs. A product is made up of several components. It starts with the **basic product**, which is the simplest form of a product. The basic product is not unique and is usually available from several companies. Additions and improvements to the basic product are known as **product features**. One model of cellular telephone offers a built-in digital camera, voice dialing, and a web browser as features. When customers are offered choices of features, the choices are known as **options**. When buying an automobile, customers can choose options such as color, engine size, and manual or automatic transmission.

A **brand name** provides a unique identification for a company’s products.

### CHECKPOINT

**List the steps in a marketing research study.**

The U.S. Census Bureau provides very detailed data that helps businesses make marketing strategy decisions. Access businessxtra.swlearning.com and click on the link for Chapter 10. Click on the American FactFinder link and locate census information on your community. Study the data and locate (1) the number of 15–18 year olds and (2) the number of renter-occupied and owner-occupied homes in your community. How might that information be used by businesses?

**businessxtra.swlearning.com**
The steps in new product planning are:

- **Idea Development** Generating new product ideas is a creative process. Ideas come from the work of scientists, from the suggestions of salespeople and other employees, and from consumer surveys and focus groups. Most ideas are for improvements to existing products.

- **Idea Screening** Companies encourage the development of a large number of new product ideas. Then they evaluate those ideas to determine which have the best chance to be successful. Ideas are screened to determine if a demand exists for the new product. Do other companies offer similar products? Can the product be produced at a reasonable cost? Is the product legal and safe?

- **Strategy Development** If a product idea appears to be workable, the next step is to develop a full marketing strategy. The target market for the product is studied carefully. There must be a strong need for the new product. Alternative marketing mixes are developed and tested with potential customers. The costs of the alternatives are compared to determine which provide the greatest value.

- **Production and Financial Planning** Next, the company develops a production procedure and identifies the facilities, equipment, and people that will be needed to produce the product. The costs of production and marketing are determined and a financial plan is developed to be sure the product will make a profit.

- **Limited Production and Test Marketing** If a new product idea makes its way through the planning process, a company may produce a limited quantity of the product and test it in a small part of the market. This step allows the company to make sure the product can be produced and marketed as planned before a large investment is made for full production.

- **Full-Scale Production** If each of the preceding steps is completed successfully, the new product will move into full-scale production and marketing. The company will continue to gather information on production and sales to be sure financial projections are being met. Competitors will also be watched since they will likely introduce competitive products if the new product is successful. Few unsuccessful products should make it through. Products that are fully screened have a much greater chance of being successful than new products that do not go through a planning procedure.
SERVICES

Products are tangible items you can see and examine such as books, boats, and hamburgers. Marketing is used for both products and services, but services are more difficult to market. Services are activities that are consumed at the same time they are produced.

Services are intangible, meaning that they have no physical form. Because services are intangible, it is more difficult to examine a service and determine if it will meet your needs. Marketers must find ways to describe the service in understandable ways to prospective customers.

Effective service marketing is done in much the same way as product marketing. Using the two-step marketing strategy, service marketers first identify target markets for services. They then develop a marketing mix that appeals to the market. In addition to the service itself, the market mix includes distribution, pricing, and promotion of the service. The nature of services compared to the nature of products requires a change in the way they are marketed.

Technology Topics

Virtual Design

When the Jeep Liberty rolled off the assembly line at DaimlerChrysler, it represented a new era in product design. The dashboard had been designed online by a worldwide team representing over 35 companies and headed by the design team of Johnson Controls in Milwaukee, Wisconsin. Johnson was responsible for building the entire cockpit including instruments and controls to be delivered to Chrysler just in time to be installed on each Liberty during final assembly.

Using specially developed software, the ideas of the companies were added to a virtual dashboard where instrument placement could be viewed, controls could be tested, and the look and feel of the dashboard could be matched with the Liberty’s interior and exterior image.

Virtual designing allows for instantaneous communication and the ability to view the entire assembly at any time from any company. When one member of the team changed a part or process, the impact of that change could be immediately viewed and evaluated by others. The use of virtual design processes cut the normal design time by over 60 percent.

Think Critically

1. What problems might be anticipated when bringing over 35 companies from around the world together online for design collaboration?
2. In addition to new product design, what other applications might be possible with the design software and collaboration procedures described?
needs it. Marketers must determine where and when consumers want a service and must be able to provide it at that location and time.

Services are **perishable**, meaning that the availability of a service must match the demand for that service at a specific time. A service cannot be stored for later consumption like many products. If all seats at a concert are filled, no more people will be able to hear that performance. If a taxi driver does not have a fare, the service goes unused.

Services are **heterogeneous**, meaning that there will be differences in the type and quality of service provided. Because people usually provide services at the time they are consumed, there is less control over quality than is possible with products. The skill, training, and motivation of the service provider affect service quality.

How can a waiter or waitress affect your perception of a restaurant?

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**Work as a Group**

The employees of a company that provides a service to consumers are responsible for the quality of the service. If your group owned a pet-sitting business, what would you do to make sure the employees provided a high quality of service for each customer?

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**Assessment**

**10-2**

**Key Concepts**

Determine the best answer.

1. True or False. Most new products introduced by companies are not totally new, but are improvements on existing products.
2. True or False. The first step in marketing research is to develop a data collection procedure.
3. The availability of a service must match the demand for that service at a specific time because it is:
   a. heterogeneous  
   b. perishable  
   c. inseparable  
   d. intangible

**Make Academic Connections**

4. **Critical Thinking** Use the Internet to locate an article describing a new product that failed. Review the information to determine the possible reasons for failure. Write a short memo to the company describing how using the new product planning process may have reduced the likelihood of failure for the product.
5. **Research** Identify a product that many of your classmates use regularly. Prepare a five-question survey to determine their feelings about the strengths and weaknesses of the product and possible ways the product could be improved. Give the survey to at least 10 students. Present the results in a short report including at least one table, graph, or chart.
Conflict can be defined as competing differences between two or more people. These differences are often caused by struggles over goals, motives, values, ideas, and resources. Believe it or not, conflict can be both good and bad, depending upon the results of the conflict. The costs of negative, unresolved conflict are decreased productivity, low employee morale, and heightened workplace tensions. These all have the potential to damage the success of a business. But conflict of the right nature can be beneficial to business. For example, friendly conflict can encourage competition, diverse thinking, creativity, and a wider variety of solutions to business problems. Prevention is the solution to many problems, including workplace conflict. Some tips for preventing negative conflict in the workplace include the following:

- Be open to others’ ideas. Listen before making up your mind.
- Avoid stereotyping your coworkers and superiors.
- Do not use language or expressions that may be offensive or demeaning to others.
- Disagree constructively. Offer alternative suggestions or solutions rather than simply rejecting others’ ideas.
- Above all, treat your coworkers and superiors with the respect you want them to show you.

Unfortunately, conflict cannot always be avoided. All types of conflict can arise, from personality clashes to conflict over business ideas. The following strategies can be helpful in managing conflict with coworkers.

- **Intervention** Ask a coworker or supervisor to provide a setting for conflict resolution between you and those with whom you are in conflict. A supervisor also might speak on your behalf to the coworker with whom you are in conflict.

- **Confrontation** Approach the coworker with whom you are having trouble. Both of you must recognize the problem and then work together toward a solution.

- **Compromise** If the conflict involves a disagreement over a particular business issue, you might work out a compromise solution. For example, you may agree to your coworker’s idea in exchange for similar treatment during the next conflict.

- **Avoidance** The avoidance technique should be your last solution, but in some situations it may be best. If you simply cannot solve a personality conflict, deal with the individual when you need to, but otherwise steer clear.

Conflict between yourself and a superior is acceptable, and in some cases even beneficial, if it leads to increased mutual respect. Conflict with superiors must be handled with care and should not be seen as a challenge to your superior’s authority. Conflict with superiors should be kept professional and private.

**Think Critically**
1. What is conflict?
2. What are the consequences of negative conflict?
VALUE AND PRICE

When you decide to purchase a product, how do you determine what to pay? Do you always pay the price that is marked on the product by the seller? Do you compare prices of several businesses to find the lowest price? Do you consider how much money you have available to spend in determining what price to pay? Are you concerned whether the seller is making a profit and whether that profit is low or high? Buyers usually want to pay the lowest price possible and sellers want to charge the highest price possible. Determining the best price for a product is a difficult marketing challenge.

Pricing Factors

Many factors go into a decision about a fair price. What you might consider an appropriate price may be different from the decision of other customers. It probably is very different from the price the seller believes is appropriate. There are both general and specific factors that influence the price paid for a product.

Supply and Demand A product that has a ready supply will have a lower price than a product with a very limited supply. If demand for a product is high, prices will increase. Products with low levels of demand will have comparatively low prices.

Uniqueness When a product has few close competitors because it is unique, the price will be higher than products that are very similar to others.

Age When products are first introduced to the market, prices will be quite high. As products age, the price gradually decreases.

Season Many products are used at a particular time of the year. Winter apparel, air conditioners, and holiday decorations have high levels of sales for
a short time and then almost no sales for the rest of the year. Prices will be highest just before and at the beginning of the season. Prices will be lower during other times of the year.

**Complexity** Highly complex and technical products have higher prices than simple products. Products with many features and options will also command higher prices.

**Convenience** People pay for convenience. If a product is easily available and the seller provides a high level of customer service, prices will go up. Customers expect to pay low prices if they shop at a large warehouse store that is not as conveniently located and offers little service.

### Price a Product

**Price** is the money a customer must pay for a product or service. The price of a product changes as it moves from producer to consumer. The manufacturer sets a price that is paid by other businesses that will sell the product to the final customer. The price is set by the business following a formula that identifies the components of the price. The formula is:

\[
\text{Selling price} = \text{Product costs} + \text{Operating expenses} + \text{Profit}
\]

**Selling price** is the price paid by the customer for the product.

**Product costs** are the costs to the manufacturer of producing the product or the price paid by other businesses to buy the product.

**Operating expenses** are all expenses of operating the business that are associated with the product. They can include salaries, storage and display equipment, facilities, utilities, taxes, and many others.

**Profit** is the amount of money available to the business after all costs and expenses have been paid.

Gross margin is an important factor in product pricing. The *gross margin* is the difference between the selling price and the product costs. It represents the amount of money on hand to pay for operating expenses and provide a profit.

**Markup** A pricing concept related to gross margin is markup. A *markup* is the amount added to the cost of a product to set the selling price. The markup is equal to the expected gross margin. A markup is stated as a percentage of the product’s cost or as a percentage of the product’s selling price. If a product costs 15 dollars and has a 100 percent markup on cost, the selling price is $30.00.

\[
(15 \times 1.00) + 15 = 30
\]

That $30 product would have a markup on selling price of 50 percent.

\[
\frac{15}{30} = 0.50 \text{ or } 50\%
\]
**Markdown** Businesses are not always able to sell products at the original price they set. If customer demand is not as high as projected, if the selling season is ending, or if there is a flaw in the product, the business may have to take a markdown. A **markdown** is a reduction from the original selling price.

A markdown should be thought of as a pricing mistake because it reduces the amount of money the business has to cover operating expenses and profits. However, the original selling price can be set high because the product is new and there is higher demand. Small markdowns result in most of the remaining products being sold while still making a profit. The leftover products may need to be sold at large markdowns that still provide some money to cover the product cost and expenses.

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**Channels of Distribution**

Do you own any products that were produced in China, India, or New Zealand? If so, the process of getting the product from that country to your city was probably both difficult and time consuming. In contrast, have you or your family shopped at an area farmers’ market? Here, local producers sell fruits, vegetables, and other homegrown products. The products have to be transported only a short distance and may be harvested the same morning they are sold. Each situation describes a distribution process.

**Distribution** involves determining the best methods and procedures to use so customers can find, obtain, and use a product or service. As a marketing mix element, **distribution** is the locations and methods used to make a product or service available to the target market. The route a product follows and the businesses involved in moving a product from the producer to the final consumer are known as a **channel of distribution**.

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**Need for Distribution Channels**

In the earliest economic exchanges, people often bartered to exchange goods and services. If each person had a larger amount of something the other person wanted, they would agree on how much of each product would be exchanged and the trade would be made. That was a relatively simple distribution process. In complex economies, exchanges are much more difficult due to several differences that exist between producers and consumers.

- **Differences in Quantity** Businesses produce or sell large amounts of each product to many customers. Each consumer needs only a very small number of products at a given time.
• **Differences in Assortment**  
Businesses typically specialize in producing a specific type of product while consumers want to purchase a variety of products.

• **Differences in Location**  
In today’s global economy, thousands of miles often separate producers and consumers. Businesses may need to distribute their products to customers in many countries.

• **Differences in Timing**  
Businesses gain efficiency by producing large amounts of a product at one time. Some agricultural products can only be produced at a specific time of the year. Consumers may want to buy products at different times than when they are produced.

Distribution channels develop to make adjustments in those differences. An effective channel of distribution takes the large quantities produced and breaks them into quantities customers want to buy. The channel gathers products from many producers to offer customers the array of products they need in convenient locations. They move products efficiently from where they are produced to where they can be sold. Distribution channels store products from the time they are produced until customers want to buy them.

**Channels and Channel Members**

The businesses that take part in a channel of distribution are known as channel members. All marketing functions and activities are performed by a channel member or by the consumer. Businesses join a channel of distribution when either the producer or consumer does not want to perform one or more marketing activities or when the business can perform the activities better or at a lower cost.

Channels are either direct or indirect. In a direct channel of distribution, products move from the producer straight to the consumer with no other organizations participating. An indirect channel of distribution includes one or more other businesses between the producer and consumer. These other businesses provide one or more of the marketing functions.

In indirect distribution channels for products that are sold to business customers, typical channel members are specialists in providing one of the marketing functions. The channel member may be a transportation company, a sales organization, or a financial institution. Some channel members may be responsible for almost all of the marketing functions. They obtain products from a number of small manufacturers and market them to many business customers.

*Retailers* are a well-known and important part of distribution channels for consumer products. Retailers are the
Retailers offer a range of products at convenient locations for consumers. They help consumers to select the best products. They can provide financing and delivery services. They may even offer repairs and other customer services. Retailers assist manufacturers by storing, displaying, and advertising the products and often paying the manufacturer well before final consumers buy the products.

**CHAPTER 10  Marketing**

**CHECKPOINT**

What is the difference between a direct and an indirect channel of distribution?

**10-3  Assessment**

**Key Concepts**

Determine the best answer.

1. Which of the following conditions will result in a lower rather than a higher price?
   a. a high customer demand
   b. a large quantity of available products
   c. a product that has very few similar competing products
   d. All would result in lower prices.

2. When businesses specialize in producing a specific type of product, a channel of distribution will be needed to adjust differences in
   a. timing
   b. location
   c. assortment
   d. quantity

**Make Academic Connections**

3. **Business Math** Visit a department store, discount store, or the online product catalog of an Internet business. Identify five products that have been marked down and for which the original price and sale price are listed. Prepare a spreadsheet on which you list the product, the original price, and the sale price. Calculate the amount of the markdown and the markdown percentage. Then for all five products, determine the amount you would pay if you purchased each at the original price and if you purchased each at the sale price. What is the total savings in dollars and as a percentage of the original prices?

4. **Critical Thinking** List the seven marketing functions. Use a business or telephone directory or the Internet and identify a business that specializes in that function as a part of an indirect channel of distribution.
Plan Promotion

COMMUNICATION AND PROMOTION
Promotional messages from businesses, organizations, government agencies, and political candidates bombard you on a regular basis. Each day newspapers, television and radio programs, and mailboxes are filled with advertisements. Sides of buses, tops of taxis, even posters in restaurant restrooms contain promotional messages asking you to buy something, support a cause, or change an opinion. Every time you visit the World Wide Web, you are exposed to a variety of virtual promotions. It is apparent that businesses and organizations believe in the power of promotion, but is it always effective? What determines whether promotion is used well or not?

Promotion is any form of communication used to inform, persuade, or remind. Businesses, organizations, groups, or individuals use promotion. It is used to influence knowledge, beliefs, and actions about products, services, or ideas. To plan effective promotion, marketers must first understand the communication process. They then must apply effective communication to interact with consumers in a way that results in information, understanding, and action.

The Communication Process
Most of you have played the game where one person starts a message by whispering in the ear of a second person. That person whispers to the next and so on until several people have heard the message. When the last person states what he or she heard, it is seldom the same as the initial message. The game makes the point that effective communication is not easy. Effective communication is the exchange of information so there is common understanding by all participants. Effective communication is illustrated in Figure 10-4 on the next page.

Goals
> Justify the importance of communication in marketing.
> Identify and describe the common types of promotion.

Focus on Real Life
The most powerful marketing tool influencing consumer behavior is promotion. It can attract your attention and remind you of important needs. It can change your emotions and encourage you to buy. It is so powerful that it can even influence you to purchase a product you later decide was not the best choice.

Advertising is a promotional tool often used to influence emotions. The image created with a picture or other graphic, the language used to communicate information, even the colors of the headline, text, picture, or background can establish feelings of pleasure, happiness, fear, or sadness. An advertisement that leaves you with a positive feeling toward the product based on your emotions will be memorable and often will influence your feelings about the product or company.

Key Terms
promotion
effective communication
personal selling
advertising

Focus on Real Life

> Justify the importance of communication in marketing.
Communication begins with a person or organization (the sender) that has information to communicate to another person or organization (the receiver). The sender chooses the way (communication channel) the information will be transmitted to the receiver. Before sending the message, the sender decides the form in which the information will be sent—text, spoken words, pictures. Preparing the information to be communicated is called encoding. The receiver obtains the information from the channel and interprets it for understanding (decoding). To be sure that the communication achieved the desired result, the sender needs to have a response from the receiver (feedback). If the receiver understood the information and responds in a way the sender wanted, communication was effective. If the receiver does not respond or acts in an unexpected way, communication failed.

**Communicating Through Promotion**

Promotion is an important form of communication. A business needs to provide information to consumers in order to persuade them to make a purchase. As the sender, the business decides what information to provide. The consumer is the receiver. The information is encoded in the form of a promotional message such as an advertisement. The business chooses an information channel. Common promotional channels include advertising media, salespeople, and the Internet. If the customer sees or hears the message, it is decoded. The response of the consumer gives feedback to the business about the effectiveness of the promotion.

Choosing target markets and studying their needs and decision-making process can make promotion more effective. When the focus of a business is a target market, communication can be very specific to the needs of that group using media that are familiar to and trusted by those consumers. The business will understand where the customers are in the decision-making process. It will tailor promotional messages at that stage. Early messages get attention and give simple information about the product or service and the needs it satisfies. Later promotions can compare the product to competing brands. They may point out advantages that are important to the target market. When customers purchase the product, promotions can switch to providing reinforcement of their decision and offering after-sale services.

**Work as a Group**

Choose a newspaper, television, or magazine advertisement that is familiar to each person. Using that advertisement, identify each of the components of the communication channel. Discuss whether the advertiser seems to be demonstrating effective or ineffective communication.

**CHECKPOINT**

How does identifying a target market improve promotion communications?
An inventor asks you for advice on how to promote a new type of cellular telephone that combines high-speed video and audio. What types of promotion would you recommend? Would it be a glitzy television campaign or direct mail to cellular service subscribers? Maybe you would suggest text messaging delivered to cell phones. What about salespeople ready to demonstrate the new product to customers who visit shopping mall kiosks? There are many choices for promotional communications. The types of promotion are divided into personalized promotion and mass promotion.

**Personalized Promotion**

Personalized promotion is the most effective form of marketing communication. It is also the most expensive. The most well known type of personalized promotion is personal selling. **Personal selling** is direct, individualized communication with prospective customers to assess their needs and assist them in satisfying those needs with appropriate products and services. Personal selling usually is done face-to-face with each customer. The customer visits the business to meet with a salesperson or the salesperson goes to the home or business of the customer. Personal selling also can be completed using telephone calls or live audio and video Internet connections. Because personal selling is often used for complex and expensive products and services, it may require several contacts between the salesperson and the customer to complete the sale.

To prepare for a sale, salespeople gather information on the prospective customer they will visit. They study product information. They need to be able to make the best match of products to customer needs. When a customer is qualified, meaning they appear to have the need for and resources to buy a product, the salesperson schedules a meeting with the customer. During the meeting, the salesperson asks questions, provides information, and demonstrates the product for the customer. If the product meets the customer’s needs, the salesperson helps the customer make a decision to purchase. The salesperson may also arrange payment or financing as well as product delivery and any services the customer requires. After the customer has used the product, the

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**FYI**

A 2004 survey by the Promotion Marketing Association found that consumer products companies spent twice as many of their marketing dollars on promotions, such as contests, coupons, and product samples, than they did on advertising.

What consumer questions would help determine the best computer system for a salesperson to recommend?
salesperson contacts the customer to answer additional questions and determine that the customer is satisfied.

**Mass Promotion**

Mass promotion is directed to many people at the same time. If the people are from the same target market, they will have like needs. Because the promotional message is aimed at many people, it cannot be as individualized and specific as personalized promotion. However, reaching many people with the same message through mass media is much less expensive. While a large company may spend hundreds of thousands of dollars on a television advertisement, it reaches more than a million people. Therefore the cost of the message for each customer is quite low.

Advertising is the most known and used type of mass promotion.

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**A Question of Ethics**

**The Price of Success**

Should a successful company be penalized because it has developed a successful product? An important principle of private enterprise is that businesses and consumers benefit from competition. The belief is that competition increases the choices and quality of products and reduced prices for consumers. European courts recently stepped in to fine Microsoft for trying to reduce competition for several of its products.

Microsoft develops and sells the operating system used in most personal computers. Because computer manufacturers know that consumers expect to buy computers that have the Microsoft operating system installed, they must purchase the systems from Microsoft. Microsoft includes many features that are added to the operating system such as an Internet browser, e-mail and productivity programs, and a media player. All of the added programs are owned and sold by Microsoft. It is not easy for consumers to uninstall the programs once they buy a computer and difficult for Microsoft’s competitors to get computer manufacturers to purchase and use their programs since Microsoft has already included them in the system.

Microsoft argues that its programs are popular among consumers, the features improve the operating system, and when pre-installed are easier to use and cheaper for consumers than if they had to buy all of the added programs separately. Its competitors argue that Microsoft is monopolizing the market by forcing computer manufacturers to include its products and reject the similar products of competitors.

**Think Critically**

1. Should courts step in to prevent Microsoft from requiring computer manufacturers to install the additional Microsoft software in order to buy its popular operating system?
2. Do you believe competition among businesses usually benefits consumers? Why or why not?
3. Use the Internet to gather the latest information on legal actions taken by governments and competitors against Microsoft designed to encourage greater competition.
Other types of mass promotion are publicity, sales promotion, and public relations. **Publicity** is non-paid promotional communication presented by the media rather than by the business or organization that is being promoted. **Public relations** is an ongoing program of non-paid and paid communications. It is planned to favorably influence public opinion about an organization, marketing effort, idea, or issue. **Sales promotion** includes activities and materials designed to reinforce a company's brand and image. It is also a direct incentive to take an action likely to immediately increase sales of a product or service. Sales promotion includes contests and games as well as the many products companies give away to consumers or sell at a low cost that highlight a brand name or product.

**Mass Personalization**
Businesses can combine the advantages of personalized and mass promotion by using mass personalization promotion. Mass personalization begins with promotion through mass media such as newspapers, mass mailings, or the Internet. Prospective customers see the advertisement and become interested in the product or service. The company then provides an easy-to-use method for the consumer to gather more personalized information.

A customer who views an Internet advertisement or uses a search engine to gather information can be encouraged to complete an online survey. The questions provide the business with more specific information about the consumer, including their interests and needs. When the survey is submitted, the consumer is taken to a more specific web site tailored to their profile or they are sent specific information via e-mail. They can even contact an online customer service representative who can answer detailed questions. A simpler form of mass personalization on the Internet is a set of links that take customers with specific questions to other web pages. The links can help them choose a specific product and complete an online purchase.

>> CHECKPOINT
Describe the advantages and disadvantages of the major types of promotion.

10-4 Assessment

**>> Key Concepts**
Determine the best answer.

1. Which of the following is not a part of effective communication?
   a. the sender  
   b. the receiver  
   c. the advertisement  
   d. information

2. The most expensive but also most effective type of promotion is:
   a. personal selling  
   b. advertising  
   c. publicity  
   d. public relations

**>> Make Academic Connections**

3. **Critical Thinking** Use Figure 10-4 to illustrate three different examples of business communications: a business-to-business communication, a business-to-final consumer communication, and a consumer-to-business communication.

4. **Research** Identify three different products or services you would consider buying. For each product, identify the information you need to help you make a purchase decision and what media or information source you would choose to gather the information. Describe how a business could use promotion to influence your decision.
10-1 Marketing Basics
1. Marketing is the process of planning and executing the conception, pricing, promotion, and distribution of ideas, goods, and services to create exchanges that satisfy individual and organizational objectives. The seven marketing functions are product/service management, distribution, selling, marketing-information management, financing, pricing, and promotion.

2. A marketing strategy is a two-step process used to plan and market products. The first step is to identify a target market and the second step is to develop a marketing mix.

3. The steps in the consumer decision-making process are: recognize a need, gather information, select and evaluate alternatives, make a purchase decision, and determine the effectiveness of the decision.

10-2 Develop Effective Products and Services
4. The steps in a marketing research study are: define the marketing problem, study the situation, develop a data collection procedure, gather and analyze information, and propose a solution.

5. The components of a product are the basic product, product features, options, brand name, packaging, and a guarantee or warranty.

6. Products are tangible items that you can see and examine. Services are intangible activities that are consumed at the same time they are produced.

10-3 Price and Distribute Products
7. Businesses use the following formula for setting the price of a product: Selling price = Product costs + Operating expenses + Profit.

8. A direct channel of distribution moves products from the producer directly to the consumer with no other organizations participating. An indirect channel of distribution includes one or more other businesses between the producer and consumer. These other businesses provide one or more of the marketing functions.

10-4 Plan Promotion
9. When the focus of a business is a target market, communication can be very specific to the needs of that group using media that are familiar to and trusted by those consumers.

10. There are two major types of promotion. Personalized promotion communicates directly with each customer using information tailored to that person. Mass promotion communicates with many people at the same time with a common message.
Identify one target market for the printer that is a business consumer and one that is a final consumer. Describe how the marketing mix would be similar and different for each target market.

4. Often it is believed that people will purchase the lowest-priced product available, but experience shows people will pay more for a product if they believe the higher-priced product is better than the lowest-priced products. Think of several products you purchase for which you know you pay more than you would have to. List the features of the products that cause you to pay a higher price. After you have developed the list, classify the reasons according to the four elements of the marketing mix: product, distribution, price, promotion.

5. The price charged for a product is affected by a number of factors. For each of the following situations, identify whether you believe it will result in a higher or lower price. Write one or two sentences to justify each answer.
   
a. One customer purchases a very large quantity of a product.
   
b. A business provides a high level of customer service.
   
c. The product is very fragile and requires special handling.
   
d. The product moves through many businesses in the channel of distribution before it reaches customers.

6. Internet services have the same traits as those provided by bricks and mortar businesses. Locate an Internet service business. Review the company’s web site and find information that describes how the service is intangible, inseparable, perishable, and heterogeneous.

>> Develop Your Business Language

Match the terms listed with the definitions.

7. Any paid form of communication through mass media directed at identified consumers to provide information and influence their actions.

8. The exchange of information so there is common understanding by all participants.

9. A specific group of consumers that have similar wants and needs.

10. Everything a business offers to satisfy a customer’s needs.

11. The locations and methods used to make a product or service available to the target market.

12. The blending of the marketing elements.

13. Intangible activities that are consumed at the same time they are produced.

14. The process of planning and executing the conception, pricing, promotion, and distribution of ideas, goods, and services to create exchanges that satisfy individual and organizational objectives.

15. The route a product follows and the businesses involved in moving a product from the producer to the final consumer.

16. Finding solutions to problems through carefully designed studies involving consumers.

17. A company’s plan that identifies how it will use marketing to achieve its goals.

18. The reasons consumers decide what products and services to purchase.

19. Direct individualized communication with prospective customers to assess their needs and assist them in satisfying those needs with appropriate products and services.

20. Any form of communication used to inform, persuade, or remind.

21. The money a customer must pay for a product or service.

Key Terms

a. advertising
b. buying motives
c. channel of distribution
d. consumer decision-making process
e. distribution
f. effective communication
g. marketing
h. marketing mix
i. marketing research
j. marketing strategy
k. personal selling
l. price
m. promotion
n. services
o. target market
DeeLites is a popular bakery in a small Iowa town. The bakery produces a variety of fresh pastries, cakes, pies, and other specialty desserts that have reduced calories. Loyal customers say that the low-calorie baked goods are better tasting than similar higher-calorie products they can purchase elsewhere. Customers have encouraged the owner of DeeLites to allow ordering over the Internet so their friends and relatives from other cities and states can purchase the products. The owner would like to increase sales, but is concerned whether the Internet is a good way to expand.

22. What would be the advantages of using the Internet to expand sales?

23. What changes in the marketing mix would have to be made to sell products using the Internet?

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24. **MATH** The use of intermediaries reduces the number of exchanges needed to distribute products from producers. Consider a situation where three manufacturers produce products that are purchased by 1,000 customers. Use the following information to determine the number of exchanges needed for each customer to purchase one product from each manufacturer.

   a. How many exchanges will be needed if each manufacturer sells one product to each of the 1,000 customers?
   b. How many exchanges will be needed if each manufacturer sells its products to 10 retailers and each of the retailers sells all three products to 100 customers?

25. **RESEARCH** Use the Internet, business magazines, or newspapers to locate a report on a marketing research study. Review the research and prepare a two-page analysis. The report should include the purpose of the research, the characteristics of the people studied, the data collection method, important findings, and the sponsor of the research. Develop one graph or chart to support your analysis. Describe how a business could use the research to improve their marketing strategy.

26. **DECISION-MAKING** Identify one product or service that is marketed by one company to at least three different target markets. Prepare a table with three columns and four rows. List three target markets for the product as column headings. List the four marketing mix elements as the headings for each row. Complete the table by keying a brief description of each marketing mix element for each target market into the table cells. Shade those elements that are the same for more than one target market. Leave those that are different unshaded.

27. **COMMUNICATION** Promotion is used for three purposes: to inform, to persuade, and to remind. Select a product or service with which you are familiar. Write three short radio advertisements for the product. Direct each advertisement at one of the three purposes of promotion. For each advertisement, develop a brief description of the audience to which the advertisement should be aimed. Also indicate the type of radio station or programming that would most likely attract each audience.

28. **MATH** When businesses determine the price they will charge customers for products, three factors are very important. The first is the price they pay for the product, known as cost. The second factor is the percentage they add to their cost, known as the markup. Markup added to the product cost determines the selling price. The selling price must cover their costs and leave an amount for net profit. The net profit is the amount remaining when all of the business’ costs are subtracted from the selling price. Calculate the missing amounts in the table below for each product.

<table>
<thead>
<tr>
<th>Product</th>
<th>Product Cost</th>
<th>Markup Percent</th>
<th>Markup Amount</th>
<th>Selling Price</th>
<th>Total Cost</th>
<th>Net Profit</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>$30</td>
<td>40%</td>
<td>$12</td>
<td>$45</td>
<td>$32</td>
<td>$2</td>
</tr>
<tr>
<td>B</td>
<td>$50</td>
<td>50%</td>
<td>$25</td>
<td>$75</td>
<td>$70</td>
<td>$5</td>
</tr>
<tr>
<td>C</td>
<td>$60</td>
<td>80%</td>
<td>$48</td>
<td>$108</td>
<td>$96</td>
<td>$12</td>
</tr>
</tbody>
</table>

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CHAPTER 10  Marketing
> > Linking School and Home

Interview three people from your family or neighborhood to learn more about the consumer decision-making process. One person should be approximately your age or younger, another at least 10 years older than you, and the third at least 20 years older than you. Ask each to identify a product they recently purchased. Then ask them questions about how they decided they needed to make the purchase, how they gathered information about choices, and how they made the decision, as well as their satisfaction following the decision. Ask them if they believe they made an effective decision or not and why. When you have completed all of the interviews, compare the procedures they followed with the steps of the consumer decision-making process. Did they follow each step? Were there differences in procedures based on the age of the person?

> > Portfolio Activity

To provide tangible evidence of your learning about marketing, do the following:

**COLLECT** an example related to one of the goals presented in this chapter’s lessons. The example could be an illustration or photo of a marketing business or marketing function, a new product or service, an interview with a person who works in marketing, or observations of consumer purchasing behavior.

**CREATE** a flowchart using the item you selected. Show in a visual format the relationship of your example to the completion of a satisfying exchange process within a channel of distribution.

**CONNECT** your flowchart to other items already in your class portfolio, or relate the flowchart to an important concept you learned in another class. Make the connection by writing a one-paragraph discussion of how marketing links to another topic you have studied in this class or other classes.

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**Business Plan**

Business plans are the key to acquiring financing for a start-up business. The business plan gives entrepreneurs a tool for evaluating, organizing, and selling a new business concept.

After conducting the appropriate research, select a business to start in your community and write a business plan. Your business plan should include an Executive Summary (brief synopsis of the key points and strengths included in the plan), Company Description, Industry Analysis, Target Market, Competitive Analysis, Marketing Plan and Sales Strategy, Operations, Management, and Organization, Long-Term Development, and Financials. You may also include additional attachments such as certifications, licenses, and tax requirements. The business plan can be single- or double-spaced, but cannot be longer than 30 pages.

The oral presentation will include five minutes for setup and 10 minutes to present your business plan. Visual aids may be used during the presentation. Following each oral presentation, the judges or class may ask questions for five minutes.

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**Performance Indicators Evaluated**

- Understand the complete business plan.
- Present the business plan with confidence and authority.
- Reinforce the business plan with appropriate research.
- Reinforce the presentation with appropriate visual aids.
- Produce a clear and concise written document that follows grammar, punctuation, spelling, and business style rules.

For more detailed information about performance indicators, go to the FBLA web site.

1. Why is the business plan so important for an entrepreneur?
2. Why does a financial institution want to know the long-term goals for a business?
3. Explain why the format of the business plan is so important.
4. List three good sources of information when writing a business plan.

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http://www.fbla-pbl.org/
Chapter 11

Business and Technology

11-1 Computer Systems

11-2 Business Applications of Technology

11-3 Other Technology Issues
Planning a Career in...

Information Technology

In your lifetime, thousands of new jobs have been created because of the increased use of computers. Computer and technology workers must meet the demands for information within their organizations. People with a variety of skills and educational backgrounds can find career opportunities working with computers and technology.

How can you gain the training you need to compete? Numerous computer training centers exist that provide many types of technology training. Some employers will pay for their employees to take computer courses. Self-paced and online programs are also available.

Employment Outlook

- The Bureau of Labor Statistics expects faster than average growth in jobs related to computers and technology.
- Since nearly 80 percent of the labor force will be working in service industries, most computer-related jobs will be in service organizations.

Job Titles

- Computer Technician
- Computer and Information Systems Manager
- Computer Programmer
- Software Engineer
- Computer Systems, Software Sales Representative
- Data Entry Clerk
- Computer Support Specialist
- Information Systems Teacher (in schools and for industry)
- Network Administrator
- Systems Analyst
- Computer Scientist
- Database Administrator
- Web Developer

Needed Skills

- Most computer-related jobs require more than a high school education. This training may be achieved through a specialized vocational program or a college degree program.
- Knowledge of computer systems, computer languages, application software, and other technology is required for specialized positions.

What's it like to work in...

Information Technology

“Should we use a flash intro? Will a banner heading be most appropriate? What functions are required to serve the needs of this new customer?” Kellye, a web developer, is in a morning brainstorming session with her team. They are planning to have some ideas ready in time for a meeting with the customer tomorrow.

Each day, billions of people access the Internet for information, entertainment, and business activities. Web sites are the basic element of the Internet. Web developers analyze, plan, design, implement, and support the web sites of their organizations. Many businesses use outside vendors like Kellye’s company to create and maintain their web sites.

Knowledge of multimedia software is a key requirement for web developers. Graphics, digital imagery, audio, and video are vital to the appeal and effectiveness of a web site. Web developers are also often involved with creating web sites for online selling and other e-commerce activities.

What about you? In what ways do you use computers and technology each day that might be the basis for a future career?
Computers are everywhere. These electronic devices process store receipts, test scores, and sports statistics. Computers in business are used to store, process, and report information. Computers are also used to design factories, control traffic patterns, and measure medical test results for hospital patients.

Nearly every business uses some type of computer. A company needs quick, efficient processing to control its operating costs, manage resources, and stay competitive. When you think about the billions of business transactions, checks, and school records that are processed each day, you realize the importance of computers.

Each day in banks, stores, offices, factories, homes, and non-profit organizations, the use of computer systems is expanding. As managers plan and implement computerized activities, they must decide how best to use technology to serve the production and distribution needs of the organization.

Focus on Real Life

Ms. Jenkins announced to her class, “The French Club will meet today during sixth period. The topic for discussion will be computers in international business.”

Fran looked at Brenda and said, “That doesn’t make sense! What do computers have to do with the French Club?”

“Recently our club decided to use a database program to keep track of our membership records,” said Brenda. “In addition,” she went on, “the club is using e-mail to talk to students in France. Then, we are planning a videoconference with other French clubs around the United States. We will also use our computer network to...”

“Wait a minute!” Fran exclaimed. “OK. OK. Computers do have a lot to do with international business.”

“Well then, I guess you’ll be coming to the meeting today after school,” responded Brenda.
Elements of a Computer System

Video games, personal digital assistants, and automated highway toll collection systems all have four basic components:

1. Input device
2. Processing unit
3. Memory and storage
4. Output device

As shown in Figure 11-1, these four basic components make up what is called a computer system. The physical elements of a computer system are called the hardware. Examples of computer hardware include keyboards, cameras, microphones, speakers, monitors (or screens), chips, and printers.

Hardware is constantly changing and expanding. For example, today most computers have sound, graphics, animation, and video. In the past, these features were only offered on large computers. Multimedia computer systems are now common in small businesses and homes.

In contrast to hardware, software refers to the instructions that run the computer system. Businesses commonly use several types of software. These include word processing, spreadsheet, database, presentation, and communications programs.

Computer Networks

Computers in businesses and schools are commonly linked together in a computer network. Organizations link computers together so users can share hardware, software, and data.

The Internet is the largest and best-known computer network in the world. The Internet is most often used for two activities: (1) the exchange of e-mail, and (2) accessing the World Wide Web.

The World Wide Web (WWW) is also called the Web. It allows computer users to access information on almost every topic. The Web uses text, images,
hyperlinks, graphics, frames, animation, video, and audio. It is an extensive information source. This global computer network provides product information, travel assistance, music, government publications, current news, weather, and sports. The World Wide Web is also an important source for handling business transactions.

A local computer network, sometimes called an intranet, is an organization’s private computer network. It is based on the same communication standards as the Internet. An intranet is a smaller version of the Internet. Only members or employees can utilize an intranet. An intranet’s web site looks and functions just like a typical web site, but it is private and only accessible to authorized users.

Like the Internet, an intranet is primarily used to share information. An intranet is an effective tool for saving time and money for companies. It can bring many benefits to an organization.

**CHECKPOINT**

List the four main elements of a computer system.

**INPUT AND PROCESSING**

Computer systems start with the entering of data or other input items. Operation of the system continues with the processing of the data.

**Input: Getting Started**

The first major component of a computer system is known as input. While people are mostly concerned with the results of computer operations, there has to be a starting point. Data is entered into a computer system with an input device.

A keyboard combined with a monitor is a common input device. Another common input device is the mouse, a handheld device used to point to commands (or images) on the computer screen.

Other types of input devices include:

- Controllers and joysticks for video games that allow you to direct the actions of game characters
- Touch-sensitive screens that allow you to use finger contact to enter data
• Light pens, which are handheld input devices that detect the presence of light
• Scanners that translate words and photos into computer-readable formats
• Voice-activated systems that allow you to enter data or commands with a microphone, with the computer translating your words into instructions
• Microphones and cameras, which allow input of audio and video

Processing: Making Things Happen
How does data become meaningful information to be used by organizations and individuals? Processing is the second major component of a computer system. This activity occurs in the central processing unit (CPU), which is the control center of the computer.

The CPU is the “brain” of a computer system. In a personal computer, the CPU consists of tiny wafers or chips. These chips carry instructions and data using electronic pulses.

The most common way to give instructions to a computer is with a program. A program is a series of detailed, step-by-step instructions that tell the computer what functions to complete.

Most powerful computer programs are in formats that are difficult to understand. The format of a computer program is a computer language. Computer language is a system of letters, words, numbers, and symbols used to communicate with a computer.

The two main types of computer programs are operating system software and application software. Operating system software translates commands and allows application programs to interact with the computer’s hardware. The most commonly used operating system is Windows®. Application software refers to programs that perform specific tasks such as word processing, database management, or accounting. The most commonly used application software includes word processing, desktop publishing, spreadsheet, and database.

Word Processing An organization’s reports, correspondence, and other information are created with word processing software. This type of program allows the user to enter, store, revise, and print text for letters, memos, reports, or standard business forms.
**Desktop Publishing**  Word processing activities may be expanded to produce newsletters, brochures, and other publications. Desktop publishing usually includes graphics software to prepare charts, graphs, and other visual elements. Today, computer graphics are commonly used in television commercials, movies, training materials, and in other settings with a need for visuals.

**Database Software**  “Create a list of employees who speak a language used in Asia.” This type of request would involve the use of database software. A database is an organized collection of information with data items related to one another in some way.

In recent years, database marketing has become popular. Software is used to maintain, analyze, and combine customer information files. The information about customers is then used to increase sales by better serving customer needs. For example, a household with young children might receive advertising about educational software. Using a database increases the chance of reaching potential customers who are likely to buy the product.

**Spreadsheet**  In the past, accountants used worksheet paper with many rows and columns. Such a worksheet is an example of a manually prepared spreadsheet. Spreadsheet software is a program that formats data in columns and rows in order to do calculations.

The location where a column and row intersect is called a cell. A spreadsheet is created with specific information, words, numbers, or formulas entered into the cells. Spreadsheets are used to prepare payroll records, financial statements, budgets, and other financial documents (see Figure 11-2).

Spreadsheet software may also be used to do a what-if analysis of a situation. For example, a manager may want to see the effect of different prices on sales.
profit. The spreadsheet automatically recalculates for each price.

**Presentation Software** Creating slide shows for educational and business seminars has become very common. The use of presentation software allows a speaker to show text, data, photos, and other visuals. These images may be accompanied by sound effects, music, or other audio. The use of multimedia elements adds to the value and enjoyment of presentations.

**MEMORY AND OUTPUT**

Various elements must be stored for use in the computer system. Other items are the result of data processing activities.

**Memory and Storage: Saving for Later**

The third major component of a computer system is the memory. When in use, a program is stored in the computer’s memory. This memory within the computer is also called internal (or primary) storage. During processing, both the program and any data entered with an input device are stored in memory.

As shown in Figure 11-3, memory capacity is measured using terms such as bit, nibble, byte, and kilobyte (K). To give you an idea of a computer’s internal storage capacity, it would take at least a 1K computer to store the information on an average page in this book.

Primary storage cannot hold all of the programs and all of the data needed by computer users. Therefore, external (or auxiliary) storage that is not part of memory is available for storing both programs and data.

A hard disk is built into the computer allowing storage of tens of millions of characters. CDs, DVDs, magnetic tapes, and flash memory sticks are examples of commonly used auxiliary storage devices.

**Output: Obtaining Results**

The final component of a computer system is known as output. This element is of greatest interest to most people. Your score on a video game, the results of a test, or the sales for a new product are important outcomes of data processing activities.

**CHECKPOINT**

What are common input devices?

Your school experiences are continually changing because of technology. Create a list of ways in which you have used computers and other technology in school settings and when doing homework. Discuss ways in which technology might be used to enhance the school learning environment.
1. Text output, which includes processing results displayed on a computer screen (monitor) or in a printed report.

2. Graphics output, which might include company logos, photos, drawings, scrolling messages, and animated graphics.

3. Audio output, which involves music and broadcast clips as well as presentations for training seminars.

4. Video output, which may be in the form of a training film, television commercial, or news report.

Quite often, a single output source, such as a web site, includes more than one of these categories.

**CHECKPOINT**

How do internal and external memory differ?

**Key Concepts**

Determine the best answer.

1. An optical scanner is a device in the ___?___ component of a computer system.
   a. input   b. output   c. memory   d. processing

2. A list of potential customers for your new product would be created using ___?___ software.
   a. desktop publishing   b. word processing   c. spreadsheet   d. database

**Make Academic Connections**

4. **Geography** Prepare a visual presentation of a computer network that is used in several countries in a region of the world.

5. **Economics** Describe how technology might affect the operating costs and profits of a company. What are possible effects of technology on the wages of workers?
Protected by deserts on both sides, Egypt has a tradition of architecture and culture. Today, the country is dependent on the fertile land along the Nile River. The Suez Canal provides a vital trade route between the Atlantic Ocean and the Indian Ocean.

As you enter a meeting in Egypt, several greetings may be used. The handshake is most common. Expect to see some traditional clothing, but foreign businesspeople should wear business suits. Clothing styles should always be modest and conservative. Even though it can be extremely hot, most of the body must remain covered. Even shirt collars are expected to be buttoned. You may be expected to take off your shoes, but only after following the lead of your host.

The workweek in Egypt runs from Saturday to Wednesday. Friday is the Muslim holy day, and most people also take off Thursday. In your negotiations, the pace will start slowly. Do not rush the situation. Since Egyptians must get to know you and like you before doing business, the decision process will take time. Also, be ready to compromise in your negotiations.

While the main language of Egypt is Arabic, many business discussions may be carried out in English or French. Business cards will be better received if one side is English and the other side is Arabic. Language meaning will not always be direct. A “yes” may in fact mean “possibly.”

Be cautious of body language. The left hand is considered unclean in the Arab world. Always use your right hand unless both are needed, such as for lifting a heavy object. While Egyptians may gesture with their hands when speaking, pointing is considered very rude. The “thumbs up” sign is offensive.

Your conversations may include talk of soccer, basketball, and boxing. Avoid talking about political issues. In regard to food, many of the most popular Egyptian recipes are thousands of years old. Wheat and barley are the basis for many breads, pastries, and cakes. Peas, beans, lettuce, cucumbers, leeks, and other vegetables are often served with oil and vinegar dressing. Figs, dates, pomegranates, and grapes are important parts of the Egyptian diet, as are fish, poultry, lamb, and beef.

**Think Critically**
1. How does doing business in Egypt differ from business activities with which you are familiar?
2. What common mistakes might a person make when doing business in Egypt?
3. Conduct library or Internet research to find additional information about business and economic activities in Egypt.
MANAGEMENT INFORMATION SYSTEMS

Managers need information to make business decisions. A management information system (MIS) is an ordered system of processing and reporting information in an organization. Computer systems and software are essential parts of management information systems.

A company may need a departmental budget that provides information on expected income and expenses for the next three months. Using an accounting program, past company data and future projections can be processed to create this budget. The resulting document helps managers plan future business decisions.

Components of an MIS

As shown in Figure 11-4 on the next page, the four main components of an MIS are gathering data, analyzing data, storing data, and reporting results. These activities allow an organization to obtain needed information in four main

Why are computer systems and software essential parts of an MIS?

Goals

- Describe the components of a management information system (MIS).
- Identify computer applications in service industries.
- Discuss e-commerce activities.

Key Terms

- management information system (MIS)
- computer-assisted instruction (CAI)
- e-commerce

Focus on Real Life

Josh Aki arrived on the first day of his new part-time job at NBI Distributors. This retailing company sells an array of products by mail, telephone orders, and via the Internet.

“Josh, please outline a report with the sales results of the new products we have introduced over the past six months,” was the request of his supervisor. Based on comments from other employees, Josh knew that some of the products were doing well and others were just sitting in the warehouse. Josh wasn’t sure how to approach this task.

Alicia saw that Josh looked confused, so she helped him by saying, “Check the database for sales results, summarize the data on the spreadsheet program, and prepare your report with our word processing software.”

“Thanks for your help,” Josh responded. “Now I think I have even more questions to ask!”

Business Applications of Technology

Goals

- Describe the components of a management information system (MIS).
- Identify computer applications in service industries.
- Discuss e-commerce activities.

Key Terms

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Why are computer systems and software essential parts of an MIS?

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categories—financial, production and inventory, marketing and sales, and human resources.

1. Financial information, including budgets, sales reports, and financial statements
2. Production and inventory information, including production summaries, lists of tools and supplies, and finished goods reports
3. Marketing and sales information, including data on customer needs, current economic conditions, and actions of competitors
4. Human resources information, including salaries, employee benefit data, and employee evaluations

Data Sources
The information for an MIS comes from several sources. External data sources are outside an organization. Financial institutions, government agencies, and customers are examples of external data sources.

In contrast, internal data sources provide input from within the organization. Internal data includes accounting records, inventory information, and company sales figures. While gathering raw data may be an easy task, changing these facts and figures into meaningful information is the major goal of an MIS.

The MIS in Action
What activities are involved in a management information system? How is needed information communicated to managers? The operation of the MIS involves the following steps:

1. Identify the information needs of the organization.
2. Obtain facts, figures, and other data.
3. Process, analyze, and organize data in a useful manner.
4. Distribute information reports to those who make decisions.
5. Update data files as needed.
Computer networks are often used in an MIS to distribute information to managers, employees, and others. These networks connect computers, printers, and other equipment within a company or around the world.

Worldwide networks are set up through telephone lines, satellites, and other communication technology. Also important for communicating information is e-mail. E-mail gives users the ability to send data quickly through a computer system. After an employee prepares a letter or report, the document is sent electronically to another computer on the local or worldwide network.

Agencies are always expanding their use of computers. Medical information can be found within seconds to save lives. Police records can be sent to other locations minutes after a crime has occurred, helping to solve the crime. Schools and other agencies can transfer records easily when someone moves to another area of the country.

Education

Computers have become vital teaching devices. Computers make it possible to train and test workers in a range of professions. Office workers learn to use word processing software in their daily tasks. At the same time, they receive instruction on the proper use of grammar, spelling, punctuation, capitalization, and document formats. Airline pilots use computerized simulators to learn and improve skills needed for flying new types of aircraft.

Computer-assisted instruction (CAI) is the use of computers to help people learn or improve skills at their own pace.

**Checkpoint**

What are the four components of a management information system?

**Technology in Service Industries**

Over 60 percent of workers in the United States are employed in service industries. The use of computers in these organizations is extensive.

**Public Service**

Government agencies use computers to keep records. For example, the federal government keeps social security records for all past and present workers in the United States and military records for people who have served in the military.

Web sites for international business must be adapted to cultural factors in other countries. Design a web site for doing business in another country. Consider the language, format, design, colors, graphics, and other factors.
pace. With CAI, students work at a speed that best serves their needs. The student does not have to go to a school building for instruction. The student can learn at home on a computer network system connected to a central training location.

The demand for computer and information technology (IT) training in the workplace continues to grow. With the proper computer skills, you will be able to compete for some of the best-paying jobs in the business world.

**Health Care**

Computers are widely used in hospitals and other medical facilities. Uses range from keeping patient records to monitoring medications during surgery.

Medical professionals are also able to see to the healthcare needs of people in rural areas without leaving the city. The use of telemedicine with videoconference equipment allows a diagnosis by a doctor in a different location. A local medical assistant administers the treatment. Technology of this type helps to expand the availability of health care in remote areas of less developed economies.

**Financial Services**

Paying bills online, checking your credit report, and selling stocks and bonds are just a few examples of computerized financial activities. Electronic banking and other financial services have made it possible for consumers to do business beyond usual banking hours. Each day, computers transfer billions of dollars. Payments to workers, businesses, and government flow through local and global computer networks.

Most people are familiar with credit cards and cash cards. You may not be aware of the existence of smart cards. These plastic cards with a silicon chip are used to store information. The chip within the card stores such data as your current account balance and credit history. It may even store medical information for emergencies.

The card could serve as a personal record keeper for travel and other expenses. In addition, a smart card can be used to prove you paid for merchandise you want to exchange, to gain admittance to your place of work, or to unlock and start your car without keys.

**FYI**

The use of mobile phones and other wireless technology is sometimes called “m-commerce” (m for mobile). Various handheld devices are expanding and enhancing e-commerce activities. Instant messaging, stock trading, banking, online buying, music, and sports video clips are most common. About one-third of the world’s population will be using wireless technology in the near future.
E-COMMERCE

You are walking through the mall. As you pass a clothing store, a message appears on your cell phone screen. “Now on special for spring, waterproof jackets, $34.95.” This targeted promotion is just one example of the fast, powerful capabilities of e-commerce and wireless technology.

E-commerce (e for electronic) refers to conducting business transactions using the Internet or other technology. These online business activities come in a range of forms. Almost every function of a company has been adapted to e-commerce. The most common e-commerce activities include:

- Providing product information
- Promoting a company
- Selling online
- Conducting market research
- Making payments
- Obtaining parts and supplies
- Tracking shipments

Types of E-Commerce

E-commerce opens up opportunities to companies previously limited by geographic, financial, or political restrictions. These online economic activities involve four basic models with two selling and buying parties: businesses (B) and consumers (C). See Figure 11-5.

The first and most familiar model is Business-to-Consumer, or B2C. Expanded sales of products in different geographic markets will create B2C growth. Examples are online companies like Amazon and Dell.

The second e-commerce model is Business-to-Business, or B2B. B2B online exchanges are the largest and fastest-growing segment of e-commerce. They account for over 80 percent of Internet transactions. Examples are Ford and General Motors buying parts online from their suppliers.

Consumer-to-Business (C2B) is the third e-commerce model. In C2B, consumers originate online transactions through price offers to businesses. The online company Priceline was one of the first companies in this category. Priceline allows shoppers to make bids for products and services such as airline tickets and hotels. The airline and hotel companies then decide whether to
accept the offers. While small at this stage of online development, C2B could expand with new technologies and consumer initiatives.

Finally, Consumer-to-Consumer (C2C) is the fourth e-commerce model. In the long economic tradition of bartering and auctions, buying and selling among consumers is growing in cyberspace. The ease and speed of transactions among online parties is encouraging more C2C exchanges. An example is the online company eBay.

Global E-Commerce
Multinational computer systems, along with software that translates information from one language to another, make it possible to do business around the world without leaving your computer. Instant transmission of data with the use of satellites makes even the farthest point on earth as close as a button on your computer. Increased global business can have an important impact on world trade and international relations.

Importing and exporting can take place using a computer system. The goods are shipped from the closest location to save time and money. For example, you may order an item from a company in Italy using your computer. When the Italian marketers receive your order on their computer, they check a database and find there are five such items in stock in Canada. They instruct the Canadian importers by e-mail to ship the items to you. You receive them the next day.

You pay the Italian company. Later, the Italian and Canadian companies settle their accounts through the computerized banking system.

Another way of bringing people together to do business is videoconferencing. This system allows people in different geographic locations to meet "face-to-face" by satellite. It is used for sales presentations, training sessions, and other types of meetings. A sales staff in Peru can make a presentation to potential customers in Spain, South Africa, Pakistan, and the United States without leaving Peru.

CHECKPOINT
What do the notations B2C and B2B mean?

11-2 Assessment

Key Concepts
Determine the best answer.

1. An example of external data would be
   a. a company sales report
   b. a list of employee qualifications
   c. a government economic forecast
   d. payroll records

2. CAI refers to
   a. paying bills online
   b. electronic inventory control
   c. providing health care to remote areas
   d. individualized instruction

Make Academic Connections

3. When a packaged food producer sells items to a restaurant, this is considered to be a ___?___ e-commerce transaction.

4. Visual Art Create a visual presentation of a management information system for a specific information flow for a company of your choice.

5. Culture Research other cultures to determine how people in these societies might react to various aspects of e-commerce.
Other Technology Issues

WORKPLACE TECHNOLOGY
Computers are present in almost every business situation. They help improve efficiency and productivity. Computers can be found in oil fields, warehouses, retail stores, hospitals, offices, and factories.

Robotics
Most of you have seen robots and other computer systems in science fiction movies set in outer space and in the future. In real life, robotics involves mechanical devices programmed to do routine tasks, such as those in many factories. An example of work where robots are used is assembly line work that requires repeated tasks.

Early robots did only simple tasks such as tightening a bolt on an automobile. Today, robots exist that can see, hear, smell, and feel. Robots are able to work 24 hours a day. These computerized workers can perform in dangerous situations such as in outer space, underwater, or underground. The use of robots is also growing to include automated checkout clerks, airline ticket agents, and hotel desk clerks.

Expert Systems
Have you ever wanted a quick answer to a question without having to find a book or person who knew the answer? Artificial intelligence (AI) is software that enables computers to reason, learn, and make decisions. It uses logical methods similar to the methods humans use. An example of artificial intelligence is computer programs that make decisions about complex topics. For example, software exists that asks people questions about their health in order to determine solutions for potential...
medical problems. This software allows people in areas without doctors to receive better medical care.

Computer programs that help people solve technical problems are called expert systems. They are now available for medical services, financial planning, and legal matters. Expert systems are based on the knowledge of human experts in many specialized areas. These systems provide intelligent answers as effectively as human experts in those subject matters. For example, employees of the Internal Revenue Service use an expert system to quickly answer questions from taxpayers.

**Computer-Aided Design**

Computers created many of the products you use each day. Computer-aided design (CAD) refers to the use of technology to create product styles and designs. CAD allows you to try different sizes, shapes, and materials for a new machine, automobile, or food package. This process can be used to experiment with many variations before spending time and money building a model or going into production.

**Telecommuting**

Each morning, more than 20 million Americans travel to their offices . . . in another room of their homes! These people do all or part of their work at home. Telecommuting involves the activities of a worker using a computer at home to do a job. Telecommuting saves travel time and costs. It results in less traffic along with reduced noise and air pollution.

Each year more and more people become telecommuters. This working arrangement is especially attractive to people who have a hard time leaving their home to go to work. These include workers who are disabled or parents who desire to be with their young children. A work-at-home arrangement is most common among workers such as writers and editors, researchers, accounting clerks, sales representatives, computer programmers, and web site designers.

These workers can easily send their reports, documents, and ideas to their employers by computer. Telecommuting is made possible with computers and other technology. E-mail and faxes allow a person to communicate with the company’s main office.

**CHECKPOINT**

How is computer-aided design (CAD) used by businesses?
HOME AND PERSONAL TECHNOLOGY

Computers not only change the way you work, but technology also affects almost all aspects of life.

School and Homework
Internet studies time and again reveal that computers are a key homework tool for students. For many students, more than one-third of homework time involves the computer. Over half of all students think the computer is their most important homework resource.

Students today find many uses for the computer. Online encyclopedias, presentation software, and other technology are increasing your skill to communicate and use ideas.

Home Robotics
Robots are no longer just in factories and businesses. Computerized systems now exist for repetitive chores such as vacuuming and mowing the lawn. Toys and other electronic devices for children can both entertain and educate. In the future, you can expect home robots to monitor household appliances, roll trash cans to the street, and assist the elderly with lifting items and bringing them medicine that need to be taken.

Can you name some kinds of software that would make household activities easier?

Household Record Keeping
At home, your computer system provides shopping assistance, financial and other information, and entertainment. You can also obtain software for household activities on a personal computer.

Programs can keep a list of names and addresses of people to whom you send greeting cards. You may store your favorite recipes by categories. A family’s medical history can be kept on file. You can have an inventory of household items for insurance records in case of theft or damage. In addition, computer programs may be used for personal financial record keeping, budgeting, writing checks, and preparing your income tax return.

Finding fast and accurate information on the Internet is the goal of most Web searches. With several hundred search engines available, how do you select the one that is best for your needs? Access businessxtra.swlearning.com and click on the link for Chapter 11. Obtain suggestions to follow when conducting a Web search.

businessxtra.swlearning.com

What types of technology tools are available to students?
SOCIAL CONCERNS OF TECHNOLOGY

New technology will continue to expand the potential uses of computers in business. New software will eliminate some jobs while increasing job growth in others. It will also continue to change the way work is done.

Expanded computer use has resulted in concerns about health and safety, criminal activities, and privacy. While computers are beneficial to society, the wise person will not place complete faith in the reliability or safety of computer systems.

Employment Trends

Many people think computers are taking away their jobs. What is actually occurring is a shift in the job duties and skills needed to work in business and industry. When computers replace workers, companies need to retrain the workers with skills in programming, operating, or repairing computer systems.

Displaced workers are workers who are unemployed because of changing job conditions. They must adapt to the changing job market in order to have continued employment. What actions can companies and workers take to be ready for the new jobs of the future?

Computers and other technology are becoming more important in our lives each day. The ability to use this technology is vital to each person’s economic survival. Computer literacy is the ability to use computers to process information or solve problems. You do not have to understand how to program a computer to use it. You do need to know how to enter, store, process, and retrieve information.

Health Concerns

Various products and substances can be dangerous. While little danger exists from using computers and other technology, some people have encountered discomfort resulting from on-the-job activities. For example, eyestrain and vision problems have been linked with prolonged work at computer screens. Muscle tension and nerve damage can occur from too many hours at a keyboard. These and other concerns have resulted in guidelines from labor organizations and government agencies for safe computer operation.

Computer Crime

Wide use of computers has led to an increase in white-collar crime. White-collar crime is illegal acts carried out by office or professional workers while at work. Workers may steal money, information, or computer time through improper use of databases or illegal access to computer systems.

While the typical bank robbery results in a loss of $10,000, computer crimes involving bank records average hundreds of thousands of dollars. Theft of a physical item is obvious. Theft of computer time or information from a database is usually harder to detect.
Piracy is stealing or illegally copying software packages or information. It can be a significant problem. In some countries, between one-third and one-half of the software used is obtained illegally. Companies that develop software may lose more than half of their profits to information pirates who violate the law. Copyright laws apply to software as well as books and music.

Destructive efforts are also a concern to computer users. A computer virus is program code hidden in a system that can later do damage to software or stored data. The virus may be programmed to become active on a certain date or when certain data is accessed. Some computer viruses are harmless, only showing up as a funny message. Others have been known to destroy critical government records.

Privacy Concerns
One of the greatest challenges facing computer users is the need to guarantee privacy. Some dishonest people have learned how to illegally access computer databases. While some laws exist to protect your privacy, many concerned people believe these regulations are not strong enough. Some businesses are becoming stricter about who can access and use company information. Tighter security systems are being developed. Some organizations change the password needed to access information several times a day to protect their databases.

In recent years, identity theft has become a major concern for consumers and companies. Thieves obtain information online about a person. They apply for a credit card in the person’s name or access the bank account of that person. Each day, more than 1,000 people have their identities stolen in the United States. Con artists illegally obtain millions of dollars each year through identity theft.

11-3 Assessment

Key Concepts
Determine the best answer.

1. Telecommuting refers to
   a. the use of computers to design products
   b. working at home by computer
   c. difficulties from overusing computers
   d. illegal acts of office workers

2. Hidden software code that can damage computer operations is
   a. piracy
   b. a displaced worker
   c. a virus
   d. computer literacy

3. Which of the following is an example of computer literacy?
   a. data entry
   b. identity theft
   c. piracy
   d. telecommuting

Make Academic Connections

4. Communication Prepare a memo that sets out the benefits of telecommuting for an organization. In your memo, present specific details of a job that would be appropriate for telecommuting.

5. Music Select three different types of music. Discuss how each might be appropriate or inappropriate for an office setting to reduce stress associated with working on computers.
“Every time you make a purchase, the money that leaves your hands goes to work.”

In an effort to make sure these dollars work to better serve the interests of consumers, workers, and society, Co-op America was created based on the belief that your purchases can support businesses that create jobs, care about their communities, engage in fair trade, and protect the environment. The organization’s mission is “to harness economic power—the strength of consumers, businesses and the marketplace—to create a socially just and environmentally sustainable society.”

Co-op America was started in 1982 and provides practical tools to address today’s social and environmental problems. While many environmental organizations fight political and legal battles, Co-op America educates people and business about making improvements through the economic system.

The main programs of Co-op America are:

- **The Green Business Program**, designed to start small socially and environmentally responsible businesses
- **The Consumer Education and Empowerment Program**, which informs people about how to vote with their dollars to make changes
- **The Corporate Responsibility Program**, which encourages corporations to become socially and environmentally responsible and provides information about boycotts and shareholder resolutions against irresponsible companies
- **The Sustainable Living Program**, providing information about practical measures people can take to make their personal, community, and work lives more meaningful and sustainable

Co-op America publishes a variety of materials. The organization’s National Green Pages is a directory of America’s leading socially and environmentally responsible businesses.

Co-op America has 50,000 individual members and 2,500 member businesses that work together to achieve the goals of the organization. In addition, Co-op America manages the Social Investment Forum, a trade organization for socially responsible investing professionals.

Each day, Co-op America encourages consumers to rethink their buying habits. Your purchases should be with companies that are trying to become more socially and environmentally responsible. Investors are encouraged to support socially responsible companies. Most importantly, Co-op America wants consumers, investors, and businesses to demand change . . . change that starts in their own homes and businesses.

**Think Critically**

1. How does Co-op America serve consumers and businesses in our society?
2. What aspect of Co-op America do you believe is most valuable for people in your state or community?
3. Go to the web site of Co-op America to obtain additional details about the activities of this organization.
>> Business Notes

11-1 Computer Systems
1. Computer systems consist of four main components: the input device, the processing unit, the memory and storage facilities, and an output device.
2. Commonly used input devices include the keyboard, mouse, video game controllers, touch-sensitive screens, scanners, and voice-activated mechanisms.
3. The main types of storage devices are the internal memory in a computer and external memory such as disks, CDs, DVDs, magnetic tape, and flash memory sticks. Data processing results are reported as text output, graphics output, audio output, or video output.

11-2 Business Applications of Technology
4. The four main components of a management information system (MIS) are gathering data, analyzing data, storing data, and reporting results. The goal of an MIS is to change raw data (facts and figures) into information that can be used by managers.

11-3 Other Technology Issues
5. Service industries that make extensive use of computers and technology include public service organizations, educational institutions, healthcare facilities, and financial service organizations.
6. E-commerce involves the conducting of business transactions over the Internet or through other electronic technology.

>> Communicate Business Concepts

1. Identify each of the following items as either hardware or software.
   a. monitor (screen)
   b. word processing program
   c. chips
   d. keyboard
   e. operating system program
   f. disk drive
   g. mouse
   h. printer

2. What are possible business activities currently performed by people that might be performed in the future using a computer system?

3. Identify whether word processing software, database software, spreadsheet software, or graphics software would be used to perform the following computer applications.

   a. Preparing a report of new equipment purchased for each office of a company
   b. Preparing a list of employees that is sorted by ZIP code
   c. Creating a form letter to go to new customers of a mail-order business
   d. Creating a pie chart showing the portion of sales of each product
   e. Preparing a document listing the total sales for each geographic area of the country
   f. Listing the employees who have not missed a day of work in five years
   g. Sending a letter to each employee who has not missed a day of work in five years

4. List examples of (a) external data and (b) internal data used by most companies.

CHAPTER 11 Business and Technology
5. Who would benefit from schools that would allow students to take classes at home by computer?

6. Describe the benefits to workers, employers, and society when an organization allows some of its employees to do all or part of their work at home.

7. How has e-commerce expanded global business in countries that previously had limited economic activity?

8. How is it possible for the increased use of computers to create more jobs than are lost?

9. How might expert systems be used in the future to help people solve medical, legal, financial, and other technical problems?

10. What are potential benefits from the use of smart cards in handling everyday transactions?

11. What actions could be taken by organizations to prevent computer crime?

> Develop Your Business Language

Match the terms listed with the definitions.

12. Several computers linked into a single system.

13. Computer programs that perform specific tasks such as word processing, database management, or accounting.

14. Instructions that run a computer system.

15. The control center of the computer.

16. The combination of an input device, a processing unit, memory and storage facilities, and an output device.

17. Conducting business transactions over the Internet or using other technology.

18. Software that translates a computer user’s commands and allows application programs to interact with the computer’s hardware.

19. A system of letters, words, numbers, and symbols used to communicate with a computer.

20. The components or equipment of a computer system.

21. A series of detailed step-by-step instructions that tell the computer what functions to complete and when to complete them.

22. The use of computers to help people learn or improve skills at their own pace.

23. A term used to describe the activities of a worker using a computer at home to perform a job.

24. Mechanical devices programmed to do routine tasks.

25. Technological assistance used to create product styles and designs.

26. Stealing or illegally copying software packages or information.

27. Programs that assist people in solving technical problems.

28. An organized system of processing and reporting information in an organization.

29. A program code hidden in a system that can later do damage to software or stored data.

30. Programs that enable computers to reason, learn, and make decisions using logical methods similar to the methods humans use.

Key Terms

a. application software
b. artificial intelligence (AI)
c. central processing unit (CPU)
d. computer language
e. computer network
f. computer system
g. computer virus
h. computer-aided design (CAD)
i. computer-assisted instruction (CAI)
j. e-commerce
k. expert systems
l. hardware
m. management information system (MIS)
n. operating system software
o. piracy
p. program
q. robotics
r. software
s. telecommuting
Decision-Making Strategies

The Kendall Manufacturing Company assembles electronic devices used in offices and homes. They employ about 600 people in various office, factory, and warehouse positions. Currently, all factory and warehouse jobs are done manually. Managers at Kendall are considering replacing 150 assembly line workers with a computerized system. The company can save $135,000 a year in operating costs by using this new technology.

31. What factors should the company consider before using the computerized assembly line system?

32. If the company uses this new system, what should the company do to help workers who are displaced by this technology?

Make Academic Connections

33. VISUAL ART With the use of photos and other graphics, prepare a visual presentation that communicates the elements of a computer system.

34. TECHNOLOGY Research types of input, output, and memory devices that have recently been developed for use by businesses and individuals.

35. COMMUNICATION Talk to people who make online purchases. What types of products do they buy most frequently? What concerns do they have about buying online? Prepare a table with a summary of your findings.

36. TECHNOLOGY Prepare a list of daily activities and information items that might be included in the processing and storage facilities of a smart card.

37. MATH Marvin Trotsky requested sales information from the computer about the Lightning pickup trucks from each of five sales districts in the United States. The computer-generated report is shown in the table below. Calculate the data that is missing in the report.

<table>
<thead>
<tr>
<th>U.S. Region</th>
<th>Trucks Allocated</th>
<th>Percentage Sold</th>
<th>Number of Trucks Sold</th>
<th>Current Inventory*</th>
</tr>
</thead>
<tbody>
<tr>
<td>East</td>
<td>4,200</td>
<td>16%</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Southern</td>
<td>7,075</td>
<td>29%</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>North Central</td>
<td>9,500</td>
<td>—</td>
<td>—</td>
<td>5,700</td>
</tr>
<tr>
<td>Southwest</td>
<td>—</td>
<td>20%</td>
<td>600</td>
<td>—</td>
</tr>
<tr>
<td>Northwest</td>
<td>100</td>
<td>—</td>
<td>—</td>
<td>86</td>
</tr>
</tbody>
</table>

*Trucks Allocated – Trucks Sold = Current Inventory

38. SCIENCE Investigate various uses of telemedicine and telesurgery in the United States and in other areas of the world.

39. MATH The Barkley Corporation usually sends about 3,800 pieces of mail per month at $0.42 each. If the firm switches to electronic mail service at a cost of $1,250 per month, how much money would it save or lose? What other factors should the company consider before making this change?

40. GEOGRAPHY Many nations around the world do not have reliable telephone service. As a result, cell phones and wireless communication has grown at a fast pace in these countries. Conduct research and prepare a map reporting the countries with a significant usage rate of wireless communication.

41. TECHNOLOGY Research recent computer viruses. What types of damage do various viruses do to computer systems?

42. LAW Conduct an Internet search to obtain information about avoiding identity theft. What laws exist to protect victims of identity theft?
**Linking School and Home**

Talk with a few family members or friends about the computers and technology they use on the job. Which items have they used for more than three years? Is there any technology that has changed within the past year? What computer skills would they recommend a person obtain for career success? Prepare a one-minute summary of your findings.

**Portfolio Activity**

To provide tangible evidence of your learning about computers and technology, do the following:

**COLLECT** photos, other visuals, and information about the use of computers and technology in various business and personal settings.

**CREATE** a flowchart to visually communicate a process in which computers are used in some business situation or home activity. A flowchart is a visual presentation of the steps in a process or procedure. This will require that you break down the steps of the process so that it can be understood.

**CONNECT** your flowchart to other items already in your class portfolio, or relate the flowchart to an important concept you learned in another class. Make the connection by writing a paragraph on this relationship.

**Web Site Development**

Business success depends on the ability to communicate ideas and concepts using the Internet and related technologies. This event challenges students to design a web site for a business.

Command Performance is a new company that specializes in electronic presentations and teleconferencing for corporate meetings. Command Performance takes care of the following business meeting details:

- Securing the teleconference format
- Preparing the agenda
- Negotiating meeting/hotel room prices
- Designing all electronic presentations and handouts necessary for the meeting

You have been hired to design a web site to advertise the services offered by Command Performance. The introduction to the web site should use Flash or Flash-type animation. The company overview should include a Mission Statement, Company Services, New Products, Company History, Staff, and one additional element. The web site must include customer service information. Current clients and a portfolio of presentations should be available on the web site (March of Dimes and FBLA-PBL, Inc. are two current clients). The site should include links, site map, FAQs, pricing and/or rates, and a Contact Us link.

**Performance Indicators Evaluated**

- Understand effective page layout and design.
- Produce a site with functional links that are consistent and support the theme.
- Include content that makes the site effective.
- Demonstrate proper use of grammar, spelling, and punctuation.
- Produce a site that is compatible with multiple browsers.
- Respect copyrights laws.

You will be evaluated for:

- Thoroughness of all important concepts on the web site
- Validity of links included on the web site
- Navigation ease of your web site

For more detailed information about performance indicators, go to the FBLA web site.

1. List two things that frustrate customers about web sites.
2. Why should a web site list current customers and projects?
3. What web site elements can close the sale with prospective customers?
4. What are the top issues that must be sold about this company?
Chapter 12

Financial Management

12-1 Financial Planning
12-2 Financial Records and Financial Statements
12-3 Payroll Management
12-4 Financial Decision-Making
Planning a Career in...

Accounting

Managing a business’ financial records and decisions is an important task. All income and expenses must be accurately identified and recorded. Financial records must be kept up to date and financial statements prepared. When requests are made for financial information, the necessary records must be retrieved, the information summarized, and reports prepared. All financial decisions of a company need to be evaluated to make sure they meet federal and state laws as well as ethical standards. Accountants complete all of the work described.

Public accountants perform accounting, auditing, tax, and consulting activities for their clients. Management accountants record and analyze the financial information of the companies for which they work. They advise executives and other managers to help them make good business decisions. A unique and growing area is forensic accounting, which investigates white-collar crimes such as securities fraud, embezzlement, bankruptcies, and other possibly illegal financial transactions, such as money laundering.

Employment Outlook

• There are over one million accountants working in the U.S. Nearly 10 percent are self-employed.
• Employment opportunities are expected to grow rapidly in both private and public accounting.
• Accountants with advanced computer skills and a specialized knowledge of business operations and legal issues will be in especially high demand.

Job Titles

• Accountant
• Auditor
• Budget Analyst
• Financial Analyst

Needed Skills

• Bachelors degree in accounting, with a masters degree or MBA preferred
• Ability to efficiently analyze and interpret facts and figures
• Ability to deal with detailed information
• Accountants can earn a certification of Certified Public Accountant (CPA) by passing a series of tests, completing advanced coursework, and documenting successful accounting experience.

What’s it like to work as... an Accountant

When you graduate with an accounting degree, you will often start as a junior accountant or accounting technician. Demonstrating your accounting skills on the job provides you with opportunities to advance. Beginning public accountants usually start by assisting experienced accountants. If you complete the requirements for the CPA, you will be promoted to senior accountant, followed by manager and finally partner in the accounting firm.

If you are entrepreneurial, you might decide to open your own public accounting firm. Another choice is an executive position in management accounting or internal auditing in a corporation. Management accountants often start as cost accountants or junior auditors. You can become an accounting or auditing manager, a controller, a chief financial officer, or even the president/CEO.

What about you? Why are both math and computer skills important to people who want to work in accounting? If you decided on a career in accounting, would you be more interested in public or management accounting? Why?
FINANCIAL PLANNING

Picture yourself as a business owner. One of the constant problems you face is financing. From the first day of the business, financing questions must be addressed. Financial questions never go away. Even the most successful businesses are continually active in financial planning.

Beginning a Business

The moment a decision is made to start a business, financial planning begins. How much money will be needed to start the business? Where will that financing come from? How will adequate funds be obtained to operate the business for the months or years until the business becomes profitable? What will be the best sources of sales and other income? What will be the major expenses? When must they be paid?

Many new businesses fail due to poor financial planning. Experts in business finance should be consulted to help the new business with its financial planning. The business owner needs to know the importance of financial planning and must develop financial management skills.

Ongoing Operations

Finances are a key part of the operations of all businesses. Every business activity costs money. Without careful planning and management, those costs can grow to a level where the business income cannot cover the expenses. All income that a business receives over a period of time is called revenue. Businesses also have expenses. Expenses are the costs of operating a business. As shown in Figure 12-1, each business is guided by the basic financial equation:

\[ \text{Revenue} - \text{Expenses} = \text{Profit or Loss} \]
If revenue is greater than expenses, the business will make a *profit*. If expenses exceed revenue, the business will suffer a *loss*.

All managers are responsible for the costs of the part of the business they manage. Each employee should also be concerned about those costs. The profitability of the business is directly linked to the number of employees and the wages the business can pay. Managers and employees should find ways to reduce waste and control expenses. They can also make suggestions about ways to increase sales and income through better products and services and higher customer satisfaction.

Ongoing operations require that employees be paid, supplies and materials ordered, and buildings maintained. Equipment must be repaired and technology updated. Each of those decisions requires careful attention to costs.

**Business Expansion**

Successful businesses expand to be able to serve more customers, reach unserved markets, and sell new products. Yet expansion costs money. The hope is that the income generated by the expansion will be far greater than the cost. A more profitable business is the result.

Business expansion calls for research to develop new products and locate new markets. New factories and equipment may be needed to produce the products. Additional employees must be hired and trained. Marketing activities will be planned and implemented to distribute and promote the products. Most expansion plans occur over a long period and can cost thousands or even millions of dollars. Each time business expansion is anticipated, careful financial planning must be completed. The planning must anticipate the costs associated with the expansion, the source of the funds to pay for the expansion, and the expected income that will result from the new plans. If the planning is not correct and the expansion results in heavy losses rather than profits, the previously successful business may fail.

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**CHECKPOINT**

What is the basic financial equation for businesses?
DEVELOPING BUSINESS BUDGETS

A budget provides detailed plans for the financial needs of individuals, families, and businesses. A business budget has two main purposes:

1. Anticipate sources and amounts of income.
2. Predict the types and amounts of expenses for a specific business activity or the entire business.

The business must be able to identify and predict the amount of each source of income and each type of expense. In addition, the business will need to determine when each expense must be paid and when income will be received. For the business to succeed, enough revenue must be available to pay all expenses.

Sources of Budget Information

To develop an effective budget, information to predict income and expenses is needed. If a business has operated for several years, identifying sources of income and types of expenses will not be difficult. The main source of that information is the financial records of the business. Budgeting is much harder for a new business. No financial records exist to serve as a guide. Other sources of information must be used.

E-Commerce in Action

Taxing Online Purchases

Forty-five states and the District of Columbia collect sales taxes on purchases consumers make from businesses that operate in their states. Those taxes are often not collected for products purchased on the Internet. From their beginning, most Internet businesses argued that they were not required to collect sales taxes except in the state where their business was located. In 1992, the U.S. Supreme Court agreed when they ruled that states were prohibited from collecting sales tax from businesses that had no physical presence in their state unless Congress specifically passes a law to allow it. While there has been much discussion about such a law, so far none has been passed.

States worry that they are losing billions of dollars of lost tax revenue each year if they cannot impose sales taxes on e-commerce. Traditional businesses argue they have a competitive disadvantage when they are required to collect the tax and online businesses are not. Internet businesses respond that customers have the additional cost of product shipping, so they have no real price advantage.

One of the major issues is the complexity of tax laws covering all 50 states. Sales tax rates vary from state to state, and many cities and counties have their own sales taxes. To collect the taxes, online retailers would need to have access to a continually updated set of tax rates and be able to match them with a customer’s address at the time of sale. Then they would have to submit the collected taxes in the right amounts to the correct tax agencies across the country. To respond to that confusion, the National Governor’s Association and the National Conference of State Legislators have proposed the Streamlined Sales Tax Project (SSTP) with the goal of creating uniformity and simplifying state and local sales tax laws. Currently, 20 states have begun to change their laws to fit the SSTP recommendations. In addition, software development companies are creating programs that make it easy for businesses to calculate, collect, and process sales taxes. That software will be in high demand if online businesses are required to collect the taxes everywhere they sell their products.

Think Critically

1. Conduct an online search of news articles on the status of collecting sales tax on online sales. Determine if your state has laws and procedures related to e-commerce sales tax.
2. Do you believe online sales should be taxed in the same way the products would be taxed if they were purchased in a local store? Why or why not?
The Small Business Administration (SBA) provides many planning tools for new businesses. Among those tools are guides to developing a budget and financial information to help the new business owner predict income and expenses. Another source of information is private businesses that collect and publish financial information on similar businesses and industries. Examples of those companies are Dun and Bradstreet, Value Line, and Standard and Poor’s. Some information is also available from business magazines and newspapers including *Fortune, Forbes, Entrepreneur, Black Enterprise*, and *The Wall Street Journal*.

Professional associations, such as the National Federation of Independent Business and the National Retail Merchants Association, offer resources to help with financial planning. A new franchise will typically receive help with financial planning from the franchisor. It may even have a complete beginning budget provided. New businesses working with a bank or other financial institution can obtain information and support there. Franchisors and financial institutions want to see businesses succeed, so they encourage careful financial planning.

**Budget Preparation**

The most important step in financial planning is developing a budget. You can compare the use of a budget to the use of a road map when you are traveling to an unfamiliar location. Without the map, you will have little idea where you are going while you travel. If you take a wrong turn, you will have difficulty knowing your mistake. It will be hard to get back to the correct road without the map. In the same way, a budget identifies where a business is going. It allows the owner to determine if the business is making progress toward its financial destination. By regularly comparing the business’ financial performance to the budget, the owner can determine if the budget goals are being met. If not, the owner can make corrections before serious financial problems occur.

A business budget has the same basic goals as a personal or family budget developed to manage the household finances. The goals are to determine the sources and amounts of income, to identify the types of expenses and predict their costs, to determine how income will be distributed to cover those expenses, and to reward investors if there is a profit.

**FYI**

U.S. businesses spend over $1 trillion dollars each year on investments in buildings, equipment, and technology. The industry with the greatest level of spending is manufacturing. Most of their purchases in recent years were for equipment and technology rather than buildings.

What do you think are the most important budget categories for most people? How might they differ from a business budget?
CHAPTER 12  Financial Management

The budgeting process involves four fundamental steps.

1. Prepare a list of each type of income and expense that will be a part of the budget.
2. Gather accurate information from business records and other information sources for each type of income and expense.
3. Create the budget by calculating each type of income, expense, and the amount of net income or loss.
4. Explain the budget to people who need financial information to make decisions.

The person responsible for preparing business budgets needs several skills. Budgeting requires an understanding of financial information, computer skills, mathematical abilities, and effective communications skills. New small business owners often seek the help of an accountant or banker when preparing a budget for the first time. Small- and medium-sized businesses may hire an accounting firm to maintain financial records and to help with budget development. Larger businesses employ accountants and other financial planning experts to maintain the business’ financial records. They also help with budgeting and using budget information.

Work as a Group

Individually prepare a personal budget for the next three months by anticipating the types and amounts of income and expenses you will have. Compare your budget with those of other group members and discuss ways to make your budgeting process more accurate.

Describe three types of business budgets.

TYPES OF BUDGETS

A large business will have many specialized budgets. Each manager will be responsible for one or more budgets in his or her area of operations. For every business, three particular budgets are essential. They are the start-up budget, the operating budget, and the cash budget. The start-up budget plans income and expenses from the beginning of a new business or a major business expansion until it becomes profitable. Most start-ups require expenditures of thousands or even hundreds of thousands of dollars in order to open. Buildings and equipment must be purchased or leased. Inventory, supplies, and materials are needed. New employees will be hired or existing employees retrained. Expenses for utilities, licenses, advertising, and transportation will be incurred before the company can sell its new products and services. Sources of financing for these expenditures must be identified from either inside the company or from outside financial sources. The amount of start-up expenses must be predicted correctly so that ample start-up financing is available until the new activities produce adequate income.

CHECKPOINT

What are the four steps in preparing a business budget?

What additional budget items would need to be considered when buying a car?
The **operating budget** describes the financial plan for ongoing operations of the business for a specific period. The operating budget is usually planned for three months, six months, or a year. An operating budget is prepared for the entire business. Each department and division of a large business will also develop and follow its own operating budget.

When planning an operating budget, income and expenses from prior budgets are reviewed. Planners look for possible changes that could increase or decrease income and expenses. Then the budget for the next period is prepared. It is used to manage the operations of the company for the period covered by the budget.

A **cash budget** is an estimate of the actual money received and paid out for a specific period. A cash budget anticipates that cash will come into a business and that cash will be paid out during each week or month of operation. If a new business is losing money, it still must have adequate cash on hand to pay current expenses. Even profitable businesses may have times when adequate cash is not available due to high expenses or a delay in receiving payments from customers.

A cash budget will determine if a business has adequate financial resources on hand to pay bills as they become due or if they will need to borrow money. It will also show when there is so much cash on hand that some of it can be invested. Investing cash on hand provides another source of business income.

**CHECKPOINT**

Identify and describe the three types of budgets needed by all businesses.

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**12-1 Assessment**

**Key Concepts**

Determine the best answer.

1. True or False. Financial planning is needed by small businesses only until they begin to make a profit.

2. The basic financial equation is
   a. revenue − profit = loss
   b. expenses + revenue = profit or loss
   c. profit − loss = revenue and expenses
   d. revenue − expenses = profit or loss

3. True or False. A cash budget is an estimate of the actual money received and paid out for a specific period.

**Make Academic Connections**

5. Math Use the basic financial equation to determine the profit or loss for each of the following:
   a. revenue $85,695; expenses $72,624
   b. revenue $1,824,300; expenses $2,183,680
   c. revenue $729,655; expenses $499,220

6. Technology Use the Internet to locate a sample business budget. Enter the entire budget into a spreadsheet program. Develop a new budget by adjusting each of the income and expense items in the budget with a 3 percent increase. Then develop another budget by adjusting the original income and expense items with a 1.5 percent decrease.

7. Economics Locate a newspaper or magazine article that describes an anticipated change in the economy that might result in higher or lower income or expenses for businesses. Write two paragraphs discussing how financial planners should use the information when developing an operating budget.
Financial Records and Financial Statements

**Goals**
- Identify several types of financial records needed by businesses.
- Describe the differences between an income statement and a balance sheet.

**Key Terms**
- financial records
- assets
- liabilities
- owner’s equity
- balance sheet
- income statement

**Focus on Real Life**
Paulette received a call from her banker. She had a payment due on the loan she had taken out to buy the building for her printing business. The banker informed her that there was currently not enough cash in her accounts to make the loan payment. While Paulette was not currently behind in her payments, the bank was reluctant to extend the loan. Paulette had been late in making payments four of the past 10 months. Paulette knew she had enough printing orders to cover the cost of the loan payment, but her customers did not always pay on time either. She was reluctant to ask customers to pay cash for large orders. She felt it might encourage them to take their business to a competitor. On the other hand, she didn’t know how she would come up with the money to pay the bank loan. Paulette called her accountant to set up a meeting to review the financial status of her business. Hopefully, they would be able to come up with a solution that would satisfy the bank.

**FINANCIAL RECORDS**
Budgets identify the financial plans of businesses. To determine if those plans have been achieved, financial records are needed. **Financial records** are used to record and analyze the financial performance of a business. Several types of records are maintained. They provide detailed information about the financial activities of the company. Local, state, and federal governments require some records. Other records provide information needed by owners and managers to aid their decision-making.

**Types of Records**
The following records are commonly maintained to document the performance of a business.
- **Asset records** name the buildings and equipment owned by the business, their original and current value, and the amount owed if money was borrowed to purchase the assets.
- **Depreciation records** identify the amount assets have decreased in value due to their age and use.
- **Inventory records** identify the type and number of products on hand for sale. Adequate records are crucial to correctly determine the number of products sold, damaged, or lost and the current value of that inventory.
- **Records of accounts** identify all purchases and sales made using credit. An **accounts payable record** identifies the companies from which credit purchases were made and the amount purchased, paid, and owed. An **accounts receivable record** identifies customers that made purchases using credit and the status of each account.
• Cash records list all cash received and spent by the business.
• Payroll records contain information on all employees of the company, their compensation, and benefits.
• Tax records show all taxes collected, owed, and paid. As a part of payroll, employers must withhold a certain percentage of employees’ salaries and wages for federal income tax. The company also makes payments for Social Security and Medicare and, in some cases, for unemployment compensation insurance. Businesses may have to pay several types of taxes on their income and value of their assets. Adequate records must be maintained to accurately calculate any taxes owed and to file the necessary tax forms.

Maintaining Financial Records
Business records have to be accurate and should be kept up to date. In the past, the preparation and maintenance of financial records was an expensive and time-consuming process. It was often done manually using paper documents that had to be carefully completed, saved, and protected. Then those documents were sent to the people responsible for preparing the company’s financial records.

Technology is changing the way financial information is collected. Much of the information is now collected using point-of-production and point-of-sale technology such as scanners, touch screens, and personal digital assistants (PDAs). Data files are transferred from the places information is collected to the computers of the people who prepare the financial records. Technology is also changing the way financial records are prepared and maintained. Businesses use computerized financial software systems that have templates for each financial record. The software completes the necessary mathematical calculations. It updates records and compares those records with budgets. The software can even complete what-if comparisons to help managers determine the impact of changes in budgets and financial performance.

Work as a Group
Create a table with two headings: Things I Own and Things I Owe. Have each member of your group in turn add items to the list representing their personal assets and liabilities. After the lists are complete, review each list and divide them into current and long-term assets and liabilities.

How has the process of maintaining financial records been affected by technology?
FINANCIAL STATEMENTS

The three most important elements of a company’s financial strength are its assets, liabilities, and owners’ equity. In simple terms, assets are what a company owns, liabilities are what a company owes, and owners’ equity is the value of the owners’ investment in the business.

Reports that sum up the financial performance of a business are financial statements. A company reports its assets, liabilities, owner’s equity, and net profit on the balance sheet.

Two other key financial elements for a business are the amount of sales and profits. Sales and profits for a specific period are reported in the company’s income statement.

The Balance Sheet

The assets, liabilities, and owner’s equity for a specific date are listed on the balance sheet. The balance sheet is usually prepared every six months or once a year. Figure 12-2 shows a balance sheet.

The left side of the balance sheet lists all assets. Assets are anything of value owned by the business. There are two common divisions of assets. Current assets include cash and those items that can be readily converted to cash such as inventory and accounts receivable. Long-term assets (also known as fixed assets) are the assets with a lifespan of more than a year. Common fixed assets are land, buildings, equipment, and expensive technology.

The right side of the balance sheet is divided into two categories. Liabilities are amounts owed by the business to others. Like assets, there are two types of liabilities. Current liabilities are those that will be paid within a year. Long-term liabilities are debts that will continue for longer than a year. Current liabilities include payments owed to banks and other financial institutions for short-term loans. Also included are

<table>
<thead>
<tr>
<th>Assets</th>
<th>Liabilities</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current Assets</strong></td>
<td><strong>Current Liabilities</strong></td>
</tr>
<tr>
<td>Cash $22,225</td>
<td>Accounts payable $18,250</td>
</tr>
<tr>
<td>Accounts receivable 42,200</td>
<td>Payroll taxes payable 1,900</td>
</tr>
<tr>
<td>Inventory 98,200</td>
<td>Wages payable 23,525</td>
</tr>
<tr>
<td>Prepaid expenses 5,340</td>
<td>Short-term bank loan payable 5,700</td>
</tr>
<tr>
<td><strong>Total Current Assets</strong> $167,965</td>
<td><strong>Total Current Liabilities</strong> $49,375</td>
</tr>
<tr>
<td><strong>Long-term Assets</strong></td>
<td><strong>Long-term Liabilities</strong></td>
</tr>
<tr>
<td>Vehicles 68,500</td>
<td>Long-term notes payable 85,200</td>
</tr>
<tr>
<td>Furniture and fixtures 21,450</td>
<td>Mortgage payable 120,600</td>
</tr>
<tr>
<td>Equipment 33,000</td>
<td><strong>Total Long-term Liabilities</strong> $205,800</td>
</tr>
<tr>
<td>Buildings 320,000</td>
<td><strong>Total Liabilities</strong> $255,175</td>
</tr>
<tr>
<td>Land 82,500</td>
<td><strong>Owner’s Equity</strong> $438,240</td>
</tr>
<tr>
<td><strong>Total Long-term Assets</strong> $525,450</td>
<td><strong>Total Liabilities and Owner’s Equity</strong> $693,415</td>
</tr>
<tr>
<td><strong>Total Assets</strong> $693,415</td>
<td><strong>Total Liabilities and Owner’s Equity</strong> $693,415</td>
</tr>
</tbody>
</table>

Can you tell from this balance sheet if this business is successful?
payments due to suppliers for inventory purchases, supplies, and inexpensive equipment. Long-term liabilities are debts owed for land, buildings, and expensive equipment.

Finally, owner’s equity is the value of the business after liabilities are subtracted from assets. It shows how much the business is worth on the date the balance sheet is prepared. Another way of looking at owner’s equity is that it shows the value of the investments owners have made in the business.

**The Income Statement**

To report the revenue, expenses, and net income or loss from operations for a specific period, a business prepares an income statement. An income statement usually covers six months or a year, but may also encompass a shorter period such as a month. Figure 12-3 shows a sample income statement.

Revenue is all income received by the business during the period. Sources of income include the sale of products and services, plus interest earned from investments. Expenses are all of the costs incurred by the business during the period. Expenses include operations, purchase of equipment, supplies, inventory, payroll, and taxes. The business has net income when revenue is greater than expenses.

<table>
<thead>
<tr>
<th>The Netinc Company Income Statement For the 6-month Period Ending December 31, 20xx</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenue</strong></td>
</tr>
<tr>
<td>Sales</td>
</tr>
<tr>
<td>Sales returns and allowances</td>
</tr>
<tr>
<td>Net sales</td>
</tr>
<tr>
<td>Cost of goods sold</td>
</tr>
<tr>
<td>Interest earned</td>
</tr>
<tr>
<td><strong>Total Revenue</strong></td>
</tr>
<tr>
<td><strong>Expenses</strong></td>
</tr>
<tr>
<td>Selling expense</td>
</tr>
<tr>
<td>Marketing expense</td>
</tr>
<tr>
<td>Administrative expense</td>
</tr>
<tr>
<td>Mortgage payments</td>
</tr>
<tr>
<td>Equipment purchases</td>
</tr>
<tr>
<td>Payroll expense</td>
</tr>
<tr>
<td><strong>Total Expenses</strong></td>
</tr>
<tr>
<td>Income taxes</td>
</tr>
<tr>
<td><strong>Net Income</strong></td>
</tr>
</tbody>
</table>
than expenses. A net loss occurs when expenses are greater than income. Business managers review financial statements carefully to determine how their businesses are performing. Since the statements summarize financial performance for a specific time, the owner can compare the performance of the current period with the performance of last month or last year. If the value of assets is increasing in relation to liabilities, the business is in a better financial position. It may be able to invest in new products, buildings, and equipment. A rapid rise in liabilities or decline in owner’s equity should cause concern. The business must carefully evaluate what is causing the change. If net income is increasing, the owner will want to maintain and improve that performance. On the other hand, if expenses are increasing but revenue is not, the owner will want to determine the reasons for the problem and make changes.

In addition to comparing financial performance from one time period to another, the owner will want to make comparisons with similar businesses. A business that is less profitable than similar businesses, or with lower sales or higher expenses, may have difficulty competing.

### 12-2 Assessment

#### Key Concepts

Determine the best answer.

1. The value of the buildings and equipment owned by a business can be determined in the
   a. inventory records
   b. asset records
   c. records of accounts
   d. tax records

2. True or False. The two most common and important financial records for businesses are the income statement and the balance sheet.

3. Current liabilities are amounts owed that will be paid in less than
   a. one month
   b. six months
   c. one year
   d. five years

4. The current value of investments made by the owners of a business can be found in the
   a. income statement
   b. balance sheet
   c. tax records
   d. record of accounts

#### Make Academic Connections

5. Government. A business is required to collect taxes and make payments to local, state, and federal governments for its employees. Use the Internet to gather information on payroll taxes (local, state, and federal) that must be collected by a business in your community. Prepare a table that identifies each type of payroll tax, how the amount of tax to be collected is determined, and when and to whom the payments must be made.

6. Accounting. Using the examples in Figures 12-2 and 12-3, any records, and your best memory, create a personal balance sheet and income statement. The balance sheet should reflect your personal financial status as of the current date. The income statement should represent your income and expenditures for the past three months.
PAYROLL SYSTEMS

One of the most important financial duties of a business is maintaining a payroll. A **payroll** is the financial record of employee compensation, deductions, and net pay. A payroll system maintains information on each employee to be able to calculate the company’s payroll and to make the necessary payments to each employee.

A business must pay every employee on a weekly, bi-weekly, or monthly basis. A majority of employees in most businesses receive an hourly wage, but the wage rate may be different for each employee. Some employees work part time while others work a full 40 hours or more a week. The rest of the employees, especially managers and others in professional positions, receive a weekly or monthly salary. Again, the amount of salary for each person may be different. Some may earn additional payments in the form of commissions, bonuses, and profit sharing.

**Focus on Real Life**

Zena picked up her paycheck from the human resources office on her way to the parking lot. She had finished a hard week of work and was looking forward to a meal and a movie with friends. She would stop by her bank on the way to the restaurant to deposit her paycheck in her savings account and get some cash for the weekend.

Zena almost hated to look at her paycheck each time she received it. In addition to the check, the company provided detailed information on her earnings and deductions. The information was so detailed that it became confusing. The report showed she had earned an extra day of vacation, but the sick day she had to take last week also was listed. The cost of all of her benefits, including health and dental insurance, reduced her take-home pay by $62 each pay period. In addition, taxes and other required government deductions totaled $143. Halfway through the year, Zena’s deductions and withholding already had topped $3,500. She knew the benefits were important to her, but she didn’t know if she really wanted to look at their cost each time she was paid.

**Key Terms**

- payroll
- payroll record
- direct deposit

**Goals**

> Describe the components of a business’ payroll system.

> Identify information included in payroll records and paychecks.

> Describe the components of a business’ payroll system.
As a part of the compensation system, most businesses provide employees a range of benefits. Benefits may include insurance options, paid or unpaid vacation, sick leave and personal leave, retirement plans, and education assistance. A business must keep records of employee benefits used. Many benefits are a part of payments made to employees as a part of the payroll.

The final part of payroll is tax records and payments. Businesses are responsible for making required federal and state payments for each employee. These taxes consist of income taxes, Social Security, Medicare, and unemployment taxes and are commonly referred to as payroll taxes.

**Income Taxes** The Federal government, most states, and some local governments require employers to withhold income tax from their employees’ pay. The taxes are based on the amount of wages and income and the number of employee dependents.

**Social Security and Medicare** These taxes are often referred to as FICA (Federal Insurance Contributions Act). The government requires employers to withhold and deposit these taxes from employees’ paychecks. Employers must also make matching contributions.

**Unemployment Taxes** Employers pay Federal Unemployment Tax (FUTA) to the unemployment insurance system.

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**A Question of Ethics**

**Disclosing Employee Performance Information**

Following a three-month probationary period, a new employee was fired. The supervisor had heard from several employees that the new worker was hard to get along with and was not carrying her full share of the work. While two work evaluations completed by the supervisor rated her performance as above average, her performance was not outstanding so the decision was made to terminate her employment. When the employee was notified of the decision, she was shocked and asked why she was being fired. Not wanting to create problems for the current employees who had complained or to disclose that the evaluations had not shown serious problems, the supervisor declined to provide reasons. Should the employee have a right to know why she was fired?

There are federal and state laws that regulate an employee’s right to information. An employee generally can examine information in his or her personnel file that relates to work performance. That includes any written notes and formal performance evaluations. An employer should be careful about making judgments that are heavily influenced by the opinions of others without direct evidence. Also, providing regular feedback on evaluations and discussing any issues or concerns before they become major problems are important management responsibilities.

**Think Critically**

1. Do you believe the supervisor was right in not disclosing the information gathered from the new employee’s coworkers? Why or why not? Do you feel the same way about the results of the work evaluations?

2. What recommendations would you make to the supervisor to prevent the type of situation from occurring again? As a new employee, what would you do to make sure you have adequate feedback on how you are doing?
The amount owed is based on the business’ total employee wages. Many states also have their own unemployment taxes.

Employers must withhold taxes from employee wages and salaries as well as make their required contributions. Businesses must prepare and maintain tax records. They also have to send required payments to the government on time.

Most payroll systems are part of a larger personnel records system. That system is a central location for all information the company maintains on all employees from the time they are hired until well after they no longer work for the business. Personnel records include personal information, employment history, performance evaluations, compensation records, and other information needed by the company. Most information in personnel files is confidential. Because of this, the businesses must carefully and securely maintain the records.

PREPARING A PAYROLL

Maintaining payroll records and preparing paychecks is an ongoing and time-consuming task for businesses. In the past, each employee completed and submitted a time card. Payroll clerks entered the information into each employee’s payroll record. When paychecks were to be issued at the end of each pay period, employee compensation and deductions had to be calculated, withholding and benefits records completed, and paychecks prepared. Today, computerized payroll record systems make the process more efficient and accurate. The software needed to manage a basic payroll system can be purchased at a relatively low cost. The system can collect employee work records each day. At the time paychecks need to be prepared, all information on benefits and deductions is entered and each employee’s pay is calculated. All payroll records are updated and individual paychecks are prepared.

Payroll Records

The form used to track each employee’s pay history is a payroll record. Each payroll record holds the employee’s name, Social Security number, address, and other needed personal information. It also includes individual tax information and a record of benefits such as vacation and sick days available and used. The employee’s current and year-to-date earnings, deductions, gross pay, and net pay are maintained in the

CHECKPOINT

What is the purpose of the payroll system?
payroll record. A similar payroll record is kept for each part-time and full-time employee. An example of an automated payroll record is shown in Figure 12-4.

Preparing Paychecks
After all employees’ payroll records have been completed and pay amounts have been calculated, a paycheck is prepared for each person. Employees will want to know how the amount of pay they receive is determined and the type and amount of deductions made. Most businesses print an earnings report that is included with the employee’s paycheck. The earnings report usually includes information for the current pay period as well as the cumulative amounts for the year. An example employee paycheck and earnings report is shown in Figure 12-5 on the next page.

Businesses may offer a direct deposit service for employees. With direct deposit, the employer transfers net pay electronically into the employee’s bank account. The employee does not receive a paycheck but is given a receipt of the funds transfer and an earnings report. The receipt may be posted on a benefits web site where the employee can print it out, if desired.

CHECKPOINT
What is the difference between a payroll record and an earnings report?

Work as a Group
Review the information in the Focus on Real Life at the beginning of the lesson. Discuss with your group what you could say to Zena to help her feel better about the deductions shown on her paycheck that reduced the amount of her take-home pay.
12-3 Payroll Management

An Employee’s Paycheck and Earnings Report

Marquese Co.
Anchora, IN

Employee Jan Exrace
2346 Transport Dr.
Tollboard, IN

Employee ID 83-221

Pay Begin Date 11/22/20--
Pay End Date 12/29/20--

Pay to the Order of $361.33

Amount Three Hundred Sixty One and 33/100 dollars

BankCo, USA Evincey, IN

Paula Morris, Marquese Co.

<table>
<thead>
<tr>
<th>Description</th>
<th>Current Year-to-Date</th>
<th>Taxes Current Year-to-Date</th>
<th>Deductions Current Year-to-Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regular Wage</td>
<td>$480.00</td>
<td>$91.20</td>
<td>$31.99</td>
</tr>
<tr>
<td>Overtime</td>
<td>$ 36.00</td>
<td>$24.00</td>
<td>$7.48</td>
</tr>
<tr>
<td>Net Pay</td>
<td></td>
<td></td>
<td>$361.33</td>
</tr>
</tbody>
</table>

Marquese Co.
Anchora, IN

Pay Begin Date 11/22/20--
Pay End Date 12/29/20--

Pay to the Order of $361.33

Amount Three Hundred Sixty One and 33/100 dollars

BankCo, USA Evincey, IN

Paula Morris, Marquese Co.

Xtra! Study Tools

How is the employee’s net pay determined?

12-3 Assessment

>> Key Concepts

Determine the best answer.

1. The financial records of employee compensation, deductions, and net pay are known as
   a. compensation
   b. payroll
   c. earnings report
   d. paycheck

2. True or False. Businesses are responsible for making required federal and state payments for each employee.

3. The electronic transfer of net pay into an employee’s bank account is known as
   a. tax withholding
   b. FICA
   c. direct deposit
   d. an automated payroll system

4. True or False. Payroll records need to be maintained for all full-time employees, but not for part-time employees.

>> Make Academic Connections

5. Math Calculate the amount of employee withholding for Social Security (6.2%) and Medicare (1.45%) for each of the following employee’s wages.

Marjorie Elder $865.00
Antoine Fresher $726.40
Amelda Francois $1,480.90

6. Art Create a poster or flowchart that illustrates the steps in the payroll process from the point that employees complete their work until their paychecks are issued.
Financial Decision-Making

**Goals**
- Recognize important financial information managers use to make decisions.
- Identify the steps in making financial decisions in business.

**Key Terms**
- financial performance ratios
- discrepancies

**Focus on Real Life**

There are an increasing number of computer applications and online tools that can make managing financial information easier. One such tool is the electronic budget. Available online or in software programs, budgeting tools can expertly help manage finances and assist with financial decision-making. Electronic budgets are easy to use. They save time and offer managers more useful information than a budget done on paper. Electronic budgets provide detailed reports of various financial data. They can even do the math for you! One key benefit of electronic budgets is that you can look at “what-if” projections. For instance, you could determine how your business’s expenses would be affected if you decided to increase your advertising budget. You could compare the results of hiring a temporary employee versus a full-time employee. Electronic financial tools help make a difficult management task easier and more accurate.

**USING FINANCIAL INFORMATION**

Financial statements are important management tools for business owners and managers. Financial statements present summaries of the financial activities of a business. Managers who understand the information in financial statements will be able to make decisions that result in the wise use of the company’s money.

**Important Financial Information**

As previously discussed, the three most important elements of a company’s financial strength are its assets, liabilities, and owners’ equity. Two other key financial elements for a business are the amount of sales and profits. A company reports its assets, liabilities, owners’ equity, and net profit on the balance sheet. Sales and profits for a specific period are reported on the company’s income statement.

What are the pros and cons of having a team of people help make decisions?
Understanding Financial Performance Ratios

Managers use those financial elements to calculate financial performance ratios. **Financial performance ratios** are comparisons of a company’s financial elements that indicate how well the business is performing. Some important financial performance ratios are the current ratio, debt to equity ratio, return on equity ratio, and net income ratio. Figure 12-6 shows the formulas used to calculate each ratio.

**Current Ratio** Current assets compared to the current liabilities is the current ratio. Current assets are those that the business could convert to cash within one year. Current liabilities are all payments that the business must make within one year. The current ratio tells you if the business can pay its debts when they become due. The current ratio should be at least 1:1 for a healthy business. A 1:1 ratio means that there are at least as many current assets as current liabilities.

**Debt to Equity Ratio** The company’s liabilities divided by the owners’ equity is the debt to equity ratio. The debt to equity ratio tells you how much the business is relying on money borrowed from others that will have to be paid back rather than money provided by the owners. Most banks want to see a debt to equity ratio no higher than 2:1. Too much debt puts a business at risk because it may have trouble meeting its obligations to its lenders.

**Return on Equity Ratio** The net profit of the business compared to the amount of owners’ equity is the return on equity ratio. The return on equity ratio shows the rate of return the owners are getting on the money they invested in the company. It should be compared to the return they could receive if they used their money in other ways such as savings, investing in other companies, or purchasing stocks and bonds.

**Net Income Ratio** The total sales compared to the net income for a period such as six months or a year is the net income ratio. The net income ratio shows how much profit is being made by each dollar of sales for the period being analyzed. You should compare the net income ratio to past periods and to competing companies. The ratio will show if additional sales are as effective at adding to the company’s profit as those in the past.

### Figure 12-6

<table>
<thead>
<tr>
<th>Financial Performance Ratio</th>
<th>Formula</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Ratio</td>
<td>Current Assets / Current Liabilities</td>
</tr>
<tr>
<td>Debt to Equity Ratio</td>
<td>Total Liabilities / Owners’ Equity</td>
</tr>
<tr>
<td>Return on Equity Ratio</td>
<td>Net Profit / Owners’ Equity</td>
</tr>
<tr>
<td>Net Income Ratio</td>
<td>Total Sales / Net Income</td>
</tr>
</tbody>
</table>

What does it mean if your company’s net income ratio increases from one year to the next?
MAKING FINANCIAL DECISIONS

Managers are responsible for the financial health of their company and for the specific areas of the company under their control. If adequate finances are not available, the work that is required will not be done as well or as quickly as needed. On the other hand, if more money than is needed is used for certain operations, there may not be enough for other parts of the company.

The first step in financial decision-making is preparing a budget. The budget identifies the amount of money needed for all parts of the business to complete planned activities. It also projects what types and amounts of income will be earned from the sale of the company’s products, services, and other investments.

Once a budget is developed and approved, managers use the budget as a guide to the operations of the business. They regularly check to see if income and expenses are meeting budgeted amounts. Income should be as high as or higher than planned. Expenses should not exceed the budgeted amount. Managers get regular financial reports. They examine them carefully, looking for discrepancies. Discrepancies are differences between actual and budgeted performance. Discrepancies let managers spot problems before they become serious enough to harm the business. They might also see areas where financial performance is better than what was budgeted. In that case, they determine the reasons for success and inform other managers whom the higher level of performance might affect.

The final step is to make needed adjustments. If income and expenses are similar to the budget, the manager will not need to take action. If there are financial problems, managers will take corrective action to try to bring performance back in line with the budget. That might include finding ways to improve revenue as well as seeking ways to cut expenses. In some cases, performance cannot be improved or factors outside the managers’ control are
responsible for the poor performance. The managers may have to adjust the budget. That should be done as a last resort since the budget had been carefully planned.

At the end of the period covered by the budget, the business will prepare new financial statements. It will use the results to determine the financial success of the operations. The company will also use the results to improve the budgeting process in the future.

Businesses usually hold managers responsible if their part of the company faces financial problems. On the other hand, they will be rewarded if they are effective in managing the financial resources of the company.

Work as a Group

Use the information from Figures 12-2 and 12-3 to calculate each of the four financial performance ratios described in this lesson. Discuss what the results mean for the businesses.

12-4 Assessment

Key Concepts

Determine the best answer.

1. Which of the following is not one of the three most important elements of a company’s financial strength?
   a. assets
   b. owners’ equity
   c. payroll
   d. liabilities

2. True or False. Sales and profits for a specific period are reported in a company’s income statement.

3. True or False. Employees rather than managers are responsible for the financial health of a company.

4. Differences between actual and expected performance are
   a. financial performance ratios
   b. budgets
   c. profit or loss
   d. discrepancies

Make Academic Connections

5. Communication You are responsible for helping a new manager understand financial statements. Prepare and present a short presentation explaining the importance of the balance sheet and income statement. Use a computer and presentation software to develop several slides for your presentation.

6. Critical Thinking In comparing current operating costs with the budget, you see that payroll expenses are much higher than budgeted, but income has not increased. How would you attempt to identify the problem? What might be some reasons for the discrepancy?
Chapter 12

Assessment

Business Notes

12-1 Financial Planning
1. The financial questions that must be answered in a business include: How much money is needed to start the business? From where will the financing come? How will funds be obtained to run the business for the months or years until it becomes profitable? What will be the best sources of sales and other income? What will be the expenses? When must they be paid?

2. The four main steps in budget preparation are: prepare a list of the income and expenses that will be a part of the budget; gather accurate information for each income and expense; create the budget by calculating each type of income, expense, and amount of net income or loss; and show and explain the budget to people who need financial information to make decisions.

3. There are three types of business budgets. The start-up budget plans income and expenses from the beginning of a new business or a major expansion until it becomes profitable. The operating budget describes the financial plan for ongoing operations of the business for a specific period. A cash budget is an estimate of the actual money received and paid out for a specific period.

12-2 Financial Records and Financial Statements
4. Financial records are used to record and analyze the financial performance of a business. The types of records maintained include asset, depreciation, inventory, account, cash, payroll, and tax records.

5. The two most common and important financial statements for businesses are the income statement and balance sheet. The business’ assets, liabilities, and owners’ equity for a specific date are listed on the balance sheet. An income statement reports the revenue, expenses, and net income or loss from operations for a specific period.

12-3 Payroll Management
6. A payroll is the financial records of employee compensation, deductions, and net pay. A payroll system maintains information on each employee to be able to calculate the company’s payroll and to make the necessary payments to each employee.

7. A payroll record is a form used to document each employee’s pay history. It includes such information as name, Social Security number, address, and tax and benefit records. After all payroll records have been completed and pay amounts have been calculated, a paycheck is prepared for each person. A paycheck usually includes the current and cumulative pay amounts and the type and amount of deductions.

12-4 Financial Decision-Making
8. The three most important elements of a company’s financial strength are assets, liabilities, and owners’ equity. Two other key elements for a business are the amount of sales and profits. Managers use those financial elements to calculate financial performance ratios to make decisions that result in the wise use of the company’s money.

9. The first step in financial decision-making is preparing a budget. Second, managers use the budget as a guide to the operations of the business. The final step is to make needed adjustments.

Communicate Business Concepts

1. Identify several unique business expenses for the three times in a business’ life: start-up, ongoing operations, and expansion.

2. What is the difference between a budget and a financial record? Why are both needed in a business?
3. Why is it important to maintain an accurate cash budget for a business? What happens to a business if it does not have access to cash even though it has other assets worth a lot of money?

4. What information is contained in a balance sheet that is not in an income statement? Is there any similar information in both types of financial statements?

5. Confidentiality of the personal information of employees is very important in businesses and other organizations. If you were the payroll manager of a large company and had several employees who had access to personnel and payroll records, what would you do to protect the confidentiality of the information that they could access as a part of their work?

6. The use of direct deposit for employee paychecks saves businesses and banks a large amount of time and money. Many employees are still reluctant to use it. What are some reasons people may not want to use this system? What could you say to a friend to convince them to use direct deposit?

7. Why are the assets, liabilities, and owners’ equity more important to the financial strength of a business than the amount of profit they earned in a particular period?

8. If you were a stockholder in a business, which of the four financial performance ratios would be most important to you? Why? If you were a banker considering loaning money to a business, which ratios would be most important to you? Why?

9. Do you believe the financial performance of a business is a more important measure of a manager’s effectiveness than other factors, such as customer satisfaction or employee satisfaction or turnover? Justify your answer.

>> Develop Your Business Language

Match the terms listed with the definitions.

10. Reports the revenue, expenses, and net income or loss from business operations for a specific period.

11. Provide detailed plans for the financial needs of individuals, families, and businesses.

12. The employer electronically transfers net pay into the employee’s bank account.

13. Plans income and expenses from the beginning of a new business or a major business expansion until it becomes profitable.

14. Used to record and analyze the financial performance of a business.

15. All income that a business receives over a period of time.

16. Lists the business’ assets, liabilities, and owners’ equity for a specific date.

17. Differences between actual and budgeted performance.

18. Describes the financial plan for ongoing operations of the business for a specific period.

19. What a company owns.

20. The costs of operating a business.

21. An estimate of the actual money received and paid out for a specific period.

22. A form used to document each employee’s pay history.

23. Comparisons of a company’s financial elements that indicate how well the business is performing.

24. The financial records of employee compensation, deductions, and net pay.

25. The value of the owners’ investment in the business.


Key Terms

a. assets
b. balance sheet
c. budget
d. cash budget
e. direct deposit
f. discrepancies
g. expenses
h. financial performance ratios
i. financial records
j. income statement
k. liabilities
l. operating budget
m. payroll
n. payroll record
o. owner’s equity
p. revenue
q. start-up budget
>> Decision-Making Strategies

Dominique sat at his office computer reviewing the financial statements for his three-year-old business. He had yet to make a profit. He was able to pay himself a small salary but still had to hold a part-time job to maintain his family’s lifestyle. He had added a part-time employee and needed another, but didn’t have the money to pay another person right now. Dominique studied the business’ balance sheets and income statements side by side. The balance sheets showed that the value of assets was increasing. Liabilities had increased as well due to the need to continue to borrow money to purchase inventory as his sales increased. He had been able to make regular payments on his building and equipment loans, so long-term liabilities were decreasing. There had been no change in the value of the owner’s equity, so his investment was not paying off. When he shifted his attention to the income statement, he could see that sales were up sharply, but so were the costs of his inventory and operating expenses. He did notice that he had more cash on hand to pay bills as they came due and that the losses were getting smaller and smaller.

27. What financial information that Dominique reviewed do you believe is positive? What information is negative?

28. Based on the financial information provided, do you believe Dominique’s business is successful or not? Justify your answer.

>> Make Academic Connections

29. **MATH** Lee Chan has owned a video business for three years. The first year, Mr. Chan barely earned a profit. The next year’s profit was more substantial. As shown in the table, he has just received the financial results from the third year and wants to compare them to those of the second year of operations.

   a. How much money did Mr. Chan earn each year?
   b. What was his total cost of doing business each year?
   c. What profit or loss did Mr. Chan earn this year? What is the difference with the profit or loss from last year?

<table>
<thead>
<tr>
<th></th>
<th>Last Year</th>
<th>This Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rent</td>
<td>$28,000</td>
<td>$28,000</td>
</tr>
<tr>
<td>Sales</td>
<td>78,250</td>
<td>80,725</td>
</tr>
<tr>
<td>Inventory</td>
<td>15,000</td>
<td>13,750</td>
</tr>
<tr>
<td>Payroll</td>
<td>17,850</td>
<td>18,210</td>
</tr>
<tr>
<td>Utilities</td>
<td>10,010</td>
<td>7,075</td>
</tr>
<tr>
<td>Supplies</td>
<td>1,020</td>
<td>2,020</td>
</tr>
</tbody>
</table>

30. **TECHNOLOGY** Use the Internet to identify two software programs that can be used by a small business to manage payroll. Evaluate the two programs and prepare a table that compares the features of the two programs. Prepare a written recommendation to a business owner on the software you believe would be the best choice with reasons for your decision.

31. **ECONOMICS** The budgets of a business are affected by events and changes outside the business, including the actions of competitors, and the strength and weakness of the local, national, and global economies. Review recent newspapers and business magazines. Find several articles that report on the economy and competition that could have a positive or negative effect on businesses in your community. Prepare a note card for each article on which you summarize the key points of the article and describe how the information could affect the financial decisions made by business managers.

32. **GOVERNMENT** Visit the web site of the United States Internal Revenue Service (www.irs.gov). Locate information on the following tax forms related to business payroll: W-2, W-4, 940, and 941. Prepare a brief description of the purpose of each form, who is responsible for completing the form, when it must be completed, and where it is sent or distributed.
>> Linking School and Home

Obtain an earnings report (pay stub) from a paycheck from your own job or from a family member. Identify the total amount of wages or salary earned during the pay period. Then identify the amount of each deduction listed. Calculate the percentage of the total wage or salary represented by each deduction. Then calculate the percentage represented by the total of all deductions. Finally, determine the percentage of the total wage or salary represented by the net pay.

>> Portfolio Activity

To provide tangible evidence of your learning about financial management, do the following:

COLLECT information that describes the financial planning process and tools used in business.

CREATE a flowchart that shows the process a manager would follow in developing and using a budget to manage a department in a business.

CONNECT your visual to other items already in your class portfolio, or relate it to an important concept you learned in another class. Make the connection by preparing a one-minute presentation on the importance of effective financial planning and decision-making to the success of a business.

Human Resource Management

The hospitality industry requires employees to strive to satisfy the needs of customers. You are the Human Resources Director for a new 500-room luxury hotel that will be celebrating its first anniversary in three months. You have the responsibility to design a professional development meeting that not only recognizes employees for good performance, but also teaches more about customer service and teamwork. The meeting must cover company goals, strategies, and incentives and involve employees in team activities that strengthen employee relationships. Team games, activities or challenges, and prizes/rewards for accomplishment should be incorporated. You must create the agenda for team participation and corporate understanding. You have 30 minutes to outline your strategy and seven minutes to present the plan to the hotel general manager or students in the class. Up to three minutes will be allowed for judges’ questions.

Performance Indicators Evaluated

- Demonstrate understanding of human relations skills.
- Describe why professional development is the responsibility of the business and its employees.
- Demonstrate effective and informative communication and presentation skills.
- Discriminate successful evaluation techniques.
- Discuss compensation, benefits, and incentive programs.
- Demonstrate knowledge of human resources management and management concepts.
- Application of critical thinking skills to interpret personnel policies.
- Demonstration of effective oral communication skills.
- Communication of employee benefits and compensation.

For more detailed information about performance indicators, go to the BPA web site.

Think Critically

1. Why must professional development meetings include games and prizes?
2. What is the main purpose for professional development activities?
3. What strategy can be used to provide associates with essential new information while strengthening the company team concept?
4. What prizes or gifts can the hotel provide at the professional development meeting?
Planning a Career in...
Industrial Engineering

Industrial engineers work to improve the ways that businesses use the factors of production to develop products and services needed by businesses and consumers. They are involved in improved product design. They help to improve operating performance of production and manufacturing businesses.

Industrial engineers are scientists and researchers. They look for ways to improve product designs and integrate technology to improve work procedures. Industrial engineers conduct research and apply mathematical and statistical models to problems. They design production planning and control systems to coordinate activities and ensure product quality.

Although most industrial engineers work in manufacturing industries, they also work in consulting businesses, health care, government, and universities.

Employment Outlook
• While the number of manufacturing companies and jobs is declining, the demand for industrial engineers is stable.
• Because businesses need to make higher-quality products efficiently and safely, the services of industrial engineers should remain in demand.
• The concern for health and safety within work environments should increase the need for health and safety engineers.

Job Titles
• Project Engineer
• Operations Analyst
• Quality Engineer
• Ergonomist

Needed Skills
• Mechanical aptitude
• Math and quantitative abilities
• Common sense and objectivity
• Organization and efficiency
• Excellent communication skills
• Creative problem solving

What’s it like to work in...
Industrial Engineering

Four industrial engineers were gathered at the national conference of the Institute for Industrial Engineering. They had all graduated 10 years ago and were discussing their recent projects.

Rachel had just redesigned a production process resulting in a reduction of worker injuries. Alistair was developing a prototype for a wristwatch-sized GPS unit for hikers and campers. Jacob had spent the last three years redesigning the emergency room layout, equipment, and procedures for a hospital in London. Frank had been accepted as an astronaut candidate. He would be training as a mission specialist to install new electronics systems in a space station.

They realized, as they talked about their work, that they were in an exciting professional area. They were making important contributions to their organizations and to society. They agreed to meet again in a few years and see where their careers had taken them.

What about you? Why do you think industrial engineers are able to work in such varied types of businesses?
Types of Production

PRODUCTION AS AN ECONOMIC ACTIVITY

The economy begins with production. Consumers need products and services to satisfy their needs and wants. Businesses also need products and services. They incorporate products and services into the products they produce and use them in operations. They also resell them to their customers.

Role of Producers

The three categories of products used by businesses and consumers are

- **Natural Resources** Raw materials supplied by nature
- **Agricultural Products** Crops and animals grown by farmers
- **Processed Goods** Products that have been changed in form to increase their value and usefulness

The following types of businesses make products.

- **Producers** Develop products to sell to other businesses or consumers
- **Extractors** Obtain natural resources, such as water, oil, coal, and timber, from the earth for processing and use
- **Farmers** Tend land and other natural resources to grow crops and livestock that are later sold and processed
- **Manufacturers** Obtain materials from other producers and convert them into products for sale to consumers and other businesses

Focus on Real Life

When you buy a pair of jeans, you probably do not think about the activities and businesses involved in making them. An interesting sequence of events occurs. First, farmers plant and harvest the cotton and sell it to a textile company. The textile company makes it into cloth and dyes it different colors. Other companies make thread, rivets, zippers, and leather. The jeans are designed. The cloth and other materials are used to make the jeans in various styles, colors, and sizes. They are labeled, inspected, and boxed before they are ready to be shipped to retailers and sold.

Different businesses, large or small, complete all of these processes. They are often located in different parts of the world. These businesses are different in many ways, but are alike in that they all are a part of the production process. They help put a product or service that you want on the market. Producers are an important, but often less visible, part of the economy that supplies the goods and services you want.
Extraction and cultivation ensure that there is an available supply of natural resources and the crops, livestock, fish, and other agricultural products needed. This is the most basic form of production.

**Processing** involves changing and improving the form of another product. Few products are used exactly as they are found in nature or grown on farms. Most are processed in some way before they are used. Water must be filtered and treated with chemicals before it can be consumed or used in the production of other products. Timber is cut and formed into lumber or processed into paper or other materials. Oil is pumped from deep in the earth. The oil is then sent to refineries to be converted into gasoline, heating oil, and petroleum-based products. They are then used in the production of other products such as plastics, cosmetics, medicines, and food. The crops and livestock raised by farmers are sent to processing plants. They are inspected, packed, and shipped to supermarkets or are processed and combined with other products. This gives you the variety of foods you prepare at home or order in a restaurant.

**Manufacturing** combines raw materials and processed goods into finished products. Either other businesses or final consumers may use those finished products. Manufacturing can be as simple as a craftsman using tools and materials to build cabinets for a kitchen. It also can be as complex as designing a microchip for a computer or building a high-speed rail system.

Each of these forms of production is needed to make all of the goods and services demanded by businesses and consumers. Each requires specialized tools and equipment, in addition to well-trained and often highly skilled personnel. The requirements to locate and pump oil from miles below the ocean floor, to design and build the equipment needed to create artificial diamonds, or the ability to plan and build a small aircraft that can be piloted from the Earth's atmosphere to the beginnings of space are hard to comprehend. But they are no more important to your quality of life than the expertise of the production team on an assembly line installing airbags into automobiles or the capability of the person inspecting the prescription drugs as they are processed and packed for distribution to hospitals and pharmacies.

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**CHECKPOINT**

What are the three forms of production?
Manufacturers get products or raw materials from other businesses. They change them into a form that their customers can use. One manufacturer might make many parts into products such as skis or snowmobiles for winter sports. Another may purchase and process meat, vegetables, and fruit into frozen entrees you can heat in your microwave. A third takes timber and processes it into lumber and plywood. A construction company then obtains those building materials to build a new neighborhood in your town.

Types of Manufacturing Procedures
Manufacturing businesses can set up production in several ways to make their products. The number of products needed and the characteristics of the products will determine the type of manufacturing procedures.

Mass Production
An assembly process that makes a large number of identical products using a continuous, efficient procedure is **mass production**. Mass production is sometimes called repetitive production. Automobile assemblies or beverage bottling plants businesses around the world complete those activities. The raw materials and processed goods move long distances as they are produced, processed, and prepared for sale. Working together, extractors and manufacturers each add their unique processes that change the form of raw materials into products that fill consumers’ needs.

**A Manufacturing Process**
Usually, several manufacturers are a part of the total activity needed to produce goods that are purchased by consumers or other businesses. Think about the jeans described in Focus on Real Life. The whole process calls for several steps performed by a number of businesses. For example, a textile mill in North Carolina buys cotton grown on an Alabama farm. It spins the cotton into yarn and makes the yarn into fabric. A plant in New England then dyes and prints the cloth. A clothing manufacturer in New York buys the cloth and makes it into jeans. Increasingly,

Work as a Group
In your group, create a table with three columns. Label each column with one of the types of manufacturing procedures. Agree on five products that would be manufactured using each procedure and list them in the column under the correct heading.

Differentiate among the various types of manufacturing.

What makes an assembly line a more efficient way of manufacturing?
often use this type of production. Mass production allows a business to assemble products in a very large quantity and at a low cost.

With mass production, employees usually have precise tasks. They use specialized tools and equipment as they work on product assembly. That allows training costs to be lower and quality to be higher. It can also result in monotonous work and reduced motivation. Companies have been testing ways to add variety and raise the quality of work in factories that use mass production. Computers and mechanized equipment now assist with or perform many of the procedures on an assembly line.

**Custom Manufacturing**

Building a specific and unique product to meet the needs of one customer is done with **custom manufacturing**. Manufacturers make products ranging from dentures to a concert hall to meet particular design standards. When each customer has quite different needs or someone is building the product for a specific use, it may require custom manufacturing.

A business using custom manufacturing works closely with the customer to plan and design the product. It may call for unique materials or a special assembly process. With products such as buildings, bridges, or landscaping, the construction takes place at a new site each time. In other situations, such as the design of a unique tool for the space program or a special running shoe for a professional athlete, the design and assembly of the unique product will occur at the manufacturer’s site. Sometimes, a small team of designers, toolmakers, and assemblers take part in highly specialized custom manufacturing. This team works closely with the customer and each other to create a particularly unique product such as a musical instrument or race car.

**Materials Processing**

Changing the form of raw materials so they can be consumed or used to make other products is **materials processing**. Oil companies refine crude oil to form gasoline and other petroleum products. Mills process grain into flour, cereal, and feed for animals. Film processors convert the film from cameras or X-ray machines into photographs or other images.

There are two types of materials processing. With **continuous processing**, the raw materials constantly move through

**FYI**

In 2002, 344,000 U.S. manufacturers produced and sold nearly $4 trillion dollars of products. Ten years earlier, there were more manufacturers—over 370,000—but they produced nearly a trillion dollars less. Reorganization, new technology, and production efficiency result in more products from fewer businesses.
specially designed equipment. This changes them into a specific product useable for consumption or for further manufacturing. Raw milk is sprayed into huge drying machines to produce powdered milk. Mills dry corn and then grind it for use in the production of feed for cattle or flakes for cereal.

Intermittent processing uses short production runs to produce a precise amount of a variation of a product. The machinery or materials are reconfigured each time to provide the required variation. A printer uses intermediate processing to complete a special order of stationary or to print and assemble a uniquely designed brochure. A baker resets the equipment to blend and bake wheat bread after making a batch of pumpernickel loaves.

13-1 Assessment

**Key Concepts**

Determine the best answer.

1. Which of the following is not one of the categories of products used by consumers and businesses?
   a. natural resources
   b. agricultural production
   c. processed goods
   d. All of the answers are correct.

2. True or False. The most basic form of production is manufacturing.

3. Building a specific and unique product to meet the needs of one customer is known as
   a. materials processing
   b. mass production
   c. extraction
   d. custom manufacturing

4. Intermittent processing would most likely be used in the production of
   a. automobiles
   b. customized houses
   c. textbooks
   d. televisions

**Make Academic Connections**

5. **History** Gather information and prepare a two-page written report on the early use of mass production and automation in manufacturing.

6. **Science** Select an article of clothing or a popular food item. Conduct research to determine the major raw materials and natural resources that are used in the production of the product. Identify the country or countries that are the major sources of the production or supply of those materials.
Production Planning

Goals

- Identify the activities involved in production planning.
- Describe how manufacturing is organized.

Key Terms

- Applied research
- Pure research
- Production process
- Continuous process improvement
- Benchmarks

Focus on Real Life

Today, American businesses see W. Edwards Deming as a hero. That was not always the case. In the 1950s and 1960s, people thought that U.S. manufacturers were the best in the world. Dr. Deming had devoted his life to studying quality issues and applying quality improvement procedures. In 1946, he formed the American Society for Quality Control. He tried to talk with American businesspeople about his ideas, but they were not interested. Japanese managers were trying to rebuild their industries. They asked Dr. Deming for assistance. His work helped Japanese businesses become international leaders in product development and product quality. Deming is a folk hero in Japanese society. Because of the Japanese success, U.S. businesses began to study Dr. Deming’s ideas and implement his quality-improvement processes. Today, businesspeople worldwide are aware of W. Edwards Deming’s 14 points for management.

Production Activities

Production and manufacturing processes are very complex. They involve a number of activities and resources that businesses must carefully plan and coordinate. Before a company can manufacture a product, it must have the facilities and equipment needed to carry out the production activities. The company must obtain the materials needed for production. It must hire enough people with the required skills. It must check finished products for quality and store them until sold. The business must then effectively distribute them to customers.

Product Development

Before any production planning can occur, the company decides what products it will produce. A business cannot rely on selling the same products year after year. As customer needs and competition changes, new products will have to be developed. Product planning involves two steps—new product research and product design.

Product Research

Companies devote a large amount of their resources to discovering new product ideas. Together, U.S. businesses spent over $200 billion for research in 2003. Many scientists and engineers devote all of their work time to research and development activities. Their goals are to develop new products that will meet the needs of customers and improve the current products offered by the company and its competitors.

Companies carry out two types of research to discover new product ideas. Applied research studies existing...
products to develop design improvements or new product uses. Engineers working for an automobile manufacturer will study the current designs to improve the efficiency of engines or increase passenger safety. **Pure research** is research done without a specific product in mind with the goal of discovering new solutions to problems. For example, scientists working for drug manufacturers study diseases and immune systems of the body. Their goal is to uncover treatments and cures.

**Product Design** When scientists develop a new product idea, businesses must turn that idea into a product that they can make and sell profitably. Design engineers create models and test them to come up with the best possible design. They select materials that make the product useable and durable.

After engineers build and test a model, the business determines all of the materials and parts needed for the final product. Financial experts determine the cost of making the product. They will get information from customers and competitors to decide the price at which they can sell the new product. By comparing cost and pricing information, the business can determine whether they can make and sell the product profitably.

**Production Planning** Once a company develops and tests a new product idea and concludes that it can sell the product at a profit, the company then develops plans to produce the product. Production planning includes three activities. First, the company develops a production process. Next, it obtains production resources. Finally, the company identifies and prepares production personnel.

**Production Process** The activities, equipment, and resources needed to manufacture a product are part of the **production process**. If the business will make the product using mass production, it must organize the assembly line. Customized manufacturing requires that the company identify the assembly steps and procedures for customizing each product.

**Production Resources** Next, the business orders or builds the machines, tools, and other equipment required for each of the production processes. Often, new products will call for customized equipment. The business must locate and organize adequate space to perform the needed production activities. This allows employees to complete work efficiently and safely. In some cases, a business will have to buy or construct a new building. In other situations, it can

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**Work as a Group**

Make a list of several new products that some members of your group like and some do not. Discuss the differences among the products and determine what makes some products appealing and others unappealing.

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convert current facilities from the production of older products that are being discontinued.

Another planning step is to determine the sources of the raw materials, parts, and supplies needed to make the product. Often the manufacturing company will not have the needed resources. It will have to identify suppliers and negotiate agreements to make sure an adequate and timely supply is available at an appropriate price. The company may decide it can produce some of the parts and materials needed.

**Personnel** Finally, the company does personnel planning. It estimates the number of employees needed to complete all production activities. It determines the skills required of each employee. The company will check to see if there are enough employees in the company and if they have the needed abilities. If not, it must hire and train new employees. Another option is to find a separate company with the ability and employees needed to complete some or all of the production activities.

**Inventory Management**

*Inventory* is a detailed account of a company’s materials, supplies, and finished products. *Inventory management* maintains the supply of all resources needed for production and the products produced. Inventory management is a vital manufacturing activity. Most products are assembled using many different parts and supplies. Each of the items needed to make a product must be available at the time and place needed for assembly. If an item is not on hand,

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**Philips HomeLab**

Can your home sense that you are too hot or cold and automatically adjust the temperature? As you fix a meal in the kitchen, can you use voice commands to choose menu items, measure ingredients, and control appliances? That is the vision guiding research in the Royal Philips electronics company. Their scientists created a laboratory called HomeLab in Eindhoven, The Netherlands. HomeLab is an actual two-story house occupied by people who live there 24 hours a day. They are observed as they interact with prototypes of products the company is designing.

Philips calls the technology it is studying ambient intelligence. They believe that, in the home of the future, technology and people will be united in a way that the technology responds to the movements, sounds, gestures, and physical characteristics of the home’s residents. They anticipate that their research will allow them to develop products ranging from lighting and appliances to entertainment units and even clothing that can interpret and respond to individual expectations and actions.

While the HomeLab is a very expensive research investment, the company believes it provides an ideal setting to conceive, test, and improve new products in an environment that reflects the way consumers live. They also believe it will speed the new product development process since the products are tested at the same time they are being developed. According to Philips’ Chief Technology Officer, “Our innovation is centered around what consumers want. By observing them using our technology in their natural habitat—the home—we can better adapt that technology into real-world products.”

**Think Critically**

1. What problems might the researchers encounter when observing people who know they are being observed? How might they overcome these problems?

2. Other than those listed, what types of products do you believe could benefit from study in this type of research laboratory?
the assembly process must be stopped. On the other hand, if a supply of any of the items is much larger than the business can use in a short time, inventory and storage costs will be too high.

Inventory managers keep records of the supply and cost of all resources used in production. They work to ensure that suppliers deliver orders on time and in the correct quantities and price. The business maintains adequate storage space to make sure it can easily locate parts and materials and move them to production lines as needed. The space is planned to make sure that materials are safe and secure and can be moved quickly and easily.

After the business completes product assembly and inspection, it moves the products for storage or for immediate distribution to customers. The business must keep an accurate product inventory in order to make sure it can fill customer orders. If there are not enough products available, it will miss sales. Too many products in inventory raise costs. In addition, products run the risk of becoming outdated before they are sold.

**Checkpoint**

Describe the three activities that are a part of production planning.

**Manufacturing Procedures**

One of the biggest changes in manufacturing businesses is the production procedures used. Pictures of old factories show long assembly lines with employees located at workstations along the line. Each employee is surrounded by tools and a supply of any parts they need to complete their part of the product assembly. Products moved slowly along the line and frequently stopped. Often, additional time was needed to complete an assembly procedure, correct a problem, or repair equipment.

Today, assembly is quite different. Employees often work in teams, completing many procedures together. Each employee is trained to be able to perform several assembly procedures. Supplies and parts move along conveyor belts or on carts to arrive just as they are needed. Many products are customized to meet specific customer requirements as they are assembled. Managers, team leaders, and employees look at the screens of computers that monitor the assembly process and provide production information. Other employees quickly step in to repair equipment or help to solve problems. Products move rapidly through the assembly process. Employees check products for quality at several points. When assembly is completed, the products are packaged, labeled, and moved to a loading area for immediate shipment to customers.

**Organizing the Work Area**

The type of product and production process will determine how the work area is organized. Mass production requires a large building. There must be space for the assembly line, equipment, tools, employee workstations, and storage for parts needed for assembly and finished products. If the company

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**Net Bookmark**

A number of data collection and reporting tools are used to study quality issues and make quality improvements in business. Access businessxtra.swlearning.com and click on the link for Chapter 13. The web site provides examples of seven quality tools. Click on each example for a description and example of how the tool is used.

businessxtra.swlearning.com
completes customized production of small products, such as eyeglasses or gift boxes, there will often be a larger workspace for each employee. They will have easy access to the variety of parts and materials needed for each product assembly. Often, as production of each customized product is planned, one employee will be assigned to collect the materials needed for an order. With a copy of the order in hand, the employee will wheel a cart through the room that stores the parts and quickly select those needed. Then the employee will move the cart to the work area of the other employees who will complete the product assembly.

Building or assembling a product at the customer’s location provides different challenges. Some examples are home construction, landscaping, and installing a telephone system in an office building. In these activities, employees, equipment, and supplies must be moved to the customer’s location. Transportation, storage, and security become major issues. Managers at the construction site must be able to communicate with inventory managers and people responsible for transporting the supplies and materials needed. Often companies have an overall project manager who works in the company’s office and visits the work site from time to time. Other managers are located at the various work sites. They supervise the construction and are in regular communication with the project manager.

**Improving Manufacturing**

Manufacturers face many challenges today as they cope with rising costs, greater competition in the global marketplace, and growing customer demands. The challenges include the need for faster production, increased quality, and reduced costs. Companies are responding to the challenges with improved manufacturing procedures and attention to quality.

Manufacturing is made up of a series of processes. One process follows another until production is complete. In the past, if there was a problem within a process, managers and employees would try to identify the problem and then attempt to correct it. That was a very slow process. It affected all of the processes that followed. Improvements were not made until problems were discovered.

Manufacturers have now adopted Continuous Process Improvement, detailed in Figure 13-1, as a way to make sure manufacturing processes are completed as effectively as possible. Continuous Process Improvement (CPI) increases the quality of work by reducing errors, inefficiencies, and waste. Rather than waiting for a problem to occur, processes are continuously reviewed with the goal of finding ways to improve them.

**Figure 13-1**

Would Continuous Process Improvement affect the prices that consumers pay for products?

<table>
<thead>
<tr>
<th>Continuous Process Improvement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Step 1 <strong>Involve</strong> everyone.</td>
</tr>
<tr>
<td>Step 2 <strong>Identify</strong> process activities.</td>
</tr>
<tr>
<td>Step 3 <strong>Establish</strong> quality performance standards.</td>
</tr>
<tr>
<td>Step 4 <strong>Select</strong> measurement tools.</td>
</tr>
<tr>
<td>Step 5 <strong>Monitor</strong> performance continuously.</td>
</tr>
<tr>
<td>Step 6 <strong>Improve</strong> process quality.</td>
</tr>
</tbody>
</table>
CPI is designed to help an organization achieve its goals by improving the quality of work. CPI should involve everyone linked to work processes. That includes employees, managers, other businesses involved in the process, and customers. It begins by listing all of the activities involved in the process. Standards for quality performance are developed. Often the standards are based on benchmarks, or the best practices among all competitors. Measurement tools are chosen and measurements are taken to determine if activities are meeting the standards that have been set. Based on those results, the people involved look for ways to improve activities to meet and exceed the standards. They also consider ways to improve the overall process by changes in activities, equipment, and resources.

13-2

Assessment

Key Concepts

Determine the best answer.

1. True or False. Once a company has developed successful products, it should be able to continue to sell them year after year.
2. True or False. Pure research is done without a specific product in mind.
3. Inventory managers keep records of
   a. personnel
   b. customers
   c. production resources and finished products
   d. All of the answers are correct.
4. The best practices among all competitors are
   a. standards
   b. benchmarks
   c. CPI
   d. quality measures

Make Academic Connections

5. Art Choose a small household product that you or your family use regularly. Evaluate the product and determine a design improvement for the product. Sketch a new design that illustrates the improvement. Show your sketch to other students and explain the product design.
6. Math A company keeps track of the number of defective products as part of its CPI program. For three months, the number of products and defects were
   January: 3,358 products, 31 defects
   February: 4,210 products, 38 defects
   March: 3,895 products, 28 defects
   a. Calculate the percent of defects for each month.
   b. Calculate the average production and defect rates for all three months.
   c. Create a graph or chart that illustrates the three months of data.
THE IMPORTANCE OF BUSINESS OPERATIONS

The day-to-day operations of a business often determine its success or failure. The company may have products that meet customer needs. They may have competitive prices. Still, several things can go wrong in daily operations that result in problems. Work procedures may not be efficient. Security issues may result in product thefts or damage to buildings and equipment. Lack of maintenance can lead to costly repairs or safety hazards for employees and customers. A poor work environment can result in dissatisfied employees who are less productive than they could otherwise be. Businesspeople need to plan business operations as carefully as they work to satisfy their customers or plan for new products.

Focus on Real Life

You put a CD in your computer and receive an error message. You purchase a memory card to use in your digital camera, but when you try to install it, the camera won’t format the card. A digital cassette isn’t compatible with the new digital video recorder you purchased. What’s going on? Why can’t manufacturers get together and agree on standard designs, sizes, and formats for their products?

Product incompatibility has been frustrating consumers and businesses for years. The International Organization for Standardization (ISO) was formed to address the need for standardization. ISO is a network of the national standards institutes from 146 countries. They develop consensus agreements among suppliers, users, government regulators, and consumers. They agree on specifications and criteria to be applied to the manufacture of products and the provision of services. As more agreements are reached and standards are issued by the ISO, there will be more cooperation and consistency among businesses and less frustration for consumers.

Key Terms

- logistics
- just-in-time
- operational plan
- schedule
- standard

Goals

- Discuss the importance of effective business operations.
- Describe tools used to manage business operations.

What are some jobs where safety is a concern?

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Types of Business Operations

Some business operations are specific to the type of business. The production activities of a manufacturer are different from the merchandise display and promotion activities of a retailer. They are different from the patient care activities of a hospital. Even among those very different types of businesses, there are some common types of business operations. They are facilities management, logistics, scheduling, and safety and security.

Facilities Management

Buildings are one of the largest investments of a business. Buildings house the work and workers. They provide space for all of the business operations as well as storage of materials, supplies, and products. Facilities management protects the company’s investment of thousands or even millions of dollars.

Facilities management begins with making economic decisions about the buildings needed. Some companies buy existing facilities. Others build new buildings to house their operations. It may be more cost-effective to rent some or all of the facilities needed. Facilities managers continually study the long-term plans of the company. They must determine if the current buildings are adequate, if more space is needed, or if some facilities are no longer needed or are out-of-date. It may be necessary to buy additional buildings or expand existing facilities. The expansion may require that expensive land be purchased. Some companies purchase land many years in advance at a cheaper price in anticipation of expansion.

Building maintenance and repair is another vital task of facilities management. A regular cleaning schedule is developed. From time to time, walls must be painted, carpets cleaned or replaced, and equipment updated. Exterior maintenance, including landscaping, is another ongoing task. A business must maintain a professional appearance for visitors and employees. It must also make repairs to facilities and equipment immediately so they don’t affect operations. Failure to maintain and repair buildings and equipment on a regular basis will result in higher costs in the future.

Another key area of facilities management is energy and environmental management. Energy costs are a rapidly growing expense. Companies need a ready supply of electricity, gasoline, heating oil, and water. Yet they also need to keep utilities costs under control. Facilities managers study ways to conserve energy resources. They also monitor the quality of air, building temperature, and other environmental factors to maintain a healthy and productive workforce.
Logistics  Large quantities of products and materials move in, around, and out of a business on a daily basis. Logistics is managing the acquisition, movement, and storage of supplies, materials, and finished products in a business. Logistics has become a very important part of business operations. A newer term for logistics is supply chain management. A supply chain is all of the businesses involved from the time raw materials are obtained until finished products are sold.

The major activities that make up logistics are locating sources of supplies, purchasing, transportation, and sales. In addition to the physical movement of resources, logistics is responsible for effective communications and information among everyone in the supply chain. One important logistics process is just-in-time. Using just-in-time, goods arrive when needed (just in time) for production, use, or sale rather than sitting in storage. Just-in-time logistics requires careful planning and coordination among supply chain members. It also requires an effective information system.

Scheduling  Even in small businesses, many activities occur at the same time. Scheduling involves determining the activities that need to be completed, the people who will complete the work, and the resources needed for the task. Consider a factory that produces a number of products to fill hundreds of customer orders. The factory must maintain the right inventory of products to fill each order. If customers have to wait too long, they may cancel their order. If too much time is spent producing one type of product, supplies of others may run low. If raw materials needed to produce a particular product arrive late, production of that product must be halted. Retail and service businesses find the same types of scheduling problems as they make sure they can match their resources with customer demand.

An important part of logistics planning is employee scheduling. Companies have a workforce made up of full-time, part-time, and temporary employees. The company assigns each employee to a work area. Each employee has a specific set of skills to meet job requirements. The company depends on having the right number of people available at any time to complete the scheduled work. The human resources department is responsible for making sure enough employees are available with the skills needed. They balance the workforce by determining the number of full-time, part-time, or temporary employees needed. They may need to hire more employees at certain times or reduce the number of employees at other times. A key human resource activity is training. Training ensures employees have the skills needed for their job assignments.
Managers, supervisors, and team leaders are responsible for the weekly and daily work schedules. They determine the work that is required. They also prepare the work schedule. If a heavier than usual workload is expected, employees may be scheduled to work more hours. The schedule must anticipate employee vacations and the possibility that employees will be absent or leave the company. Most managers have a specific wage and salary budget they are expected to meet. They must schedule carefully so as not to exceed the budget but still get the work finished.

**Safety and Security**

Companies are responsible for protecting people and property. Many events and circumstances can result in injury to people or damage to property. Companies devote a great deal of effort to providing security and safety.

Security procedures and personnel protect both people and property. Damage and injury can occur because of crime, unintentional actions, or natural causes, such as storms and earthquakes. Security personnel study the resources and activities of a business to identify potential security problems. They then prepare security plans and procedures to prevent problems whenever possible. The plans also minimize the amount of loss if a security problem occurs.

Safety is another main business concern. The business wants to prevent accidents and injuries to employees and customers. Businesses work to maintain safe work areas and work procedures. They provide safety training and enforce rules and regulations designed to reduce accidents. Many businesses place safety posters around the workplace. They recognize work units that have a record of no accidents or injuries for a period of time.

**Information Management**

Effective business operations require the coordination of many activities, resources, and people throughout the business. It usually involves the activities of other businesses. For a growing number of businesses, operations in many locations and even in several countries need to be coordinated.

*Information management* uses technology to access and exchange information to complete the work of an organization.

---

**FYI**

The National Retail Security Survey reports that retailers lose over $30 billion of their inventories each year. The sources and proportion of those losses are:

- **Employee theft:** 46.0%
- **Shoplifting:** 30.6%
- **Administrative errors:** 17.6%
- **Vendor fraud:** 5.8%

What can retailers do to recover losses suffered from shoplifting?
Information management has four goals.

1. To collect, organize, and securely maintain all needed information.

2. To provide instantaneous access to information required to perform work and make decisions.

3. To prevent access to information by those unauthorized to use it.

4. To use technology to improve communication and information sharing.

There are many types of information used in businesses. They include text, data, graphics, pictures, and video. Businesses exchange information in a number of ways. Oral communications include telephone, voice mail, face-to-face meetings, and now voice-over-Internet. Written communications take the form of letters, memos, reports, e-mail messages, brochures, manuals, and many others.

Information managers are responsible for designing, purchasing, installing, and maintaining the many types of technology used in the business. They must develop procedures for collecting, storing, and using information. They make sure the information is accessible yet secure. They provide training to all employees on the use of technology as well as on effective communications skills.

The Internet has become a vital resource for information management. The Internet provides a method for worldwide and continuous access to a company’s information by employees, customers, business partners, and even competitors. Virtual communication using the Internet replaces face-to-face meetings. It saves time and reduces travel budgets. Yet the Internet also presents a number of security challenges for information managers. Those challenges include viruses, attacks by hackers on the business web site and computers, and equipment and software failures. Advances in technology and an understanding of how the Internet can be used encourage businesses to rely on it more often for effective communications and information sharing.

Can you think of other ways that technology has made communication easier?
TOOLS FOR BUSINESS OPERATIONS

Several tools help people manage the day-to-day operations of a business. They include management tools and technology tools.

Management Tools

Operations activities require careful management. This means the activities must be planned, put into practice, and controlled. Operational activities are planned to help a business achieve its goals. Operational plans are developed in each area of a business to identify the activities that will be needed. An operational plan identifies how work will be done, who will do it, and what resources will be needed. An operational plan for the production area of a factory determines when each product will be produced. It assigns production activities and determines the number of employees needed.

It also schedules adequate supplies of resources. In a marketing department, the operational plan will match salespeople to customer groups, outline the promotional plan, and schedule sales promotion activities. The operational plan for marketing must be coordinated with the factory plan. The plans must ensure that enough products will be on hand to fill all customer orders.

Several management tools support the operational plan. An operating budget is a detailed financial plan for a specific area of the business. An operating budget is prepared for the production unit, the marketing department, and every other area of the business. The budgets help managers determine the amount of money needed for planned operations as well as how and when the money will be spent. The budgets will anticipate all types of operating expenses and areas of income, if any, for the specific area of the business.

A schedule is a time plan for completing activities. Schedules match people with resources to make sure activities are finished on time. A supervisor develops a weekly work schedule for employees. An inventory manager prepares a schedule of suppliers' deliveries of raw materials. An advertising manager makes up a schedule that coordinates television and newspaper advertising.
A procedure is a list of steps to be followed for performing a particular work activity. To maintain the quality of an activity and make sure it is completed as quickly as possible, a company may set up operating procedures. Employees are trained to follow those procedures. Following procedures and schedules helps employees coordinate their work with others.

A standard is a specific measurement against which an activity or result is judged. Businesses set standards for key activities to make sure an appropriate level of quality is maintained. The standard may state the number of products that should be finished on an assembly line. It may set the number of customers that should be served in a fast-food restaurant in a stated time period. It may also establish an acceptable number of product defects or customer complaints for those operations. Standards must be clear and realistic. By establishing standards and using them to measure performance, the quality of operations should remain high.

Using Technology to Manage Operations
Businesses can plan and manage most operations activities using computer software. Using technology to help manage operations will make planning and decision-making more accurate, rapid, and timely. It also makes it easier to access and exchange information. The exchange may occur within a company, with other business partners, or with customers. Some of the most important software used in businesses to manage operations is described in Figure 13-2.

What are the advantages of using software designed for a specific purpose?

**Common Types of Operations Software**

<p>| | |</p>
<table>
<thead>
<tr>
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</thead>
<tbody>
<tr>
<td><strong>Project Management</strong></td>
<td>Keeps track of project calendars, tasks, to-do lists, work assignments, and project resources.</td>
</tr>
<tr>
<td><strong>Budgeting</strong></td>
<td>Automates budget planning, compares budgets from one time period to another, and coordinates budgets among departments.</td>
</tr>
<tr>
<td><strong>Scheduling</strong></td>
<td>Manages employee facility, resource, and production scheduling. Allows easy review of schedules by all participants as well as quick updating.</td>
</tr>
<tr>
<td><strong>Inventory</strong></td>
<td>Helps the management of sales, purchases, and payments; tracks production, usage, and sales levels; and even prints bar codes.</td>
</tr>
<tr>
<td><strong>Computer Security</strong></td>
<td>Provides access and restrictions, usage data, privacy, and virus protection for computers and networks.</td>
</tr>
<tr>
<td><strong>Document Management</strong></td>
<td>Controls the production, storage, management, and distribution of electronic documents.</td>
</tr>
<tr>
<td><strong>Manufacturing Automation</strong></td>
<td>Monitors and often controls manufacturing machines, checks for errors and defects, and reports on production levels.</td>
</tr>
</tbody>
</table>
New types of software are now available to assist with supply chain management and support virtual collaboration of team members using their computers. Supply chain management software allows cooperating companies to share ordering, production, and shipping information, track products, and exchange customer data. Collaboration software (also called groupware) provides real-time communications capabilities by voice, text, and video. It also allows team members working at their own computers from anywhere in the world to view the same documents on their computer screens and work on them as a team.

**Assessment**

**Key Concepts**

Determine the best answer.

1. Which of the following is a part of facilities management?
   a. personnel scheduling
   b. logistics
   c. energy and environmental management
   d. information management

2. A(n) __?__ is a time plan for completing activities.
   a. budget
   b. schedule
   c. operating plan
   d. standard

3. True or False. Document management software keeps track of project calendars, tasks, to-do lists, work assignments, and project resources.

**Make Academic Connections**

4. **Math** Using the information from the FYI feature, if the total U.S. retail sales losses for last year were $32.6 billion, what would be the amount of each type of loss listed in the feature? If one retailer had total sales for the year of $128.6 million and losses were 7 percent of sales, calculate the total value of the business’ loss. Use the percentages from the feature to calculate the amount for each type of loss for the business.

5. **Communications** A small business owner is beginning to use the Internet to communicate with customers and suppliers. The company will soon have a web site with purchasing capabilities. Write a memo to the owner that discusses security issues that the business may encounter. Make three recommendations of ways to protect the business and customers.
Designs That Make a Difference

When the hostilities in Kosovo ended in 1999, nearly three-quarters of a million refugees came back from nearby countries where they had fled for safety. They found their homes destroyed. They had no place to live. They needed some form of shelter and protection while they rebuilt their houses.

HIV/AIDS spread quickly through the continent of Africa during the 1990s. There were few local medical facilities. Without local health centers, it would be almost impossible for health workers to treat the disease and educate people about risks and prevention.

In 2003, an earthquake hit southern Iran, killing thousands. It left cities in rubble and most of the people homeless. There seemed to be no solutions to rebuild homes rapidly and inexpensively or to provide needed services.

Architecture for Humanity took on each of those challenges by using the professional skills of the organization’s members. It sponsored an open competition to design five-year transitional housing for the returning Kosovars. More than 200 architects and designers from 30 countries submitted plans. Since the earthquake in Iran, Architecture for Humanity has been working with Relief International to raise funds and help with the design and construction of two clinics, a school, and water supplies. They will continue their efforts by providing expertise and assistance as people rebuild their homes. To meet the HIV/AIDS crisis in Africa, the organization challenged architects and health care professionals to submit designs for a mobile HIV/AIDS health clinic. Designers were given six months to develop plans that would be easy to deploy and maintain, be accepted by the communities in which they would be located, and not be expensive to build and operate. From the top designs, a prototype is being developed and labs will soon be built.

Architecture for Humanity was the brainchild of Cameron Sinclair, who was trained as an architect at the Bartlett School of Architecture in London. He has a long-term interest in building designs that meet social, cultural, and humanitarian goals. His postgraduate research focused on providing shelter to homeless people on the streets of New York. In 1999, he formed a nonprofit organization to encourage architects and designers from around the world to contribute their expertise to help communities in need. The organization sponsors competitions and educational programs. It solicits architects to donate time and effort to improve lives. Recently, the editor of the Architectural Record wrote, “Architecture for Humanity represents the finest of the new breed of architectural leadership, employing architectural skills and directing them for the larger good. Architecture for Humanity stands up for people in need.”

Think Critically
1. Use the Internet to locate additional information about Architecture for Humanity and to view examples of its designs and projects.
2. Suggest other professions that could contribute to solving social and humanitarian problems and the types of skills and expertise each profession could contribute.
13-1 Types of Production
1. Producers are businesses that develop products to be sold to other businesses or consumers. Consumers need products and services to satisfy their needs and wants. Businesses also need products and services to be incorporated into the products they produce, to be used in operations, and for resale to their customers. The three forms of production are extraction and cultivation, processing, and manufacturing.

2. Manufacturing businesses can organize production in several ways to produce products. The types of manufacturing procedures are mass production, custom manufacturing, and materials processing.

13-2 Production Planning
3. Production and manufacturing processes are very complex. They need to be carefully planned and coordinated. Product planning involves two steps—new product research and product design. Production planning includes three activities: a production process is developed, production resources obtained, and production personnel identified and prepared. Inventory management maintains the supply of all of the resources needed for production and the products produced.

4. The type of product and production process will determine how the work area is organized. Manufacturers face many challenges including the need for faster production, increased quality, and reduced costs.

13-3 Planning and Managing Business Operations
5. The day-to-day operations of a business often determine its success or failure. Businesspeople need to plan business operations as carefully as they work to satisfy their customers or plan for new products. Common types of business operations are facilities management, logistics, scheduling, and safety and security.

6. Several tools help people manage the day-to-day operations of a business. They include management tools and technology tools.

> > Communicate Business Concepts

1. Provide two examples for each of the three categories of products. For each example, identify one consumer use and one business use of the product.

2. What are the major differences between a processing business and a manufacturing business? What, if any, are the similarities between the two types of producers?

3. Why are several manufacturers usually a part of the total activity to produce a product? Why do you believe most manufacturers do not want to or are unable to complete the entire manufacturing process for a product? (Use an automobile as an example to explain your answer.)

4. How do scientists approach pure research differently than applied research? Why would a company choose to use one type of research rather than the other?

5. Identify three new products that appear to have been developed using applied research. Then identify three products that appear to have been developed using pure research. What differences, if any, do you see in the types of products that result from each type of research?

6. What are the advantages for a company and for employees in using an employee team to assemble a product rather than the traditional assembly line where each employee completes a specific task?
7. Why should business partners and customers be involved in a continuous improvement process? What can they offer that managers and employees cannot?

8. For each of the following types of businesses, identify a business operation that would be unique to that business and not to the others:
   a. Hospital
   b. Law firm
   c. Dairy farm
   d. Internet service provider
   e. Taxi service

> > Develop Your Business Language

Match the terms listed with the definitions.

11. The best practices among all competitors.

12. Managing the acquisition, movement, and storage of supplies, materials, and finished products in a business.

13. Changes the form of raw materials so they can be consumed or used to manufacture other products.

14. Studies existing products to develop design improvements or new product uses.

15. Products are obtained from nature or grown using natural resources.

16. Combines raw materials and processed goods into finished products.

17. Increases the quality of work by reducing errors, inefficiencies, and waste.

18. An assembly process that produces a large number of identical products using a continuous, efficient procedure.

19. A specific measurement against which an activity or result is judged.

20. Identifies how work will be done, who will do it, and what resources will be needed.

21. Goods arrive when needed for production, use, or sale rather than sitting in storage.

22. Changing and improving the form of another product.

23. Building a specific and unique product to meet the needs of one customer.

24. The activities, equipment, and resources needed to manufacture a product.

25. Time plans for completing activities.

26. Done without a specific product in mind with the goal of discovering new solutions to problems.

Key Terms

a. applied research
b. benchmarks
c. Continuous Process Improvement (CPI)
d. custom manufacturing
e. extraction and cultivation
f. just-in-time
g. logistics
h. manufacturing
i. mass production
j. materials processing
k. operational plan
l. processing
m. production process
n. pure research
o. schedule
p. standard
Decision-Making Strategies

Eric Elongue has worked in construction his entire life. He worked part-time with a small contractor while completing his bachelor’s degree in Construction Management at Eastern State University. Since then, he has been employed full-time for the past 15 years in increasingly responsible positions with a national homebuilder. He now wants to start his own home construction business. He is deciding between two options for his business.

**OPTION A:** Use a mass production process in which he builds four models of homes. Customers can choose one of the four models, but cannot customize them. With this business model, Eric can build 20 homes a year. His work crews will not need to be as skilled. Materials and operating costs will be 10 percent lower than the industry average.

**OPTION B:** Build custom houses in which each home is specifically designed for the homebuyer. Eric’s company will only be able to build 12 custom homes a year. It will require workers with much higher construction skills, and his costs will be 15 percent higher than the industry average. If he is able to maintain quality, he will be able to command premium prices for the custom homes.

27. What are the advantages and disadvantages of each option from the viewpoint of (a) managing business operations and (b) controlling quality and costs?

28. What option would you recommend to Eric? Why?

Make Academic Connections

29. **SCIENCE** Identify several natural resources that are extracted and processed in your state. Using the Internet, print a map of your state. Mark and label the primary sources of those resources on the state map. List one company that is involved in the extraction or processing of each of the natural resources.

30. **ECONOMIC GEOGRAPHY** Some manufacturers locate their businesses very close to the sources of supply for the materials they need for production. Others locate closer to their main customers. Identify three manufacturers that fit each of those categories. Based on the types of products produced by the companies in each category, suggest reasons for the location decisions.

31. **TECHNOLOGY** Select one type of operations software listed in Figure 13-2 on page 335. Use the Internet to locate two companies that offer the type of software you chose. Study the product information from each company. Develop a table that compares the two software packages.

32. **HISTORY** Research the history of manufacturing in the United States from 1900 to the present. Prepare a visual timeline that identifies 15 events, products, and people that had a significant influence on manufacturing procedures during that time.

33. **RESEARCH** Pure and applied research is an ongoing activity of businesses, universities, and government agencies. Use the Internet to locate reports of current research that holds promise for new products. Based on your research, prepare an oral report that identifies the type of research being done, the organization(s) conducting the research, the amount of money that has been invested in the research, and the new product or product improvement that is being developed.

34. **MATH** In 2004, *Fortune* magazine identified the top five international manufacturers and processors. The companies and their 2003 sales and profits are as follows:

<table>
<thead>
<tr>
<th>Company</th>
<th>Total Sales (mil.)</th>
<th>Net Profit (mil.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>BP</td>
<td>$232,571</td>
<td>$10,267</td>
</tr>
<tr>
<td>Exxon Mobil</td>
<td>222,883</td>
<td>21,510</td>
</tr>
<tr>
<td>Royal Dutch/Shell</td>
<td>201,728</td>
<td>12,496</td>
</tr>
<tr>
<td>General Motors</td>
<td>195,324</td>
<td>3,822</td>
</tr>
<tr>
<td>Ford Motor</td>
<td>164,505</td>
<td>495</td>
</tr>
</tbody>
</table>

a. Determine the total sales and net profit earned by all five companies combined.
b. What percentage of each company’s sales is represented by its net profit?
> > Linking School and Home

Safety and security has become an important issue for families, communities, and businesses. Interview several family members and neighbors. Discuss their concerns about personal safety and security. Prepare a list of recommendations that could be followed in your home and neighborhood that address the safety and security concerns you heard. For each recommendation, identify who should be responsible for implementing the recommendation and the procedures that need to be followed.

> > Portfolio Activity

To provide tangible evidence of your learning about production and business operations, do the following:

**COLLECT** information on a product that is produced or manufactured in your community.

**CREATE** a visual that illustrates the steps in the production or manufacturing process. As a part of the visual, identify important resources and materials used and other companies involved in the process.

**CONNECT** your visual to other items already in your class portfolio or relate it to an important concept you learned in another class. Make the connection by preparing a one-minute presentation on the importance of production and manufacturing to local, state, and national economies.

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**Small Business Management Team Event**

The Small Business Management Team Event involves a 90-minute test and a 10-minute oral presentation followed by five minutes of questions from the judges. A team of two to four members must present a solution for a Management Case Study. Your team may use one laptop/notebook computer, posters, flip charts, or graphs for the presentation.

**CASE:** Productivity in the U.S. is at an all-time high. This increase in productivity has resulted in some individuals losing their jobs. Increased productivity has required workers to learn more about technology. Workers must be flexible and willing to complete continuing education to learn about the latest technology. More education will usually result in higher-paying jobs. During an election year, two topics that receive a great deal of attention include the impact of productivity on employment and outsourcing of jobs to other countries.

Your management team for a major automobile manufacturer must explain how manufacturing has changed and present a strategy to train employees for the latest production technology. Your presentation must give employees incentives to continue their education.

**Performance Indicators Evaluated**

- Organize ideas and communicate orally in a group presentation.
- Apply an understanding of managing production processes.

Your team will be evaluated for

- Delegation of responsibilities needed to perform required tasks
- Demonstration of teamwork skills needed to function in a business setting
- Demonstration of self-esteem, self- and team-management, and integrity
- Demonstration of a working knowledge of business management concepts
- Demonstration of critical thinking skills to make decisions and solve problems

For more detailed information about performance indicators, go to the BPA web site.

**Think Critically**

1. Why must management create strategies that encourage employee involvement?
2. What advantages exist for production workers who take classes to learn the latest production technology?
3. What are the downsides for employees that result from increased productivity?
Chapter 14
Risk Management

14-1 Overview of Risk Management
14-2 Insurable Risks
14-3 Uninsurable Risks
Consumers and businesses buy insurance for protection against risks. When people are injured, need health care, or suffer property damage, insurance companies pay for some or all of the costs. Insurance companies rely on actuaries to determine the premiums needed to cover the costs. An actuary determines the amount of risk insurance companies face and sets the rates charged. They evaluate investments to maximize the company’s return.

Although actuaries work in all parts of the economy, many work in financial services businesses. Corporations and state and federal governments also employ actuaries. Many work for consulting firms. Actuaries need to pass professional exams that give employers evidence of their professional knowledge and skill. Since 1988, the Jobs Rated Almanac has rated the job of actuary as the first or second best job in the United States.

Employment Outlook

- Actuarial positions are expected to grow 3 to 9 percent through 2010.
- Actuaries usually work in the insurance industry to develop, price, and evaluate products such as life, auto, health, or homeowners insurance.
- The fastest employment growth is expected in industries including finance, investments, software development, data processing services, health services, management, and consulting.
- Consulting jobs in the healthcare and retirement planning field are expected to grow faster than the average.

Job Titles

- Actuarial Assistant
- Actuarial Analyst
- Chief Actuary

Needed Skills

- A degree in mathematics, actuarial science, statistics, or computer science
- Courses in business, economics, and finance to understand business operations and costs
- Courses in English, speech, and business writing to develop communications skills

What’s it like to work as...

an Actuary

After Janine graduated from college, she obtained her first job working for a large insurance company as an actuarial assistant. During the first year, she worked on three projects. The projects involved evaluating the company’s expenses to process claims, reducing time to review and update rates for group medical insurance, and developing an online insurance rate calculator for customers.

The company encouraged its actuaries to prepare for and pass the series of professional exams. New employees met twice a month with experienced actuaries for study sessions. Janine completed the first of seven exams while in college and now had passed three more.

While her work is hectic, she enjoys the variety of the projects. “No day is like any other day,” Janine stated. “You have to like pressure and tight deadlines.” Eventually, she hopes to move into a management position and then maybe into consulting.

What about you? What do you think are the benefits to Janine for passing the professional exams? How does the company benefit?
IDENTIFYING RISKS

Every day you face risks. Risk can be thought of as the possibility of incurring a loss. You face many types of risks and possible losses. Some are very important to you and can have long-term effects. The risk of a serious illness or an accident that results in an injury would have a major impact on your life. A hurricane, tornado, or fire can leave homes, businesses, and even entire communities damaged or ruined.

Other risks are inconvenient but have little lasting effect. If you are caught in traffic, you risk being late for an appointment. When you buy a new product, you risk that it might go on sale in two weeks. Even if you are very careful, you cannot avoid all risks and losses. Still, individuals and businesses need to be aware of risks and try to reduce possible losses, especially for those risks that may result in physical or financial harm.

Focus on Real Life

As Jaimie walked away from the cell phone kiosk, he was facing two important decisions. He had found a cell phone with all of the features for which he was looking. It was a bit more expensive than he anticipated, but he did have enough money. The monthly plan was affordable with the services he wanted. The salesperson told Jamie he could save $100 on the price of the phone if he would sign a two-year contract with the wireless service provider. Yet if he cancelled the service during that time, he would have to pay the company $150. The service provider was a new company. Jamie wasn’t sure he would like it enough to commit to two years.

In addition, the salesperson offered Jamie a plan that would protect his phone from being lost or stolen for a cost of $4.95 a month. Jamie had never lost his phone but knew of several friends who had. He knew he could not afford to replace the phone. He realized the total cost of the protection for two years was almost $120. Should he choose the options or not? He would have to think about the costs versus the risks before making a final decision.

Focus on Real Life

Can you think of reasons for taking a warranty on a product you just purchased?
Types of Risks
There are many ways of viewing risks. Being able to identify the type of risk helps to determine how to plan for the risk. Planning for a risk may reduce the chance that it will occur or reduce its impact if it does occur.

**Economic and Non-Economic Risks** A risk that can result in financial loss is an economic risk. There are three categories of economic risks. A personal risk can result in personal losses such as health and personal well-being. A property risk can lead to loss of personal or business property including money, vehicles, and buildings. A liability risk relates to harm or injury to other people or their property because of your actions.

Non-economic risks may result in inconvenience or embarrassment but do not have a financial impact. A traffic accident is an economic risk. It can result in expenses such as medical care, automobile repairs, and higher insurance rates. Deciding with your friends to perform at the school talent show is a non-economic risk. You may be uncomfortable or embarrassed if the show does not go well, but you won’t suffer financially.

**Pure and Speculative Risks** A risk that presents the chance of loss but no opportunity for gain is a pure risk. Severe weather is an example of a pure risk. The storm may pass with no harm to a business. A heavy snowstorm that causes the business to close for a day or two will reduce sales. Wind and rain damage to a building will add to expenses because of the cost of repairs.

Speculative risks offer the chance either to gain or to lose. Suppose you invest your money in a new business. If it is successful, you will make a nice profit. On the other hand, if it fails you can lose all of the money you invested.

**Controllable and Uncontrollable Risks** A risk that you can reduce or eliminate by actions you take is a controllable risk. To prevent loss from theft, businesses install security systems, hire guards, and train employees to be alert for possible problems. Uncontrollable risks cannot be reduced by your actions. A sudden hailstorm or early freeze can affect a farmer’s crops and little can be done to reduce the losses suffered.

**Insurable and Uninsurable Risks** People look for ways to protect themselves from the negative effects of risks. A common form of protection is insurance. Insurance exchanges the uncertainty of a possible large financial loss for a certain smaller payment. If a large number of people face a given risk and the cost of possible losses can be predicted, it is an insurable risk. If a risk is not common or if it is impossible to predict the amount of loss that could be suffered, it is an uninsurable risk.
DEALING WITH RISKS

Suppose you and nine of your friends each have a new set of golf clubs. Each set is worth about $600. You all decide to form an organization called the Golf Club Owners Insurance Association (GCOIA) as shown in Figure 14-1. The purpose of the GCOIA is to reduce the risk of a large financial loss should one member’s clubs get stolen. To provide protection, each member agrees to share the cost of replacing any stolen clubs. Therefore, if your golf clubs were stolen, each member (including yourself) would contribute $60 to buy new clubs for you. If you are not a member of the GCOIA and your clubs are stolen, you would have to pay the total cost ($600) of new clubs. As a member, new clubs would only cost you $60. When a member loses golf clubs, each member suffers only a relatively small economic loss. In that way, the members help one another by sharing the risk of economic loss.

Everyone faces risks. Many of those risks will result in financial damage or possible disaster if the loss is severe. Individuals and businesses must determine how they will deal with the risks and possible losses they face. Figure 14-2 shows that there are four possible ways to deal with risks.

Avoid the Risk

With thought and planning, you might be able to avoid some risks. If you don’t believe you have enough experience or skill to start your own business, you can decide not to become an entrepreneur. If a snowstorm is in the forecast, you can choose not to take a planned trip to avoid a possible accident. If market research suggests there may not be enough demand for a new product to cover the costs, a business can choose not to make that product. In order to avoid risks, decision-makers need to be aware of risks that can threaten a decision. They must determine the costs and possible rewards of their decisions. They must estimate the size of losses if anticipated problems occur. If the likelihood of risk or the amount of loss is too great, they may make the decision to avoid the action. This ensures that there will be no loss.

FYI

The Insurance Services Office (ISO) defines catastrophes as events causing at least $25 million in insured property losses to a significant number of insurers and policyholders. A record eight catastrophes, including four hurricanes, hit the U.S. in the third quarter of 2004, resulting in total losses of $21.3 billion.
Transfer the Risk

Sometimes an activity must occur even though there is a risk that can have serious financial consequences. If a business is not in a position to assume the risk, it may choose to transfer it. When a business transfers a risk, someone else assumes the risk. A company may not be able to afford losses that it could suffer if the company offers customer credit and several credit customers do not pay their bills. In that situation, the company may transfer the risk of poor credit to a bank or credit card company. Those businesses already have a credit operation. They are able to manage credit customers more effectively. They are also in a position to handle larger credit losses. The bank or credit card company will be willing to accept the risk of credit sales with the likelihood that they can make a profit on the interest paid by the credit customers.

A company can transfer the risk of product damage by using other channel members to store and distribute products. A manufacturer can transfer the risk of a costly or unsuccessful research process by forming a joint venture with an experienced research firm. The cost of the research will be shared with the other company that already employs experienced researchers. If the research is successful, the manufacturer will produce and sell the product. It will then share the profits with the research partner.

Insure the Risk

If a business faces the same type of risk also faced by others and the size of losses can be reasonably predicted, it is possible to purchase insurance. In the case of the Golf Club Owners Insurance Association described earlier, each club owner insured the risk of stolen clubs by paying a small amount to the Association. In the same way, businesses that face the risk of fire damage to their buildings, equipment, and inventories can pool those risks with other businesses by purchasing fire insurance.

It is possible that a few businesses will have losses from fires during a specific period. Based on the history of fires in businesses, it is possible to reasonably estimate the total amount of fire damage among a number of businesses for that amount of time. Each business will pay a small amount for insurance that will cover the losses of the businesses that suffer a loss from fire.

Assume the Risk

Some companies decide that they are willing to assume certain risks. That means that if they suffer a loss, they will deal with the result. Typically, if a business decides to assume a risk, it means that the result of damage will not have serious negative consequences on the business. The company believes available funds can cover any financial loss.

A very large business may choose to set aside a small amount of money each month rather than purchasing insurance. They believe that if a financial loss occurs because of a risk, there will be enough money saved to cover the amount of the loss.

<table>
<thead>
<tr>
<th>Method</th>
<th>Activity</th>
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<tbody>
<tr>
<td>Avoid</td>
<td>Choose not to complete the risky activity</td>
</tr>
<tr>
<td>Transfer</td>
<td>Find another business to complete the activity</td>
</tr>
<tr>
<td>Insure</td>
<td>Purchase insurance to pay for any losses</td>
</tr>
<tr>
<td>Assume</td>
<td>Complete the activity with full responsibility</td>
</tr>
</tbody>
</table>
In other situations, it may not be possible to avoid, transfer, or insure a risk. If that is the case, the business will need to assume the risk. Once a business produces or purchases a product for resale, it must be able to sell the products at a reasonable price in order to cover its costs. If the sales goals are not met, the business suffers a loss. It assumes the risk of being able to sell its inventory at a profit.

Some risks are so unlikely that the company decides to do nothing. It assumes a problem will not occur. The company may be forced to take emergency actions if it is wrong. A company hires enough employees to operate the business. It knows a few extra employees are needed because at any time a certain number will be on vacation, on sick leave, or out for other reasons. If the company is suddenly hit with a major flu epidemic, there may not be enough employees available to run the business for a few days. Managers will have to decide whether to hire temporary employees, reduce some operations, or even close the business until employees recover.

14-1 Assessment

>> Key Concepts

Determine the best answer.

1. True or False. Every risk you face results in a loss.

2. Which of the following is not a type of economic risk?
   a. personal risk
   b. property risk
   c. liability risk
   d. All are economic risks.

3. Using another business to complete a risky activity is known as __?__ the risk.
   a. assuming
   b. avoiding
   c. transferring
   d. insuring

4. True or False. To be insurable, the same type of risk must be shared by a large number of businesses or individuals.

>> Make Academic Connections

5. Environment Storms, earthquakes, and other natural disasters are often very costly to individuals, businesses, and communities. Millions of dollars in damages are suffered. It takes months and even years to recover. Use the Internet to identify the most costly natural disasters that have occurred in recent years. Identify the type of disaster, the country or region affected, and the estimated financial costs of each. Prepare a table to report your findings.

6. Critical Thinking Think carefully about the types of risks you and other family members face as a part of your daily lives. Make a list of at least ten of those risks. Classify each risk as controllable or uncontrollable. Justify each of those decisions. For each of the controllable risks, describe actions you and your family members can take to reduce the risk or the possible damage that could occur.
The decisions people make about lifestyles are by far the most important factors influencing their health. The U.S. Centers for Disease Control and Prevention report that several key factors influence a person’s well being.

- Quality of medical care, 10%
- Heredity, 18%
- Living and working environment, 19%
- Lifestyle choices, 53%

People want to live long, healthy, and happy lives. Even so, the day-to-day choices you make can result in poor physical and emotional health, accidents, and relationship problems. Your lifestyle reflects your activities, values, beliefs, and behaviors. Choices you make not only add to your day-to-day achievements, but also to your long-term health and happiness. Making risky choices or failing to be concerned about your physical and emotional health can have negative consequences. These consequences may be hard to overcome or even life-threatening.

Positive lifestyle choices include nutrition, physical activity, medical care, emotional health, interpersonal relationships, and personal development. Making positive lifestyle choices is key to reducing personal risks.

Nutrition  Eat a balanced diet that includes a variety of foods. Select foods that promote energy and health. Don’t overeat or eat too little. Avoid regular snacking or foods and beverages filled with “empty” calories.

Physical Activity  Maintain an active schedule involving enjoyable physical activities. Take part in aerobic activities that exercise your heart, strengthen muscles, and build flexibility. Develop skills in physical activities you can enjoy all of your life.

Medical Care  Schedule regular visits with your family doctor, dentist, and eye-care specialist. Follow your doctor’s advice. Discuss any health issues or questions. Maintain required immunizations. Use only prescribed medications.

Emotional Health  Stay active mentally and emotionally. Develop friendships, but also take time for yourself. Take on creative activities. Don’t bottle up your emotions. Don’t be afraid to discuss your feelings or seek help from counselors and mentors.

Interpersonal Relationships  Spend time with family and friends. Avoid using negative communications that others can easily misinterpret. Be open to people with different backgrounds and experiences. Resolve conflicts before they affect long-term relationships.

Personal Development  Set personal, academic, and career goals. Make plans to achieve them. Think about the short- and long-term consequences of your decisions and actions. Avoid risky behaviors including smoking, alcohol use, and drug use. Drive safely and avoid distractions. Think before participating in activities that can lead to accidents or injuries to you or others.

Think Critically
1. How can decisions made today affect your lifestyle in the future?
2. What additional recommendations can you make for a healthy and happy lifestyle?
PURCHASING INSURANCE

Most individuals and businesses cannot pay for large economic losses. Instead, they share the risk with other individuals or businesses. They buy insurance to provide the financial protection they need in the event they suffer a financial loss. When people buy insurance, they have peace of mind knowing that even if they have an accident, injury, or other loss, they will be able to concentrate on recovery. They will not have to worry about how to pay for the costs of the loss.

Insurance Basics

Insurance companies provide planned protection against economic losses. The company, called an insurer, agrees to take on certain economic risks and to pay for losses if they occur. The person or business for which the insurer assumes the risk is the insured. To show that it has taken on the risk, the company issues a written contract, or insurance policy. The person or company buying the policy is the policyholder. An insurance policy states the conditions to which the insurance company and the policyholder have agreed. The amount the policyholder must pay for insurance coverage is a premium. The policyholder makes payments monthly, quarterly, every six months, or once a year. A claim is a policyholder’s request for payment for a loss that the insurance policy covers.

Insurance Companies

In addition to offering financial protection for policyholders, insurance companies are also investment companies. The premiums collected from the policyholders make up the funds from which the insurance company pays for claims. The company invests these premiums. The additional amount earned from these investments allows the company to make a profit and to cover the costs of claims.
You can get insurance protection in several ways. Individuals can buy insurance directly from an insurance company. Employers may provide insurance as a part of employee benefits. Professional organizations and other groups may offer insurance coverage to members. Businesses often offer insurance for customers to provide protection for related risks. When using credit, customers may want credit insurance. Shippers may offer transportation insurance. Security companies may provide theft insurance.

Most people purchase insurance from an insurance agent. An insurance agent represents the insurance company and sells insurance policies to individuals and businesses. A key part of an insurance agent’s job is to help each client choose the proper kind and amount of protection from possible economic losses. Based on the decisions, the agent submits information to the insurance company that will prepare the policy.

There are two basic types of insurance agents. One works for a large insurance company and sells only policies written by that company. The other is an independent agent who may sell many kinds of policies from a number of different companies. You can also purchase insurance directly from an insurance company or through an agent using the Internet.

Most people are concerned about the type and cost of insurance when choosing an insurance company. Any time you purchase insurance, the offerings of several companies should be compared for features and prices. Another key factor is the service provided by the company if a loss occurs. When a loss is suffered, policyholders want to be able to rely on the insurance company to act quickly in providing help. It should be easy to contact the company. Their response should be prompt. The process used to file a claim needs to be easy and understandable. Full reimbursement for losses covered by the policy should be processed as quickly as possible.

Work as a Group

Have group members locate the web sites of several insurance agents from your community. Identify the insurance company or companies that the agent represents and the types of insurance sold by each for consumers and for businesses. Compare the results of the searches.

What other types of insurance might an employer purchase on an employee’s behalf besides health insurance?
Insured Losses

Both consumers and businesses can buy insurance to cover almost any kind of economic loss. Violinists can insure their fingers. Professional athletes can insure against injuries. Writers may insure their manuscripts. Businesses can insure against the loss of rent from property damaged by fire, injury to consumers resulting from the use of the company’s product, or theft by employees.

The kinds of insurance protection that will be important to most consumers are vehicle, property, health, and life insurance. Businesses also insure their vehicles and property. They may provide health and life insurance for some or all employees. They also need liability insurance. Liability insurance protects against losses from injury to people or property resulting from the products, services, or actions of a business.

CHECKPOINT

What information should be considered when selecting an insurance company?

BUSINESS INSURANCE

A company uses its financial resources to invest in land, buildings, operating equipment, inventory, and people. If the business suffers a serious loss of any of those resources, the business may have trouble replacing the resources and continuing to operate. Businesses buy many types of insurance to obtain financial protection for their assets. Figure 14-3 illustrates the three major business insurance categories of personnel, property, and business operations.

Insuring Personnel

The health and well-being of managers and employees are important to a business. If workers are sick or injured, they will not be able to work. The costs of medical care are high. Costs will need to be paid by either the employee or the company. If an accident occurs on the job, the business will often be responsible for the cost of medical care and lost wages while the employee recovers. Businesses purchase or offer to employees several types of insurance to provide protection for the costs of those risks.

Figure 14-3

What risks might a business face if each of these components is not properly insured?
Health Insurance Many businesses offer health insurance, which provides protection against the high costs of individual health care. Health insurance covers routine costs of medical care. It may also cover costs of hospitalization or other needed medical treatments. Businesses often offer group health insurance. With group insurance, a large number of employees and their family members are covered under one policy. The policy covers many people, and premiums are paid for all members of the group. Therefore, the cost of insurance is lower than if each person bought a separate policy. Some companies pay for the entire cost of employee health insurance. Most only pay a percentage of the cost and employees pay the remainder of the premium.

Disability Insurance Another type of insurance that businesses may offer is disability insurance. Disability insurance provides payments to employees who are not able to work for an extended period due to serious illness or injury. The amount of payment is usually a percentage of the employee’s income. It is based on the number of years worked and the seriousness of the disability. A special type of disability insurance is known as workers’ compensation. Workers’ compensation is a system of insurance set up by state law that pays employees who are injured on the job. Each business makes payments to the insurance fund based on the number of employees.

Life Insurance Many businesses also offer life insurance, which pays the amount of the insurance policy upon the death of the insured. The payment is made to people named in the policy known as beneficiaries. Beneficiaries are usually family members of the insured. Partnerships often purchase a life insurance policy on each partner with the company named as beneficiary. This provides money that will be used to maintain the business operations that the deceased partner performed. Corporations often insure the lives of key executives because of their importance to the company’s success. Businesses may offer a small amount of life insurance for each employee or allow employees to purchase low-cost life insurance as a benefit.

Insuring Property Businesses buy various types of insurance policies to protect their property. They obtain protection for buildings, equipment, and building contents, including inventory, through commercial property insurance.

Commercial property insurance covers property losses resulting from fire, storms, accidents, theft, and vandalism. Special policies can also provide coverage for flood damage and earthquakes.

Vehicle insurance covers the automobiles, trucks, and other business vehicles. Damages to the vehicles and occupants resulting from accidents are covered. Vehicle insurance pays the costs of damage to the property of others. It also pays medical costs for those injured if people driving the company’s vehicles cause an accident.
Insuring Business Operations

Employees’ actions or business operations may result in accidents, injuries, property damage, or other losses. The business can purchase various types of insurance to protect against those losses. *Business interruption insurance* provides compensation for ongoing business expenses that occur if a business has a temporary shutdown due to a fire, flood, or other major problem.

Liability insurance provides coverage for claims by others based on damages suffered because of business operations, employees, or products. A customer may be injured while visiting the business. The use of a product may result in physical injury, illness, or even death. An employee may be dishonest or take action that injures another person. The business may be held financially liable for any of those situations.

Can you think of several types of insurance that a business owner might make a claim against in order to recoup damages from a fire?

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**CHECKPOINT**

What are the three major areas that can be covered by business insurance?

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**14-2 Assessment**

**Key Concepts**

Determine the best answer.

1. The reason businesses and individuals purchase insurance is to
   a. make a profit
   b. provide financial protection
   c. reduce taxes
   d. increase sales

2. True or False. Another term for an insurance company is the policyholder.

3. True or False. An insurance agent can work for only one company or may represent several insurance companies.

4. Insurance that provides coverage for claims by others based on damages suffered as a result of business operations, employees, or products is
   a. health insurance  
   b. property insurance
   c. vehicle insurance
   d. liability insurance

**Make Academic Connections**

5. **Debate** The high cost of liability insurance is a controversial topic. Form two teams to study and debate the following issue: “The maximum amount of damages that a company should have to pay to one individual for any liability claim should be $1 million.”

6. **Math** A new employee had an individual health insurance policy that costs $180 per month plus $125 per month for his spouse and two children. The company offers a group policy that costs $165 a month for an individual or $286.50 for the entire family. The company contributes 10 percent of the cost of the individual policy toward either choice.
   a. How much does the group policy reduce the cost of health insurance for the entire family without the company’s contribution?
   b. What will be the amount the employee will pay for family health insurance for an entire year? What is the annual savings compared to the previous policy?
Uninsurable Risks

**Goals**
- Describe why some business risks are uninsurable.
- List the strategies a company can use to reduce the risks of doing business internationally.

**Key Terms**
- property rights
- counterfeiting

**Focus on Real Life**
Microsoft has a greater share of the software market in China than it does in the United States. Surprisingly, it is not happy with that statistic. The reason is that most of the company's software has been pirated. That means Chinese companies have stolen it and then sold it to Chinese consumers.

The problem is not exclusive to Microsoft. It is estimated that 92 percent of business software and 96 percent of entertainment software used in China has been pirated. The result is the companies that developed the software receive no money for their products. Honest consumers pay higher prices since the companies miss out on millions of dollars of sales from the Chinese market. Microsoft is responding by filing lawsuits against the companies that steal and resell their software. They are also working to establish business operations in China including a large research center, production facilities, and sales. They hope their presence in the country will reduce the amount of illegal activity.

**Identifying and Reducing Risks**
Businesses cannot insure many of the risks they face. Some are too expensive to insure. If the chance that a risk will occur cannot be reasonably predicted or the possible financial loss to the business cannot be calculated, it is not likely that an insurance company will provide coverage. The costs of some risks, such as medical malpractice or product liability, are so high that a business cannot afford the cost of insurance protection. In that case, the business must determine other ways to deal with those risks.

**Types of Uninsurable Risks**
Several circumstances can lead to business risks that can be very costly to a company. Those circumstances are economic conditions, consumer demand, competitors’ actions, technology changes, local factors, and business operations.

What are the economic results of pirating entertainment software?

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Economic Conditions  When the economy is strong, consumers and business customers are more willing to spend money. Sales will be strong and profits high. A downturn in the economy can quickly reduce sales and profits. If the company does not cut production and expenses, it can experience real problems. Managers need to study the economy carefully. They must be prepared to respond to improvements or declines in economic conditions.

Consumer Demand  Companies produce products that they think will meet consumer demand. They study customer needs and preferences. If they can predict a change in demand, they may be able to take advantage of the need with new products. If consumer tastes change, the company may end up with products in inventory that they are unable to sell at a profit.

Competitors’ Actions  Businesses function in a competitive environment. The actions of competitors can affect the success of a business. If a competitor starts a major advertising campaign or decides to reduce prices, a business will have to decide whether it needs to respond or not. The wrong decision can result in lost sales and profits or additional unneeded expenses. A new competitor may enter the market or a current competitor may introduce a new product. If a company is not prepared for those types of competitive actions, its share of the market can quickly decline.

Technology Changes  What happened to traditional businesses when other companies started to use the Internet? If a company is not prepared to accept debit cards as a form of payment, will customers take their business elsewhere? When consumers can download music and movies from web sites, will brick and mortar music and video stores be affected? Anytime technology changes, there is a possible effect on a business. The cost of putting new technology in place is usually high, but if the business doesn’t adopt the technology, it may lose sales.

Local Factors  The highway that runs in front of a fast-food business closes for a month for repair. The utility company serving the city has a

Insurance companies offer educational services by preparing brochures and videos, conducting training sessions in business, and providing public service announcements on safety, health, and accident prevention. They conduct these activities to help reduce risks and lower the cost of insurance.
5 percent rate increase for the cost of electricity. The county zoning board rejects a business’ request to expand its production facilities. The laws, regulations, taxes, and infrastructure of a local community can have an influence on the operations of a business. Some businesses decide to move from one community to another to get conditions that are more favorable. Businesses work with government officials and community organizations to keep a positive environment for business.

**Business Operations** The day-to-day operations of a business can have a major impact on its success or failure. A poorly run business will have higher costs, low morale, increased turnover, and a poor customer image. A lack of employee training and poor management can lead to production errors, safety problems that result in accidents and injuries, poorly maintained equipment and facilities, and labor relations problems. If managers and employees are not committed to the success of the company, they will miss opportunities to improve operations, increase customer satisfaction, and control expenses.

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**E-Commerce in Action**

**Online Insurance**

Purchasing insurance to protect against the many risks an individual, family, or business might face is a difficult and time-consuming task. Insurance companies must be identified and insurance agents contacted. Detailed information will need to be collected and provided in order for the agent to determine appropriate coverage and premium costs as well as to prepare each insurance policy. Finally, the purchaser will need to compare coverages, prices, and reputations of the insurance companies to make the best possible selection.

Internet resources can make the sometimes unpleasant task of obtaining insurance more pleasant and less intimidating. Most large insurance companies have their own web sites that offer product information. Consumer organizations and government web sites provide information and advice on making good decisions. Most sites offer guidance to understand insurance policies before you choose one. Tips are also available on how to handle major life changes, such as buying a home, becoming a parent, or getting married. You can even create an online insurance portfolio to hold your quotes and policies. Together, the insurance web sites can offer everything you need to prepare for a visit to an insurance agent or even to purchase a policy over the Internet.

A number of factors can affect the insurance premium you pay. Many insurance companies’ web sites allow you to use different scenarios in calculating insurance premiums. Some provide an online survey for you to complete in order to obtain a rate quote. As you complete the survey, variables can be changed so you can find ways to reduce rates. For instance, before buying a car, you can put in various models to determine the insurance rate for each model.

Selling insurance online has resulted in both benefits and drawbacks. Consumers can more easily compare insurance coverage and rates. On the other hand, potential policyholders must be wary of paying too much for insurance or buying unneeded coverage. Many customers may believe they received a great rate on a policy only to learn too late that the policy doesn’t cover a specific risk or the company provides very poor customer service when a claim is filed.

**Think Critically**

1. Conduct an Internet search to identify the web sites of an insurance company, a consumer organization, and a government agency that provide helpful information for buying insurance.

2. Use the identified web sites to obtain suggestions for lowering the cost of auto, home, or life insurance. Prepare a poster or other visual presentation with a summary of your findings.
Managing Risks

Each of the situations just described poses a risk to businesses. Alone, any of the risks can cause serious financial problems. If several occur at the same time, it is not likely the business will survive. Uninsurable risks present important challenges to managers and employees.

Everyone in a business needs to be aware that there are many uninsurable risks. The business must inform them of the types of risks that are particularly important to their part of the operations. All employees must be watchful for changes that can lead to problems.

Businesses need to implement measures to gather information and spot possible problems. They should continually study all of the risk areas. Managers need to be aware of changes in the economy, competitors’ actions, and technology. The business should collect and review customer information, including complaints and requests. It should carefully watch sales to identify which product sales are increasing and which are decreasing. It should monitor all operating costs to make sure they do not get out of control.

Businesses should inspect facilities and equipment to make sure they are running properly and safely. Careful employee hiring and ongoing training will also add to effective and safe operations. Businesses should put security measures in place to prevent theft and vandalism and to protect employees and customers. Important information and company records should be protected from all forms of possible damage. Backup copies should be prepared and stored in safe locations.

Businesses should be active in their local communities. They should work to develop and maintain a positive image. They should build relationships with local, state, and national government officials. Businesses must be aware of any proposed changes in laws and regulations that could affect operations. Careful study and planning followed by positive actions will have the greatest effect on reducing business risks.

What security measures are put in place by department stores to deter theft?
RISKS IN INTERNATIONAL BUSINESS

As an international business manager, would you be willing to ship automobiles to a company in another country before receiving the payment? Would you agree to take a country’s currency for payment instead of U.S. dollars? These are examples of risks faced by every organization involved in international business.

Strategies for Reducing Risk

To reduce international business risk, management experts advise the use of four strategies. First, carry out business in many countries. This approach reduces the risk faced when doing business in only one country or a single region. If turmoil occurs in one nation, causing lost sales and profits, the global company is covered with profits from other markets.

Next, offer a range of products. When an organization broadens its product line, reduced sales of one item will not mean complete failure for the company. Successful global organizations continually create new products, seek new uses for existing products, and look for new markets for their products.

Third, involving local business partners may reduce risk. Joint ventures with local companies help to reduce political and social risks. An agreement between a global company and a local business can help both organizations. In addition, the citizens and government of the host nation will not feel as threatened by outsiders if a company they are familiar with is involved.

Finally, employ local management in order to lower global business risk. Executives and other managers who are native to a country or region better understand cultural norms and political actions. This knowledge can help the international company adapt its product and business activities to the needs of the foreign market being served.

International Property Rights

In some South American countries, local companies not connected to the National Basketball Association make shirts celebrating the championship of an NBA team. In China, street vendors illegally duplicate and sell copies of popular movies, music videos, and books. These are both examples of violations of property rights.

Property rights are the exclusive rights to possess and use property and its profits. This excludes everyone else from interfering with the use of the item. Intellectual property refers to technical knowledge or creative work. It includes software, clothing designs, music, books, and movies. For many companies, their intellectual properties are valuable assets that generate sales and profits. A patent is the exclusive right of an inventor to make, sell, and use a product or process. An inventor may obtain a patent on a computer component, a new package design, or a prescription drug. These inventions can give a company a competitive advantage. Patents are designed to encourage innovation and progress.

A trademark is a distinctive name, symbol, word, picture, or combination of these that a company uses to identify products or services. Common trademarks known around the world include...
the McDonald’s golden arches and Kellogg’s Tony the Tiger. A *copyright* protects the original works of authors, composers, playwrights, artists, and publishers. In the United States, a new copyright gives originators sole rights to publish and exhibit their creative works for their lifetime plus 70 years.

Most other countries have similar laws. There may be differences in the definitions and type of protection. Some countries do little to enforce those laws, especially when the products of a foreign company are involved. *Counterfeiting* refers to illegal uses of intellectual property, patents, trademarks, and copyrights. For example, a company may make slight changes in a well-known product and sell it in other countries. They are using the product illegally so they don’t have to pay for the development costs of their own products or pay the original company for the product. By using the actual product name or trademark illegally, they are trying to profit from the reputation of the famous company. When property rights laws are not enforced, companies can lose profits. This discourages them from participating in international trade.

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**14-3 Assessment**

**>> Key Concepts**

Determine the best answer.

1. True or False. Every risk a business faces can be insured.

2. The growing use of the Internet as a business tool is an example of what type of business risk?
   a. economic conditions
   b. technology change
   c. consumer demand
   d. business operations

3. True or False. To reduce the risks of international business, a company should conduct business in many countries.

4. The exclusive right of an inventor to make, sell, and use a product or process is a
   a. trademark
   b. copyright
   c. patent
   d. None of the above is correct.

**>> Make Academic Connections**

5. **Economics** Use the business section of newspapers and business magazines to gather information on predictions for changes in the economy for the next six to twelve months. Based on that information, prepare a two-page written report for small business owners in your community identifying how those changes might affect their businesses in a positive or negative way.

6. **International Relations** Use the Internet to gather information on the fraudulent use of the intellectual property of U.S. businesses in other countries. Develop a table that identifies the U.S. company, the product that has been misused, the country or countries in which the fraud has occurred, and any action taken by the company to protect its property rights. Present the information in your table to other class members. Discuss the effect of the fraud on businesses and consumers.
With more than 130 protected parks, refuges, and reserves, the natural beauty of Costa Rica is the foundation of this country’s pride and its main tourist attraction. When you are having a casual conversation with local business associates, the country’s tourist sites and natural beauty are acceptable topics.

Business negotiations and decision-making usually involve people at various levels of an organization, not just the top officials. In business settings, wear dark, conservative suits. Your business cards should have a Spanish translation on the back. Be sure to present the cards so they can be read by the people receiving them in their own language. While business gifts may not be expected, small presents are appropriate when you are invited to someone’s home. The most common gifts are flowers, candy, fruit, or a plant.

Expect to dine between 7 and 8:30 p.m. Always be on time for a business meal and other meetings. These visits are usually prearranged. In rural areas of the country, life is less formal. Quite often, people visit unannounced. When you arrive at the door, don’t knock. Instead, shout “Upe!” This greeting in Costa Rica means “let me in” or “anybody home?”

The stable political and economic environment of Costa Rica makes it an attractive location for investors. Full ownership of real estate and businesses by foreigners is allowed. This freedom is different from many countries where local ownership must exceed 50 percent. The high educational standards of Costa Rica also make it appealing to international companies. High-tech businesses are adding to the economic base of the country. As technology exports increase, traditional products, such as coffee and bananas, will become a smaller portion of the country’s total trade.

Black beans and rice are foundation elements of the Costa Rican diet. Breakfast may consist of gallo pinto (a combination of rice and beans). At lunch, rice and beans might be mixed with salad, eggs, or meat. Then, for your evening meal, you may have rice with chicken and, of course, beans.

Think Critically
1. How does doing business in Costa Rica differ from other countries?
2. What elements of Costa Rican society help to enhance the country’s economic development?
3. Conduct library or Internet research to find additional information about business and economic activities in Costa Rica.
14-1 Overview of Risk Management

1. There are many types of risks and possible losses. The main types of risks are economic and non-economic, pure and speculative, controllable and uncontrollable, and insurable and uninsurable. Individuals and businesses need to be aware of risks and attempt to reduce possible losses, especially for those that may result in physical or financial harm.

2. Individuals and businesses must determine how they will deal with the risks and possible losses they face. There are four possible ways to deal with risks: avoid the risk, transfer the risk, insure the risk, or assume the risk.

14-2 Insurable Risks

3. Most individuals and businesses cannot pay for large economic losses, so they share the risk with other individuals or businesses. They purchase insurance to provide the needed financial protection in the event they suffer a financial loss.

14-3 Uninsurable Risks

5. If the chance that a risk will occur cannot be reasonably predicted or the possible financial loss to the business calculated, it will be unlikely that an insurance company will provide coverage. The costs of some risks are so high that a business cannot afford the cost of insurance protection.

6. To reduce international business risks, companies should conduct business in many countries, offer a variety of products, involve local business partners, and employ local management.

1. Identify one personal, property, and liability risk faced by a family. Identify one of each that is faced by a business. Now identify a non-economic risk for an individual and for a business.

2. What are several controllable risks you and your friends might face? What are some uncontrollable risks you and your friends might face? What makes the risks you identified controllable or uncontrollable?

3. People and businesses can deal with risks in four ways. Identify them and describe the advantages and disadvantages of each.

4. Under what circumstances should you consider buying insurance? Are there circumstances where you are facing an insurable risk and you would choose not to buy insurance? Why would you make that decision?

5. List several questions you would want answered about an insurance company before you decided to purchase insurance from the company.

6. Visit the web site of a company that sells automobile insurance. What are the procedures you should follow if you are involved in an automobile accident and that company insures you? Are the procedures different if the accident is your fault rather than the fault of the driver of another vehicle?

7. Visit the web site of a large employer in your community or region. Locate information about the insurance benefits that the company offers its employees. Determine the types of insurance offered, who is eligible for the insurance benefits, and whether the company pays some or all of the costs for the insurance premiums.

8. Identify a type of business you would consider owning or managing. What are some specific risks the business could face that would be uninsurable because the chance of the risk occurring...
the amount of loss cannot be easily predicted? Are there some risks facing the business that could be very expensive to insure?

9. What information sources are available that could be used by businesspeople to keep track of changes in economic conditions that could affect their companies? What are some current economic conditions that could have a positive or negative effect on U.S. businesses?

10. Suggest several ways that a retail business can improve security to prevent theft of merchandise by customers and employees. Are there ways operations can be changed or improved to reduce the chances of theft?

11. You own a small business that produces computer games. You are considering selling the games in several foreign countries. What risks might you face as you begin international trade that you didn't face in the U.S.? Which of the risks are controllable and which are uncontrollable? Identify several steps you could take to reduce those risks.

> > Develop Your Business Language

Match the terms listed with the definitions.

12. Agrees to take on certain economic risks and to pay for losses if they occur.

13. Those that can be reduced or eliminated by actions you take.


15. The amount the policyholder must pay for insurance coverage.

16. The person or business for which the risk is assumed.

17. Those that can result in financial loss.

18. The possibility of incurring a loss.

19. A policyholder's request for payment for a loss that is covered by the insurance policy.

20. The person or company purchasing the policy.

21. Presents the chance of loss but no opportunity for gain.

22. The exclusive rights to possess and use property and its profits.

23. States the conditions to which the insurance company and the policyholder have agreed.

24. Exchanges the uncertainty of a possible large financial loss for a certain smaller payment.

25. Can result in losses, such as health and personal well being.

26. Can lead to a loss of personal or business items such as money, vehicles, and buildings.

27. Related to harm or injury to other people or their property because of your actions.

Key Terms

a. claim
b. controllable risk
c. counterfeiting
d. economic risk
e. insurance
f. insurance policy
g. insured
h. insurer
i. liability risks
j. personal risks
k. policyholder
l. premium
m. property rights
n. property risks
o. pure risk
p. risk
Decision-Making Strategies

The Chrismann Company is a manufacturer of lawn equipment that it sells through garden centers in a ten-state region of the upper Midwest. To distribute its products, it maintains a fleet of 25 trucks. It also has 18 cars driven by its sales people. The company recently finished a review of its vehicle insurance costs. Records show that the average cost to insure each truck is $960 a year and $725 for each car. Insurance claims filed for the past eight years averaged $31,200 a year. When studied closely, data shows that claims in two of those years were under $10,000 and for three years exceeded $45,000. The company’s executives are considering canceling their vehicle insurance. They want to set up a fund in the company using the money they currently pay to the insurance company. That fund would be used to pay costs of repairs and injuries resulting from any vehicle accidents.

28. If the average costs continue for the next five years, how much will the company save using their new plan?

29. Develop reasons for and against the new plan. If you were an executive, would you be in favor of or opposed to the plan?

Make Academic Connections

30. ECONOMICS Speculative risks offer the chance to gain or to lose. People invest their money hoping to get a good return on the investment. Still, most investments have some risk, which means the money can be lost. Common investments are savings accounts, stocks, and real estate. Identify two additional investments. Prepare a table that compares each of the investments in terms of their risk and possible gain or loss.

31. WRITING You have been asked by a business owner to give advice on how to deal with a risk the business is facing. During the winter after an ice storm, the parking lot and sidewalks are often very slippery. There is a risk that employees and visitors may slip on the ice and be injured. Prepare a memo to the business owner describing some ways the business might deal with the risk. Recommend the actions that should be taken and reasons for your recommendations.

32. TECHNOLOGY Use your local telephone or business directory or the Internet. Identify five insurance agents that sell business insurance in your area. Use a computer to create a database of information about those agents. Include the agent’s name, agency name, address, telephone number, e-mail address, insurance company represented, and types of business insurance sold.

33. MEDICINE AND LAW The medical profession has been faced by rapidly increasing costs for malpractice insurance. There is a debate about the reasons for those increases which include increasing medical costs, poor practices by some health professionals, expensive judgments ordered by juries against doctors in court cases, and high fees charged by lawyers. Conduct research on medical malpractice and prepare a two-page report on your findings. Include recommendations on how to reduce the cost of malpractice insurance.

34. GRAPHICS Businesses try to reduce the number of accidents and injuries in their buildings by continually reminding employees of the importance of safety. Prepare a poster that could be displayed in a local business that has an attention-getting message about safety and accident prevention.

35. CONSUMER RESEARCH Visit a store in your community that sells clothing for men, women, and children. Study the items that have been reduced in price. Identify factors that explain why the merchandise is not selling and needs to be placed on sale. Note any differences in those factors for women’s, men’s, and children’s apparel. Based on your research, develop several recommendations that can be used by the company in the future to select products that will respond to consumer needs and preferences.

36. INTERNATIONAL BUSINESS Several unique types of insurance are available for companies that participate in international commerce. Use the Internet to identify five types of insurance that might be considered by a company buying or selling products in another country. Prepare a table that identifies each type of insurance, its purpose, and a company or organization that offers the insurance for sale.
> > **Linking School and Home**

Meet with family members to discuss the types of risks that members of your family face at home, at work, and in the neighborhood. Discuss whether the risks are controllable or uncontrollable and insurable or uninsurable. Identify any insurance policies held by family members and the risks that are insured by each policy. Decide whether your family is doing as much as it can to be protected from the risks that you identified.

> > **Portfolio Activity**

To provide tangible evidence of your learning about identifying and managing business risks, do the following:

**COLLECT** information on events that have been in the news that describe important risks faced by businesses.

**CREATE** a visual to illustrate how businesses can take steps to reduce the risks they face.

**CONNECT** what you learned about managing business risks to an important concept you learned in another class. Make the connection by preparing a one-minute presentation on how businesses deal with risks.

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**Advanced Interview Skills Event**

Advancement in the workforce depends on skills, work ethic, and an organized career portfolio.

You have been employed by Secure Insurance for five years since you graduated from high school and attended college. File clerk was your first position with the company. Your strong work ethic and quick understanding of the industry earned you a promotion to the position of insurance adjuster. You will earn your college degree in Business Administration next month. Since you have thoroughly enjoyed working for Secure Insurance, you would like to apply for a management position. You take great pride in your work ethic and understanding of the insurance industry.

You must create a career portfolio to sell your qualifications. You also will participate in an interview to prove your qualifications. The application letter must be addressed to:

Ms. Cassandra Smith  
Human Resources Department Manager  
Secure Insurance  
2345 Old Cheney Road  
Lincoln, NE 68502

**Performance Indicators Evaluated**

- Demonstrate knowledge of job search skills.
- Apply technical writing skills to produce an application letter and resume.
- Demonstrate effective communication skills.
- Demonstrate the ability to create and effectively use an employment portfolio.
- Complete a job application form.
- Discuss understanding of work ethics and work environment.
- Describe knowledge of job advancement.
- Demonstrate interpersonal skills.
- Create an attractive portfolio for use during a job interview.

For more detailed information about performance indicators, go to the BPA web site.

**Think Critically**

1. What is your definition of a strong work ethic?
2. Why is experience during college important for career advancement?
3. What colors would you wear for this interview?
Global Business Project

Implement International Business Operations

Goals
- Identify international marketing activities.
- Explore technology uses of business in varied global settings.
- Name income sources, operating expenses, and financing sources for international business operations.
- Research production methods used in countries with varied levels of economic development.
- Analyze risks faced by companies involved in international business.

Activities
Use your textbook, library materials, web sites, interviews with people, and other resources to complete the following:

1. Plan global marketing activities.
   Marketing has four main elements: (1) the product, (2) pricing methods, (3) promotional activities, and (4) distribution channels. Using a business idea from the previous unit (or another international business), briefly describe each component of marketing for this good or service in a specific country or region of the world.

2. Identify technology uses. Research information needs of companies involved in international business. Describe types of computer systems, networks, and software used by multinational companies in various countries.

3. For your business idea, list items (with estimated amounts) that would be necessary to create and market this international product. Research start-up costs and financing sources (such as loans, money from investors, or personal assets). Identify sources of income and operating expenses.
4. Production methods around the world vary based on tradition, technology, economic conditions, and local labor skills. Describe common production methods used in various regions of the world.

5. Create a list of economic, social-cultural, and political-legal risks a company might encounter when doing business around the world.

Present

Prepare a portfolio (folder, file, or notebook) to store the information and materials you created in the activities above.

1. Create a visual summary (poster, computer presentation, or web site) of your international marketing activities. Also, develop a package design or advertisement to communicate the main parts of your global business idea.

2. Based on your global business idea, describe information needs for these categories: (1) financial information, (2) production, (3) sales and marketing, and (4) human resources. Create a flowchart to communicate the movement of information within your planned business organization. Show sources of data, such as customers, sales records, and employee time cards, as the input section. The output section might include information items such as financial statements, inventory records, and payroll reports.

3. Create a presentation (with visuals) listing start-up costs, projected monthly revenue, and monthly expenses for your business idea. Spreadsheet software may be used to prepare a summary of the financial data.

4. Prepare an in-class presentation (or video) to communicate production methods and business risks from around the world.
Unit 4

Personal Financial Management

15 Consumers in the Global Economy
16 Money Management and Financial Planning
17 Banking and Financial Services
18 Consumer Credit
19 Savings and Investment Strategies
20 Insurance
Online Medical Information You Can Trust
Where could you find valid online information about health? Consider the resources of Animated Dissection of Anatomy for Medicine (A.D.A.M.). This Atlanta-based company provides interactive medical information for health care organizations, medical professionals, consumers, the media, and students.

A major product of A.D.A.M. is its extensive multimedia medical encyclopedia covering 3,500 diseases and conditions. The service includes graphics, 3-D image models, virtual tours of the human body, and broadcast-quality animation. Physician-reviewed text ensures the highest quality of medical information.

Efforts by A.D.A.M. for global expansion have been successful. Within a few months of starting to look at international opportunities, the company sold its interactive medical software in Singapore, Switzerland, and Malaysia. They also have a representative in Spain and a distributor in Taiwan.

Think Critically
Create a plan to provide professionals and consumers with other types of vital information they might need in their daily activities.

Providing for Consumers with Special Needs
Joe Semprevivo worked in the ice cream shop owned by his parents, but was not able to eat the product he served to others—he had had juvenile diabetes since he was nine years old. Joe was motivated to change that. By age 12, he developed the first sugar-free ice cream. Within three years of creating the ice cream, Joe placed his product in about 75 stores. He visited with supermarket managers and convinced them to carry the product. He explained that his product would serve the needs of diabetics and other health-conscious consumers.

Joe next desired to have a snack he could take with him to school. Along with his parents, at age 15 he developed a cookie appropriate for those with his same medical condition. Today, Joseph’s Sugar-Free Cookies come in eight flavors. His marketing efforts include the National Diabetes Outreach (NDO), which raises funds by selling Joseph’s Lite Cookies. Income from the cookies helps communities to provide diabetic education, testing, and other resources to fight this disease.

Think Critically
What are some special needs that might be met with new products?
Chapter 15

Consumers in the Global Economy

15-1 Consumer Buying Decisions
15-2 Consumer Rights and Responsibilities
15-3 Consumer Protection Actions
Planning a Career in...
Consumer Assistance

Each day, millions of consumers seek information and assistance on various buying topics. These requests can range from finding which stores carry certain brands to getting a refund for a defective product. Employment opportunities in consumer assistance can be a career in business, in government, or with a nonprofit organization. A consumer affairs professional in a public relations position may help with expanding an organization’s markets. Customer service departments provide information and support. Others might create materials on the proper use of a product. For example, banks and insurance companies print booklets to help consumers manage their money. Some large retail firms provide printed materials and web sites to help consumers with their buying decisions.

Employment Outlook

• Slow growth for government employment positions in the consumer protection field.
• Continued growth of customer service representatives for companies expanding their sales and business activities.
• Some growth of consumer protection employees with specialized training in law, technology, health care, and financial services.

Job Titles

• Customer Service Representative
• Consumer Affairs Director
• Consumer Products Specialist
• Consumer Agency Administrator
• Consumer Agency Researcher
• Consumer Credit Counselor
• Legal Aid Attorney
• Legal Aid Assistant
• Legislative Lobbyist

Needed Skills

• Most consumer assistance positions require a basic understanding of business activities, marketing, and consumer behavior. Courses in sociology and psychology are also of value.
• Strong interpersonal, research, and communication skills are a necessity when working to locate and present consumer information.
• Legal training can be of value to workers in a variety of consumer information and consumer protection fields.

What’s it like to work in...
Consumer Protection

The e-mails continue to come in every day. Today, several messages request information about identity theft. Yesterday, it was complaints about online auctions. Tomorrow, it could be comments about a proposed consumer protection law.

A consumer affairs specialist with a state or local consumer protection office must be ready for a variety of activities. Research, responding to requests, and report preparation are just a few of the daily responsibilities.

While salaries may be low, the satisfaction of helping others is very rewarding. When a low-income person who was scammed in a work-at-home scheme gets back some money, the day has been very worthwhile.

What about you? Would working in the field of consumer information and protection be of interest to you?
CONSUMER INFORMATION SOURCES

Consumers have the power to decide to buy or not to buy. Businesses must serve the needs of consumers. Without satisfied consumers, businesses would not make sales, earn profits, or remain in business. Several information sources are available to help consumers with their buying decisions.

Product Testing Organizations

Product testing organizations test products and services for the benefit of consumers and business. Manufacturers pay these organizations to perform safety tests on products. Underwriters Laboratories tests electrical components of products from all over the world for fire and electrical safety. The UL symbol indicates that the product has been tested and judged safe for normal use.

The Association of Home Appliance Manufacturers (AHAM) develops and maintains performance standards for appliances such as refrigerators, air conditioners, and freezers. The AHAM seal indicates that a product has met performance standards. The Carpet and Rug Institute and the Motorist Assurance Program issue other seals of quality.

Consumers Union reports scientific, technical, and educational information about products and services. This nonprofit organization performs independent tests on consumer goods. It publishes articles in a monthly magazine called Consumer Reports.

Media Sources

Each day, you have access to a range of media sources offering consumer information.
**Print Publishers** Many magazines and newspapers provide various types of consumer assistance. General interest magazines such as Consumers Digest, Good Housekeeping, and Parents provide articles and product information. For money management, financial planning, and investment advice, you could read Money or Kiplinger's Personal Finance Magazine.

Specialty magazines and newspapers also provide information about specific types of products or services. These publications cover topics such as motor vehicles, computers, boats, electronic equipment, travel, and education. Readers can obtain a better understanding of the technical aspects of these products and services.

**Broadcast Organizations** Radio and television are valuable sources of consumer information. Most stations carry programs to inform you about product safety, care and use of products, and shopping tips.

**The Internet** Online information has become a very valuable resource for consumers. Most consumer information sources can be accessed through the Internet. The use of a search engine allows you to obtain specific answers for your consumer questions.

**Government Agencies**
Federal, state, and local governments also inform consumers. The federal government has the Consumer Information Center, which serves as headquarters for consumer information. This agency puts out a quarterly catalog of publications. It also maintains an extensive web site to assist consumers.

The United States Department of Agriculture (USDA) offers publications and online information about food buying, meal planning, and nutrition. The USDA also inspects and grades meat and other foods. It makes that information available to consumers.

The U.S. federal government maintains one of the most comprehensive web sites with information for consumers. Go to businessxtra.swlearning.com and click on the link for Chapter 15. Select a specific consumer topic. What types of information are available on this topic? What federal agencies provide this information? Describe some specific suggestions for consumers related to this topic.

businessxtra.swlearning.com

Other federal government agencies that provide consumer information include the Federal Trade Commission (FTC), Food and Drug Administration (FDA), Consumer Product Safety Commission (CPSC), National Highway Traffic Safety Administration, Department of Housing and Urban Development, and Environmental Protection Agency.

Every state has consumer protection agencies. These agencies have web sites

Name some ways in which you are protected on a daily basis by the activities of a government agency.
to provide information and handle consumer questions. State departments of banking and insurance are available to assist with those areas. Large cities and counties also have consumer assistance offices.

**Business Sources**

As a public service and in an effort to sell goods and services, businesses make consumer information available.

**Advertising** Advertising is widely available. It is a popular source of consumer information. The main purpose of an advertisement is to encourage you to buy. Because of this, you should carefully evaluate this information source.

Advertising can be helpful. Useful advertisements tell you what the product is, how it is made, and what it will do. Advertisements give facts that you can use to compare the product with other competing products. Beware of advertising claims that really tell you nothing about the product. If an advertisement states that a product is better, ask, “Better than what?”

**Product Labels** A label, attached to or printed on a product, provides useful information. A label will report the nature or content of a product. The label will also likely tell you what the product is made of, its size, how to care for it, and when and where it was made. Clothing labels must tell you what the product is made of and must give instructions for washing or cleaning.

**Customer Service Departments**

Many businesses have special departments focused on customer service. Some firms provide customers with booklets on a range of consumer topics. For example, banks and insurance companies publish booklets to help consumers manage their money. Some large retail firms provide printed materials to help consumers with their buying problems.

**Better Business Bureau**

The Better Business Bureau (BBB) can provide helpful information. If you plan to buy a used car from a particular dealer, you could call the BBB to find out what experiences others have had with that dealer. If consumers have reported problems with the firm, you could find out about these complaints. BBBs give facts only. They do not recommend products or firms.

**Personal Contacts**

An often-used information source is “word of mouth.” This includes information received from other people. You often trust information provided by others who have bought and used a product. When planning a purchase, you may talk to someone who already owns the product or has used the service. This word-of-mouth consumer information can be a valuable resource when making consumer decisions.

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**CHECKPOINT**

What are the main sources of consumer information?
WISE BUYING STRATEGIES
Whenever you plan to buy something, think about several key decisions. These include the following. Do you really need the item now or can you wait? Which stores should you consider? What quality do you want? What price are you willing to pay? Should you pay cash or use credit? If you make the purchase, what other important item may you have to do without?

Use Decision-Making
As a consumer, you should follow the decision-making steps when making a purchase.
1. **Identify your needs or wants.** Be able to state clearly why you intend to buy something.
2. **Know the choices available.** These choices include price, quality, location, variety, reputation, and other factors.
3. **Determine your desired satisfaction.** You should develop answers to questions such as, “How much am I willing to pay?” “What quality level do I want?” and “How long am I willing to wait for the item?”
4. **Evaluate alternatives.** At this stage, you will shop for the products and services that could satisfy your needs. You will compare them in terms of the criteria you have identified.
5. **Make the decision.** Decide whether to buy or not. Determine what product or service is most satisfying. Decide from which business you will make the purchase.

Good buying skills will make you a better consumer. You can get greater value for your money each time you make a purchase.

Technology Topics

Electronic Package Tags
You are walking along and suddenly you receive a text message on your cell phone. You are informed that a certain item is on sale at a store as you walk by that exact store. This message could be both convenient and frightening.

Radio frequency identification devices (RFIDs) in clothing labels and other products will allow keeping track of things and people. Currently, RFIDs are being used for highway toll lanes, pets, library books, and baggage tracking by airlines. They are also used in warehouses to monitor the location of inventory. Companies are able to know the exact location of their products. This system reduces theft and misplaced inventory.

Two components make up an RFID system. First, the data-loaded tag (called the transponder) is attached to the item to be tracked. Second, a reader (the transreceiver) captures the tag’s data using radio waves. These data are then sent to a computer for processing.

In the future, RFIDs could be used in homes to turn on appliances and monitor heating and security. Tagging of individual consumer products and clothing is also expected. A purchase you make could be tracked from the store to your home and everywhere else it is used.

Think Critically
1. What are possible uses of RFIDs that could benefit consumers?
2. What concerns might be associated with RFIDs?
Comparison Shopping

Smart consumers are comparison shoppers. They compare price, quality, services, and brands.

**Compare Prices** A unit price is a price per unit of measure. Most stores help consumers compare among various brands and sizes of the same product. Shelf labels show both the total price and the price of one standard measure, or unit, of the product.

If you need to calculate a unit price, divide the price of the item by the number of units per measure. For instance, in the supermarket, you see that a 16-ounce bag of Golden Frozen Corn costs $1.26. An 8-ounce box of Yellow Perfection Corn sells for $0.69 per box. Which is the better buy for the dollar?

If you compare the total prices only, it is not easy to decide. Since stores usually post the cost per ounce, the unit price, you could quickly compare the two package sizes. In this case, the 16-ounce bag would show a unit price of 7.9 cents an ounce ($1.26 ÷ 16). The 8-ounce box would be 8.6 cents per ounce ($0.69 ÷ 8). Unit pricing would quickly tell you that the 16-ounce bag is a better buy per ounce for the dollar.

Prices of products can vary greatly. The cost of the same item often differs from store to store and in different geographic regions. For example, an identical camera may be available with prices ranging from $25 to over $40. These price differences emphasize the need for comparison shopping.

**Compare Quality** High-quality products and services often cost more. Buying lower-quality items can sometimes turn out to be more expensive than buying higher-quality items. For example, if you buy a lower-quality pair of shoes, they may wear out in a short time. You will have to replace the lower-quality shoes sooner. You may end up buying two pairs of low-quality shoes in a short span of time.

**Compare Services** Most businesses try to provide good service, but types of services can differ. Some businesses sell for cash only. Others offer credit. Some businesses provide free delivery. Other services offered may include layaways, repairs, and special orders. Service is important, but be careful not to pay for more service than you need.

**Compare Sales** The word “sale” is perhaps the most overused, and least trusted, word in marketing. You have probably seen sale signs a thousand times. When an item is really on sale, it is offered at a price lower than its normal selling price. Some “sales” may not really be sales at all.

Promotional sales are used to promote the selling of regular merchandise with short-term price reductions. This type of sale may be used when a new product...
store opens or when new products are introduced. Retailers may use promotional sales in hopes that customers will buy the sale items as well as other products not on sale.

A clearance sale is used to clear merchandise that stores no longer wish to carry. This may be end-of-season items, odd sizes and models, or discontinued merchandise. Clearance sales usually offer some bargains. Be sure that you need a sale item before you buy it.

**Compare Brands** A brand is a name given to a product or service to distinguish it from other similar and competitive items. The company that makes the product or service usually creates a brand name. Brand names are designed to help build customer loyalty.

National brands are advertised all over the country. They are sold in almost every community. Among these goods are items such as food, clothing, shoes, tools, and cosmetics. Manufacturers of such goods often place brand names on the items they make. Well-known brand names include Kellogg’s, Jell-O, Colgate, The Gap, and L’Oreal. Recognizing national brand names allows you to expect uniform quality. Buying brand-name goods is especially helpful when it is hard to inspect for quality, such as packaged products.

Some stores have their own brand names, called store brands or private label brands. For example, Craftsman has long been one of the brand names on tools sold by Sears. Store brands are usually sold at a lower cost than national brands. Buying store brands may save you money and offer good quality at the same time.

Stores may also carry unbranded items at reduced prices, called generic products. Generic products are less expensive because they do not require advertising and fancy packaging. These lower costs result in lower prices. Differences in quality between generic and branded products may be small, making these items a good value.

**Wise Buying: A Summary**

Skillful consumers are efficient in their shopping activities. They save time, energy, and money by planning.

**Take Your Time** “I just don’t have the time” is something many people say. Spending time planning purchases usually results in savings. Taking your time will allow you to look for the best values. As a good shopper, you should refuse to be hurried. Then, you can avoid buying things that you really do not want or need.
Work as a Group

Today, consumers have more ways to buy than ever before. Using the three main categories of buying locations (traditional retailers, contemporary retailers, and non-store shopping), create a list of businesses in your community. Then, discuss the advantages and disadvantages of using each of the three categories.

> Describe the main types of shopping locations.

**Time Your Purchases** For some items, prices are lowest at predictable times. Certain seasons and conditions favor goods and services being sold at reduced prices. Some examples include:

- Fresh fruits and vegetables are usually lower in price during the peak of their growing season.
- Winter clothing is often on sale in January.
- Firewood often costs less in the summer.

Consumer information sources can help you add to this list.

**Avoid Being Impulsive** The opposite of spending time and effort is buying too quickly and is called *impulse buying*. Impulse buying should be avoided. It often happens when an item is nicely displayed where customers are likely to see it, such as near the checkout counter.

Some impulse buying is harmless when the cost is small and the item is worth the price. Be aware that buying more expensive items on impulse can be costly. One of the best ways to avoid impulse buying is to use a shopping list. You can save money with a list whether it is for groceries, hardware, or clothing.

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**SHOPPING LOCATIONS**

When deciding where to buy, you have many choices. The types of stores and other buying locations expand every day because of competition and technology.

**Traditional Retailers**

Many of the stores in which you shop have developed over the past 100 years. *Department stores* have an extensive product line and emphasize service. They may have personal shoppers, make deliveries, and wrap gifts.

*Discount stores* emphasize lower prices on their products. Most discount stores base their success on a high volume of sales and low prices. If service is not important to you, this may be where you should shop.

*Specialty stores* have a special line of products for sale. They carry a wide variety of products in a narrow line such as sporting goods, jewelry, or women’s shoes. Some specialty stores may also be discount stores.

In food retailing, a *supermarket* is the large, full-service store that carries many brands. *Convenience stores* are small stores that emphasize the sale of food items, an accessible location, and long operating hours. These stores usually stock popular items at higher prices.

**Contemporary Retailers**

Today, *specialty superstores* offer low prices and a wide variety of a limited product line. These include retailers such as OfficeMax, Home Depot, and Best Buy.

Discount stores have expanded to include a wide array of food products. These *superstores* may also include other retail services such as a bakery, restaurant, pharmacy, video rentals, and banking.

The *warehouse club* is a no-frills outlet focusing on the sale of large
quantities at reasonable prices. Products are displayed in simple settings resembling a warehouse. These stores target small business owners who are looking to buy various supplies and equipment.

*Factory outlets* have been popular. These stores have a reputation for selling high-quality merchandise at low prices. Products are direct from the factory and sometimes have minor flaws.

**Non-Store Shopping**

Shopping at home started with door-to-door sales. Then, *mail order* catalogs became very popular. People sent in their orders by mail and later called by telephone. Now, you can buy using your television, computer, or fax machine.

Non-store shopping also includes *vending machines*. Each year, more and different products are available through these automated devices. In Japan, a person can buy everything from eggs and toys to flowers and toilet paper from a vending machine.

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**15-1 Assessment**

**>> Key Concepts**

Determine the best answer.

1. The most reliable consumer information source will usually be
   a. advertising
   b. comments from salespeople
   c. comments from other consumers
   d. reports from consumer testing organizations

2. The first step in the buying decision-making process is to
   a. identify product alternatives
   b. evaluate the services at different stores
   c. decide whether to use cash or credit
   d. identify your needs

3. Which of the following is an example of a non-store shopping location?
   a. club warehouse
   b. vending machine
   c. factory outlet
   d. hypermarket

**>> Make Academic Connections**

4. **Math** A 12-ounce package of cereal is priced at $3.20. A larger container of the cereal costs $5.20 for 1½ pounds. What is the unit price for each item?

5. **Communication** Select several advertisements. Develop a list of questions to ask when evaluating advertising. Use these guidelines to evaluate the ads you selected. Prepare a one-page summary of your findings.
Consumer Rights and Responsibilities

**Goals**
- Explain the consumer movement.
- Explain seven consumer rights.
- Describe consumer responsibilities.

**Key Terms**
- consumer movement
- fraud
- guarantee
- express warranty
- implied warranty

**Focus on Real Life**
Juan met Michelle after school. “Hi, Michelle. Have you decided which computer to buy?”
“I don’t know,” replied Michelle. “I looked at the computers at Bayside Computer Store and they have the lowest price. But I got the impression they didn’t take me seriously because of my age.”

Young people often comment that businesses do not respect them as customers or treat them as well as adults. Successful businesses recognize that teens are a powerful consumer group with purchasing power. They not only choose where they want to spend their money, but often influence the buying decisions of family and friends.

Businesses that ignore or disrespect younger customers will likely lose current sales. They may also lose long-term customers who don’t feel comfortable when shopping in these stores. You can be sure that businesses that are aware of consumer rights and buying power will welcome teen customers.

**THE CONSUMER MOVEMENT**
In the past, some businesses were viewed as often trying to take advantage of consumers. False claims were sometimes made about products. Prices were often too high. Some products were unsafe. To fight against unfair business practices, consumers united to demand fair treatment from businesses, giving rise to what is known as the consumer movement.

Because of this movement, public and private agencies, policies, laws, and regulations were developed to protect consumer interests. In 1962, President John F. Kennedy presented his Consumer Bill of Rights and declared that every consumer has the first four rights shown in Figure 15-1. In 1969, President Richard M. Nixon added the fifth right to the list. In 1975, President Gerald R. Ford added the sixth. In 1994, President William J. Clinton added the seventh.

**Figure 15-1**
What are some consumer rights that you have received?

<table>
<thead>
<tr>
<th>Consumer Bill of Rights</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. The right to be informed.</td>
</tr>
<tr>
<td>2. The right to safety.</td>
</tr>
<tr>
<td>3. The right to choose.</td>
</tr>
<tr>
<td>4. The right to be heard.</td>
</tr>
<tr>
<td>5. The right to a remedy.</td>
</tr>
<tr>
<td>6. The right to consumer education.</td>
</tr>
<tr>
<td>7. The right to service.</td>
</tr>
</tbody>
</table>
YOUR CONSUMER RIGHTS

As a consumer, you have the right to expect honesty and fair treatment from businesses. Few businesses are intentionally dishonest. Being a skilled consumer means that you know the Consumer Bill of Rights and how to exercise these rights.

The Right to Be Informed
Most products and services are described in advertisements, on labels, or by a salesperson. You have a right to know what the product or service is and what it will do for you.

Fraud occurs when consumers are given false information in an effort to make a sale. If a salesperson knowingly sells you a car on which the odometer has been turned back 30,000 miles, fraud has occurred.

Not all product information you receive can be expected to be perfectly accurate. Suppose you were looking for a used car for transportation to and from school. If a salesperson told you she thought the car would get about 20 miles to the gallon but it only got 18, you were not deceived. The salesperson may not have been accurate in estimating gas mileage, but no guarantee was made.

When a salesperson exaggerates the good qualities of a product and says, “It’s the best” or “It’s a great buy,” there is no fraud. On the other hand, if the salesperson tells you a car has new brakes and it does not, this is fraud.

The Right to Safety
Consumers have a right to be safe from harm associated with using products or services. Several agencies work to assure the safety of consumers. The Consumer Product Safety Commission has the authority to set safety standards, ban hazardous products, and recall dangerous products from the market.

The Food and Drug Administration (FDA) makes certain that food, drug, and cosmetic products are not harmful to consumers. This federal agency enforces laws and regulations that prevent the distribution of unsafe or misbranded foods, drugs, and cosmetics.

The FDA also works to ensure that product labels do not mislead consumers. The United States Department of Agriculture (USDA) helps ensure consumer safety by setting quality standards for farm products. The USDA also controls the processing, inspection, and labeling of meat products.

The Right to Choose
The right of consumers to choose from a variety of goods and services has become well established. In fact, one of the main activities of the Federal Trade Commission (FTC) is to prevent one firm from using unfair practices to force competing firms out of business. When a business has no competitors and controls the market for a product or service, it is said to have a monopoly. Competing firms encourage customers to buy from them by offering a choice.

CHECKPOINT

What are the seven rights of consumers?

Explain seven consumer rights.

Why is it important for consumers to have choices?
of products and services at a range of prices. By driving away this competition, monopolies limit the right to choose.

**The Right to Be Heard**

Most businesses have a customer service department to hear the concerns or complaints of customers. Some smaller businesses have a specific person assigned to that duty. Businesses are usually happy to take care of problems you have with their products or services.

Several federal government agencies, such as the FTC, also assure your right to be heard. As a consumer, you can complain directly to the FTC if you believe that your consumer rights have been violated. The FTC regulates advertising and encourages informative and truthful advertising.

State government agencies, such as the Office of the Attorney General or the Department of Consumer Affairs, have responsibility for protecting the rights of consumers. They can prosecute businesses for breaking state consumer protection laws. These offices also inspect advertising practices. They handle consumer problems related to automobile repairs, credit, and door-to-door sales practices.

Privately funded groups also help to make certain you are heard. Various national and local groups inform and protect consumers in a variety of purchasing areas. Some groups specialize

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**A Question of Ethics**

**Frauds by Consumers**

- Writing a check on someone else’s account, or changing the amount on a check
- Eating items in a store without paying for them
- Buying a book, reading it, and returning it for a full refund
- Buying clothing, wearing the item, and then returning it
- Asking for a cup for water and using it to take a soft drink from a self-serve dispenser
- Switching price tags from lower-priced items and putting them on the more expensive items

While most of these actions are illegal, all affect the operating costs of businesses. Each of these “frauds by consumers” results in higher prices. Many of these practices have become more difficult with technology. While new electronic devices have improved store security, this equipment has also added to business costs and higher prices.

**Think Critically**

1. What other actions by consumers can result in higher prices for the things you buy?
2. Describe how businesses and individual consumers might help reduce these actions that result in higher prices for everyone.
in auto safety or consumer credit. Others will assist with any consumer problem.

The Better Business Bureau is concerned with problems arising from false advertising or misrepresented products and services. Dues paid by member businesses support BBBs. They work to maintain ethical practices and combat consumer fraud. If you believe your consumer rights have been violated, you can get help from one of 120 Better Business Bureaus around the country. After reporting your concern, the bureau will try to persuade the business to fix the problem. Most businesses willingly carry out the BBB request.

**The Right to a Remedy**

The Fair Packaging and Labeling Act, National Traffic and Motor Vehicle Safety Act, Truth in Labeling Act, and Fair Debt Collection Practices Act all protect consumers. These and other laws are designed to provide assurances that consumers can seek a legal remedy when a problem occurs.

Consumers also have protection provided through a guarantee. With some purchases, a consumer can expect a guarantee or a warranty. A **guarantee** is a promise by the manufacturer or dealer, usually in writing, that a product is of a certain quality. A guarantee may apply to the entire item or only to some parts of it. It may promise that defective parts will be replaced only if a problem occurs during a specified period. No guarantee covers damages caused by misuse.

When making a purchase, a skillful consumer asks about a guarantee. A guarantee is frequently in the form of statements like these: “The working parts of this watch are guaranteed for one year.” “This sweater will not shrink more than 3 percent.” These kinds of guarantees are sometimes called express warranties. An **express warranty** is made orally or in writing and promises a specific quality of performance.

You should review the guarantee before buying an item. You can also require the business to put in writing any other guarantees that have been offered orally. Written guarantees are useful if you need to return a faulty product. Read the guarantee carefully to find out exactly what is covered and for what period.

Some guarantees are not written. They are called implied warranties. An **implied warranty** is imposed by law and is understood to apply even though it has not been stated. In general, the law requires certain standards to be met. For example, it is implied that health care products purchased over the counter at a pharmacy will not harm you when used according to the directions.

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**FYI**
Teenage consumers spend over $200 billion each year. The main categories of their spending are food and snacks, clothing, entertainment, school items, and automobile expenses.
The Right to Consumer Education

Although individual buying decisions are important, educated consumers need to understand how their choices affect the economy. Consumer education should take into account how buying actions create an interaction between consumers and producers. Educated consumers are aware that their decisions not only affect their personal situation, but also have economic and social implications.

The Right to Service

This latest right suggests consumers can expect convenience, courtesy, and responsiveness to consumer problems and needs. The right to service encourages businesses to take steps necessary to ensure that products and services meet the quality and performance levels claimed for those products and services.

YOUR CONSUMER RESPONSIBILITIES

Just as some businesses have not met their responsibilities to consumers, some consumers try to take advantage of businesses. Even consumers who are not unethical or dishonest may have expectations that businesses cannot meet. Consumers also have responsibilities in business relationships.

Be Honest

Most people are honest, but those who are not cause others to pay higher prices. Shoplifting losses are estimated to be in the billions of dollars each year. Businesses make up losses from shoplifting by charging higher prices.

As a responsible consumer, you must be as honest with a business as you want it to be with you. You should be as quick to tell the cashier that you received too much change at the checkout counter as you are to say that you received too little.

Be Reasonable

As a buyer, you are usually responsible for what you buy if the business has been honest. If you are dissatisfied and wish to complain, you should complain in a reasonable way.

You should first be sure that you have a cause for complaint. Be sure that you have followed the directions for using the product. After you have confirmed the details of your complaint, calmly explain the problem to an employee of the business from which you bought the item. In most cases, the business will be glad to correct the problem because it does not want to lose you as a customer.

Be Active

As a responsible consumer, you should report unethical business practices to prevent other consumers from becoming victims. By reporting the matter to
a consumer agency, you might be able to get the shop to keep its word both to you and to future customers.

**Be Informed**
The most important responsibility you have as a consumer is to be informed. Just having the right to be informed will not make you an informed consumer. You must find and use the information available to you.

You should also keep informed about your rights as a consumer. Learn about the laws and agencies that protect your rights and how to report a violation of your rights. Being an informed consumer is hard work, but the extra effort spent in making your dollars go as far as possible will be worth it.

**Be Involved**
In the United States, involvement is an important consumer activity. As a citizen, you have a responsibility to participate in government, which starts by being an informed voter.

As a consumer, you also have responsibilities. When the opportunity arises, make your concerns known to government officials or consumer agencies. Only when you become involved as a consumer can agencies do their jobs and legislative bodies pass appropriate laws.

You have an obligation to society to be a wise and efficient consumer. The world has only a limited supply of natural resources such as petroleum, metals, clean air, and clean water. Sometimes, uninformed consumers unnecessarily waste these resources and contribute to damaging the environment.

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**Assessment**

**Key Concepts**

Determine the best answer.

1. True or False. The U.S. Consumer Product Safety Commission is responsible for regulating the safety of food.
2. True or False. An implied warranty is usually printed in the owner’s manual of a product.
3. A person who compares product information on labels is using the consumer right to
   a. service
   b. be informed
   c. be heard
   d. a remedy
4. If a person returns an item as new for a refund after using it, this violates the consumer responsibility to be
   a. honest
   b. involved
   c. informed
   d. active

**Make Academic Connections**

5. **Research** Go to the web site of the U.S. Consumer Product Safety Commission (CPSC). What services does this government agency provide? How do you and other consumers benefit from the actions of the CPSC?
6. **Law** The Truth in Labeling Act requires that certain information be presented on food labels. Using a label from a food product in your home, identify some of these required items. How would you make food labels more informative for consumers?
Imagine 24 different washing machines all operating in the same room. Envision 32 digital cameras being used by a small group of people. These are scenes you might encounter in one of the 50 testing laboratories of Consumers Union in Yonkers, New York.

Consumers Union was created in 1936 to provide information on products and services to help buyers get the most for their money. Today, Consumers Union continues to sort out low-quality and unsafe products from those items that will give you the best value. Each month, the results of these consumer tests are reported in Consumer Reports magazine and on the Consumer Reports web site.

Consumers Union also conducts extensive testing on motor vehicles. Each year, the organization buys the vehicles the same way you would buy a car. That is, Consumers Union has shoppers bargain with dealers for the best price. After an inspection of the vehicle’s features, road testing occurs on a 195-mile course. Engineers record various performance data. Finally, crash tests are conducted to assess safety and the possibility of a rollover. All of these findings are then published to help consumers make wiser car-buying choices.

In recent years, as consumers spend more of their income on services, Consumers Union has expanded its activities. Every month in the magazine, consumers are provided with information about banking services, health care, insurance, lawyers, and other personal and financial services.

Consumers Union is involved with protecting consumers in other ways. Offices in Washington, DC, California, and Texas promote improved consumer protection laws. The Washington office works to build support for laws related to telecommunications, product safety, food safety, financial services, health care policy, energy, international trade, and other consumer issues.

The Consumer Policy Institute (CPI), a division of Consumers Union, conducts research and offers educational programs on consumer topics. CPI publishes reports, organizes conferences, and testifies at government hearings.

**Think Critically**

1. How do the activities of Consumers Union assist consumers?
2. Conduct research to create a list of current consumer issues that are of concern to Consumers Union.
**COMMON CONSUMER PROBLEMS**

Consumers hope that their purchases will always result in a satisfactory transaction. Still, problems sometimes arise. The item may have been damaged in transit. The wrong size sweater may have been shipped. These types of consumer problems are usually resolved quite easily.

Sometimes, problems that are more serious might occur. Your credit card payment may not be properly recorded to your account. A product you purchased might stop working after just a few days of use.

**Sources of Complaints**

Various consumer agencies report that the main sources of consumer complaints involve the following types of business.

- Motor vehicle purchases, repairs
- Deceptive investments
- Identity theft and credit card fraud
- Guaranteed and advance-fee loans
- Credit repair scams
- Telemarketing, catalog, and magazine sales
- Internet auctions, online purchases
- Prizes, sweepstakes, and phony lottery promotions
- Work-at-home and start-your-own-business opportunities
- Travel and vacation promotions
- Health and diet gimmicks

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**Focus on Real Life**

Monica Robinson bought an expensive leather purse. Unfortunately, after she used the purse for a few weeks, the zipper broke. She took the purse back to the store from which it was purchased. Monica very politely and calmly described to the salesperson how the zipper broke. She also had her receipt from the purchase to show that the purse was only six weeks old. It was decided that the store would pay for the repair of the zipper. It took one week to repair the zipper, at which time Monica got her purse back as good as new.

This consumer problem had a pleasant ending. Most of them do. You should not get upset or angry in order to get satisfactory results from a business. In fact, most businesses are eager to solve problems that consumers have. They want happy, satisfied customers who will return.

Solving consumer problems is usually a matter of practicing good two-way communication. Let the business know what you want. The job of the business is to tell you what you can expect to get. If both consumer and business are honest and fair, the problem can be solved.
Deceptive Business Activities

Consumer fraud can be discovered in media ads, in the mail, or even on a city street corner. Various scams, cons, and swindles have been around for a long time. When a deal seems like it’s too good to be true, it probably is! Each year, federal government agencies report consumers losing billions of dollars on phony investments and other deceptive offers.

The Internet has become the number one source of fraudulent offers. Consumers may not know the identity or location of all online merchants. This makes it difficult to track down the con artist after you have already lost your money.

The most common online scams involve sales of Internet services and general merchandise. Online auctions, pyramid schemes, business opportunities, and work-at-home offers are also common sources of fraud.

Internet scams can also take the form of prizes, sweepstakes, and credit card offers. Consumers have lost as much as $10,000 through Internet fraud. Be cautious when making your online purchases.

Protection for Shoppers

With the increasing popularity of e-commerce comes the concern for consumer rights. Federal laws that protect Internet and TV shoppers are the same as those that govern purchases made by telephone. The seller must send you the item within 30 days or within another period specifically stated by the company. If there is a delay, the seller must notify you. You then have the right to cancel your order.

If an unreceived or returned item is billed to your credit card, you have 60 days to dispute it. The credit card company then has 30 days to respond. Within 90 days of your letter, the credit card company must investigate the matter and explain why the bill is correct or incorrect.

You do not have to pay the part of your credit card bill under dispute until the matter is resolved. To avoid finance charges, you must pay the rest of your bill on time.

FYI

“Phishing” is a high-tech scam that uses spam or pop-up messages to deceive you into revealing your credit card number, bank account information, Social Security number, passwords, or other sensitive information. The Federal Trade Commission warns consumers never to disclose personal data online to a questionable source.

Name some Internet or other scams in media of which you are aware. How do you know that they are probably not legitimate offers?
THE COMPLAINT PROCESS

While no one wants consumer problems, they do occur. When they happen, a person should be prepared. Consumer protection experts suggest four steps when trying to resolve a purchasing problem.

Step 1 Contact the Place of Purchase
Most consumer complaints are settled by returning to the place of purchase. Calmly explain the situation. Provide evidence of your purchase and the problem. A receipt or other dated documents will help you convince the store to take action in your favor.

Step 2 Contact the Company Headquarters
If communicating with the place of purchase does not bring satisfaction, you should move up in the organization. Contact the customer service department or other office within the company. The address, phone, and e-mail of most organizations can be obtained on the package or through a search.

When contacting the company, once again provide facts about the situation. Tell what happened in a brief letter or e-mail. Include copies of any documents that back up your story. Be specific about what action you would like them to take.

Step 3 Involve a Consumer Agency
If communication with the business fails to satisfy your demands, consider using the services of a consumer agency or public interest organization. Contacting a local, state, or federal government agency can encourage the business to take action.

Some agencies and organizations specialize in specific consumer topics such as consumer credit, health care, motor vehicles, or telecommunications. Other groups, such as state consumer protection offices, will help you with almost any consumer concern.

Step 4 Take Legal Action
When the first three steps do not work, more extreme actions may be required. Several legal actions are available to consumers. These include the use of a third party for dispute resolution, class action suits, small claims court, and hiring a lawyer.

CHECKPOINT
List the steps of the consumer complaint process.

Why might someone decide not to pursue a lawsuit against a company even when the company has been fraudulent?
LEGAL ACTIONS FOR CONSUMERS

If contacting the business or a consumer agency does not resolve the problem, various legal actions may be considered.

Third-Party Settlements

A third party may be used to settle consumer differences. Mediation involves the use of a third party who tries to resolve the complaint between the consumer and the business. A mediator suggests a compromise between the two parties. This process helps the parties work out their own mutually agreeable solution to the dispute.

If the parties agree to it in advance, another third-party action may be used. Arbitration results in a decision that is legally binding. After hearing both sides and considering evidence, the arbitrator makes a decision. Both the consumer and business must abide by the arbitrator’s verdict.

Class Action Suits

What would you do if you are overcharged a couple of dollars? Maybe nothing, but what if this same injustice occurred to thousands of consumers? A class action suit is legal action by one party on behalf of a group of people who all have the same grievance. In this type of lawsuit, one person or a small group represents the interests of many others (the class). The settlement may result in a refund to all consumers involved. If they cannot all be identified, the funds are sometimes given to public education programs or schools.

Name some benefits of joining a class action suit rather than trying to win a case alone.
Small Claims Court
In every state, a court system exists to resolve cases involving small amounts. These courts are called small claims court. In these courts, disputes are resolved quickly and inexpensively.

The rules are simple and informal, and the dispute involves less than a set amount. The limits for cases heard in small claims court vary by state. The amount ranges from less than $1,000 in some states to $10,000 in others.

Most often, lawyers are not involved. Individuals present the facts of the situation and provide written and other evidence. Witnesses may also be used.

Using a Lawyer
If all else fails, a final step might be to hire a lawyer. When a situation involves larger amounts of money or severe injuries from a product, the use of an attorney may be appropriate. Information about potential lawyers may be obtained from advertisements or referrals from other people.

Before using the services of a lawyer, you should ask various questions. Is the lawyer experienced in this type of case? Will you be charged a flat fee or an hourly rate? When will you be required to make payment for services?

15-3 Assessment

**Key Concepts**
 Determine the best answer.

1. Most consumer complaints are resolved by
   a. taking legal action
   b. using arbitration
   c. hiring a lawyer with consumer protection experience
   d. returning to the place of purchase

2. A company refused to refund $10 to over 4,000 customers. This situation might result in the use of
   a. mediation
   b. arbitration
   c. a class action suit
   d. small claims court

**Make Academic Connections**

3. Visual Communication Create a poster or other visual that communicates the four steps in the consumer complaint process. Use a specific consumer problem as the basis for your visual presentation.

4. Research Use library materials or an Internet search to determine the small claims court limit amount in your state. Also, obtain information about filing a case in small claims court.
**Business Notes**

**15-1 Consumer Buying Decisions**
1. The main sources of consumer information are product-testing organizations; media sources such as print publishers, broadcast organizations, and the Internet; government agencies; business sources such as product labels, customer service departments, and Better Business Bureaus; and personal contacts.
2. Comparison shoppers will evaluate price, quality, service, sales, and brands when making a purchase. Wise consumers take their time when making purchases, buy when prices are lowest, and avoid impulse buying with shopping lists.
3. The main shopping locations used by consumers can be viewed in three categories. Traditional retailers include department stores, discount stores, specialty stores, supermarkets, and convenience stores. Contemporary retailers include specialty superstores, warehouse clubs, and factory outlets. Non-store shopping options include door-to-door, mail order, phone, computer, and vending machines.

**15-2 Consumer Rights and Responsibilities**
4. The consumer movement emerged to fight unfair business practices. Because of this movement, public and private agencies, policies, laws, and regulations were developed to protect consumer interests.

5. The Consumer Bill of Rights declares that every consumer has the right to be informed, to safety, to choose, to be heard, to a remedy, to consumer education, and to service. Being a skilled consumer means that you know the Consumer Bill of Rights and how to exercise these rights.
6. Consumers also have responsibilities in business relationships. The five basic responsibilities of consumers are to be honest, to be reasonable, to report unethical practices, to be informed, and to be involved.

**15-3 Consumer Protection Actions**
7. The main consumer complaints are related to automobiles, deceptive investments, identity theft and consumer credit, telemarketing and catalog sales, work-at-home schemes, contests, vacation promotions, phony diets, and buying online.
8. Four steps are suggested when encountering a consumer problem: (1) contact the place of purchase, (2) contact the company headquarters, (3) involve a consumer agency, and (4) take legal action.
9. A variety of legal actions is available to help consumers. Mediation and arbitration involve the use of a third party to resolve a consumer complaint. Class action suits allow a small group of consumers to act on behalf of many. Small claims court allows a person to take legal action without the use of a lawyer.

**Communicate Business Concepts**

1. Why do you think most businesspeople like to have well-informed customers?
2. Do you go through all of the steps of comparison shopping on every purchase you make? Explain.
3. List factors you might consider when evaluating the usefulness of a consumer information source.
4. If you were planning to buy a microwave oven, what information sources might be most valuable?
5. One autumn day, a woman and a man came to Carrie Franklin’s door. They said they were chimney sweeps and would like to clean her chimney before she began using her fireplace. The man said it would be inexpensive and make her home safer, reducing the chances of
a chimney fire. Mrs. Franklin looked out her window and saw the name “Chim Chim Chimney Sweeps” on their truck. How can she find out if the firm is reliable?

6. When would you consider an impulse purchase a harmless activity?

7. What are some factors you might consider when deciding where to shop?

8. Which of the consumer rights have you recently used?

9. Why, with all of the laws and organizations to protect consumers, do you continue to hear of examples of consumer fraud?

10. Which of the following situations would be considered fraud? Why?
   a. A salesperson says the sound system you are looking at is the best on the market. After you buy it, you find it rated in a consumer magazine as second best.
   b. An advertisement for a bookcase cabinet claims it is made of solid walnut. Upon close inspection after buying the bookcase, you see that it is only walnut veneer glued over less expensive plywood.
   c. The person who sells an electric corn popper says it is completely washable. Before using it, you put it into a sink filled with water to wash it. The first time you try to make popcorn, there is a flash and the popper’s electrical unit catches fire. When you return the popper to the store, the salesperson tells you that she did not mean the popper could be put under water. She says you should have known that electrical appliances should not be put in water. She refuses to give you either a refund or an exchange.

11. Describe situations in which a person might use (a) a class action suit and (b) small claims court.

12. When might you use a lawyer to resolve a consumer dispute? What are some of the pros and cons of using a lawyer versus other dispute resolution methods?

>> Develop Your Business Language

Match the terms listed with the definitions.

13. Use of a third party who attempts to resolve the complaint between a consumer and business.


15. A name given to a product or service to distinguish it from other similar products or services.

16. A legal system for resolving cases involving small monetary amounts.

17. The price per unit of measure of a product.

18. When false information is given to a customer in an effort to make a sale.

19. A lawsuit brought by one party on behalf of a group with the same grievance.

20. Guarantees made orally or in writing that promise a specific quality of performance.

21. Third-party settlement resulting in a decision that is legally binding.

22. A promise by the manufacturer or dealer, usually in writing, that a product is of a certain quality.

23. Guarantees imposed by law that are not stated orally or in writing and that require certain standards to be met.

24. Banding together of consumers to demand fair treatment from businesses.

Key Terms

a. arbitration
b. brand
c. class action suit
d. consumer movement
e. express warranty
f. fraud
g. guarantee
h. implied warranty
i. impulse buying
j. mediation
k. small claims court
l. unit price
Decision-Making Strategies

Pierre needs a new digital camera to take on his trip to Mexico as an exchange student. He is not a photography expert, but he has taken some pictures for the school newspaper. He intends to use the camera to take indoor and outdoor pictures of people as well as scenery.

Pierre has about $150 to spend on the camera. He wants the camera to be sturdy, easy to use, and to take good-quality pictures.

What sources of information could Pierre use to find out what cameras are in his price range?

What two sources of information do you believe are best? Why?

Make Academic Connections

27. LAW Prepare a summary of various federal consumer agencies and laws designed to protect consumers related to product safety, motor vehicles, food, medical products, and consumer credit.

28. VISUAL COMMUNICATIONS Select a magazine advertisement. Create a poster describing various elements of the ad. Highlight the sections of the ad that would be useful or deceptive to consumers.

29. CULTURAL STUDIES Interview two people who have visited or lived in another country. How is shopping different in that country? How are consumer rights and responsibilities different in that country?

30. MATH Conduct a survey of consumers regarding the places they shop most frequently and the reasons for shopping there. Prepare a statistical summary of your findings by creating tables and graphs.

31. RESEARCH Collect examples of advertisements with the word “sale” included. Group the ads into categories based on the type of sale being displayed. What types of sales are most common?

32. ART Design a label for a food product with your own brand, product name, graphics, nutritional information, and other features.

33. MATH Berri purchased a new cell phone that stopped working one month after the warranty expired. When she returned to the store, she was offered the choice of purchasing a new phone for 5 percent off the list price of $98 or a reconditioned phone that carried the same warranty as a new phone for $75.

a. What would be the price of the new phone with the discount?
b. What percent of the price of a new telephone is the price of the reconditioned phone?
c. How much money would Berri save by purchasing the reconditioned phone?

34. LAW Conduct library research or an online search to obtain information about different types of implied warranties. How do these guarantees that are not directly stated protect consumers?

35. CULTURAL STUDIES Examine the label attached to several items of clothing. What information is provided on these tags? How does this information benefit consumers? Create a list of the countries that are the source of these items.

36. TECHNOLOGY Conduct an online search of Internet frauds. What types are most common? How can a person avoid these deceptive online business practices?

37. MATH The Jones family ordered a new car from Germany. The express warranty said the average driver would get 48.3 kilometers for every 3.85 liters of gasoline used.

a. How many miles per gallon is this?
b. If they traveled 90 miles and used 10.5 liters of gas, did the car perform better or worse than the warranty claimed?

38. HISTORY Conduct research on the way that people shopped in the 1800s to mid-1900s. Comment on some of the cultural, geographic, economic, and social factors that contributed to these customs.
> > Linking School and Home

Talk to people about the types of consumer problems they have encountered. What was the nature of the situation? What actions did they take to resolve the problem? What suggestions do they have for other consumers? Prepare a short written or oral summary of your findings.

> > Portfolio Activity

To provide tangible evidence of your learning about consumer buying, do the following:

**COLLECT** information about a major product you might purchase in the future. First, identify the specific product. Next, obtain advertisements, catalogs, articles, product comparisons, prices, consumer comments, and online information.

**CREATE** a table comparing brands, prices, features, shipping costs, and other factors you would consider when buying the product. In your table, present a summary of locations where the item might be purchased.

**CONNECT** your table findings to other items already in your class portfolio, or relate the table data to a concept from another class. Show the relationship of your research to other economic or social aspects of society. Prepare a one-paragraph summary of your research findings and other observations about comparison shopping.

Global Marketing Team Event

Marcella is interested in providing nutritious meals that are easy to prepare. She has created a line of meals called Marcy’s Gourmet. These meals do not require freezing. Each meal takes into consideration a well-balanced diet. Selections include meat and vegetarian choices. Each meal takes five minutes to prepare in a microwave or 20 minutes in an electric oven. Prices for Marcy’s Gourmet meals range from $3.00–$5.00.

Your team of two will develop an international marketing plan for this new product. The marketing plan must not exceed 10 single-spaced pages. Team members will present before a panel of judges (class members) and a timekeeper. The length of the presentation will be no more than 10 minutes. The completed plan should include, but is not limited to: Title Page and Table of Contents, Synopsis or mini-plan, Company Goals, Description of Customers and Their Needs, Description of Pricing Strategy, Competition, and Price Selection Methods.

**Performance Indicators Evaluated**

- Develop an international marketing plan.
- Identify a customer base, including consumer and organizational markets.
- Illustrate fundamentals of consumer behavior in different cultures.

You will be evaluated for your

- Knowledge of demographics in the international market
- Understanding of the marketing mix
- Understanding of economic, social, legal, and technological trends
- Use of appropriate research and accompanying documentation
- Description of timeline for business success

For more detailed information about performance indicators, go to the BPA web site.

Think Critically

1. Can the product be a success in America, internationally, or both?
2. What groups of individuals will this product appeal to (consider gender, age, education, and income)?
3. What is the most appropriate method of distribution for this product?
4. What demographic and cultural issues must be considered when marketing this product?
5. Will the name “Marcy’s Gourmet” have any effect in the international marketplace?
Planning a Career in...

Financial Planning

“How much should I save for retirement?”
“What is the best type of life insurance for my family situation?” “What actions can I take to reduce the amount of debt I owe?”

These and many other questions are answered by people who work in personal financial planning. Employment in this field has a wide range of opportunities. Your work may involve financial planning activities within a company with hundreds of employees. Or, you might work for a social service agency that helps people avoid financial difficulties as a result of a job loss or illness.

Employment Outlook

- Faster than average growth in employment is expected as the personal financial choices faced by people become more complex.
- Employment of financial analysts in large firms will grow as fast as the average for most occupations.
- Jobs for community-based and nonprofit budget counselors will expand as various economic conditions and personal situations result in needed services.

Job Titles

- Credit Counselor
- Budget Advisor
- Certified Financial Planner
- Financial Data Analyst
- Personal Financial Advisor
- Family Money Management Counselor
- Tax Preparer

Needed Skills

- Knowledge in accounting, finance, economics, and other business fields
- Communication skills
- Continuing education, especially in taxes and estate planning laws
- Certification of financial planning competencies, available from the Certified Financial Planner Board of Standards and other organizations

What’s it like to work in ... Financial Planning

At 8 a.m., Carl leaves for work, in the next room. Carl runs a personal financial planning business out of his home. This morning he is reviewing the files of several clients before advising them about various personal financial decisions. Then it’s time to get on the road. At 10 a.m., Carl is scheduled to meet with a person who just retired but does not have enough income to cover current living expenses. At noon, he meets with several small business owners who want to create a retirement fund for their employees.

The afternoon is open so Carl can relax or take care of personal errands. In the evening, things get busy. Right after dinner, Carl meets with a family who wants to create a savings and investment program to set aside funds for their children’s college education. His day ends with a phone call from a client who has a question about recent tax law changes.

What about you? What personal financial situations might result in a need for hiring someone trained as a financial planner or budget counselor?
MONEY MANAGEMENT BASICS

Right now $1,000, or maybe $100, seems like a lot of money to you. Once you graduate from high school, and perhaps college, and have a full-time job, your thinking about what is a large amount of money will change. You probably will earn well over one million dollars in your lifetime. As a college graduate, you will likely make even more.

While this may seem like a lot of money, remember that you will be responsible for many living expenses. You will have to pay for food, housing, clothing, and transportation as well as other goods and services you need and want. Upon beginning a career and living on your own, you will face the same problem you face now—having a limited amount of money to pay for all the goods and services you want and need.
Money management refers to the day-to-day financial activities associated with using limited income to satisfy your unlimited needs and wants. Money management involves getting the most for your money through careful planning, saving, and spending. It involves making and using a plan for spending.

Some people have the wrong idea about money management. They think it means never spending, doing without things, and not having any fun. If you learn to manage your money well, you will be able to buy what you really want. Planning ahead and deciding what is important will help you have money for things you enjoy. If you set goals, make wise decisions, buy wisely, and live within your income, you will be a successful money manager.

The process of good money management should start with knowing your current financial status. When watching a baseball or soccer game, most people want to know the score. In the money management game, score is kept with the use of two financial statements: the balance sheet and the cash flow statement.

**PERSONAL BALANCE SHEET**

“How much money do you have?” might be the first question many people would ask when measuring your financial situation.

The answer to that question would not give the entire picture since most people have other items of value besides money. A balance sheet is a record of assets and liabilities at a point in time. It reports what a person or family owns as well as owes. The main parts of a balance sheet are displayed in Figure 16-1.

**Assets**

Items of value are personal assets. Assets include such things as money in bank accounts, investments, furniture, clothing, automobiles, jewelry, and rare coins. The current value of all assets of an individual or family is the first thing stated on a balance sheet.

**FYI**

According to the Bureau of the Census, the main assets of U.S. households are motor vehicles, homes, savings accounts, U.S. savings bonds, certificates of deposit, mutual funds, stocks, corporate bonds, and retirement accounts.

**CHECKPOINT**

What are some characteristics of a wise money manager?

What accounts for the bulk of this family’s assets, liabilities, and equity?

<table>
<thead>
<tr>
<th>Personal Balance Sheet</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assets</strong></td>
<td><strong>Liabilities</strong></td>
</tr>
<tr>
<td>Checking account</td>
<td>Home mortgage $45,000</td>
</tr>
<tr>
<td>Savings account</td>
<td>Credit card balance 230</td>
</tr>
<tr>
<td>Home</td>
<td>Education loan 1,800</td>
</tr>
<tr>
<td>Automobile</td>
<td>Total liabilities $47,030</td>
</tr>
<tr>
<td>Household items and furniture</td>
<td></td>
</tr>
<tr>
<td>Personal computer</td>
<td>Owner’s Equity (Net Worth)</td>
</tr>
<tr>
<td>Jewelry</td>
<td></td>
</tr>
<tr>
<td><strong>Total assets</strong> $113,250</td>
<td>Total assets – Total liabilities $66,220</td>
</tr>
</tbody>
</table>
Liabilities
Amounts owed to others are liabilities. These debts may include credit card balances, automobile loans, a home mortgage, or personal loans. A listing of your liabilities is the second item on a balance sheet.

Net Worth
The difference between a person’s assets and liabilities is your net worth. This difference represents the amount of money that could be claimed if all assets were sold for cash and all debts were paid off. For example, if a family has $189,000 in assets (including the value of a home and other valuables) and has $87,000 in debts (mainly their home mortgage), the family has a net worth of $102,000.

Cash Inflows
The first part of a cash flow statement reports cash inflows, or your income. Cash inflows is the money you have available to spend as a result of working or from other income, such as interest earned on your savings.

When preparing a cash flow statement, first report your net income or take-home pay, which is the amount of a paycheck after taxes and other payroll deductions. These deductions may include retirement contributions, charges for health benefits, and other things, as well as local, state, and federal taxes. Your take-home pay is the amount you actually have available to spend. Be sure to include any other income, such as interest.

Develop a personal cash flow statement.

Many people have more cash outflows than inflows, resulting in financial difficulties. In your group, create a list of actions that a person or household might take to make sure cash outflows are less than cash inflows.

Work as a Group

Make a list of ways to increase your current cash inflows.
Cash Outflows
Keep a record of all spending so you can report your cash outflow. Amounts spent for food, clothing, transportation, and other living costs are cash outflows. Keeping track of how much is spent for various living expenses will help you plan and control your spending. Your personal cash flow statement can be used to develop a budget, which can help you avoid cash flow problems.

Compare Inflows and Outflows
The final step in preparing the cash flow statement is to subtract the cash outflows (total spending) from the cash inflows (total income). If you spent less than you had in income, the difference represents an increase in your net worth. Most likely, this amount will be kept in savings for future needs or wants. If you spent more than you had in income, you either had to use some of your savings or had to use credit to pay these additional expenses.

Figure 16-2
What percentage of total income did this person spend on basic needs?

<table>
<thead>
<tr>
<th>Personal Cash Flow Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash Inflows (Income)</td>
</tr>
<tr>
<td>Net income (take-home pay)</td>
</tr>
<tr>
<td>Other income (interest)</td>
</tr>
<tr>
<td>Total Income</td>
</tr>
<tr>
<td>Cash Outflows (Expenditures)</td>
</tr>
<tr>
<td>Rent</td>
</tr>
<tr>
<td>Food</td>
</tr>
<tr>
<td>Clothing</td>
</tr>
<tr>
<td>Utilities</td>
</tr>
<tr>
<td>Telephone</td>
</tr>
<tr>
<td>Transportation</td>
</tr>
<tr>
<td>Personal care</td>
</tr>
<tr>
<td>Recreation/entertainment</td>
</tr>
<tr>
<td>Total Spending</td>
</tr>
<tr>
<td>Net Cash Flow</td>
</tr>
</tbody>
</table>

CHECKPOINT
What do cash outflows represent?

16-1 Assessment

Key Concepts
Determine the best answer.

1. Savings accounts and a home are examples of
   a. liabilities
   b. assets
   c. net worth
   d. cash outflow

2. A payment for rent represents
   a. a cash inflow
   b. a cash outflow
   c. a liability
   d. an asset

Make Academic Connections

3. Math Calculate the missing amount.
   a. Assets $7,000
      Liabilities $1,800
      Net worth __?__
   b. Assets $26,000
      Liabilities __?__
      Net worth $19,000
   c. Assets __?__
      Liabilities $5,600
      Net worth $67,800

4. Research What types of liabilities are commonly listed on the personal balance sheets of households in the United States?
Imagine trying to do business in a country with more than 250 languages and ethnic groups. In Nigeria, the most populous country in Africa, you are likely to encounter a variety of business situations.

When in Nigeria, you will conduct important business in face-to-face meetings. In these settings, you may see Nigerian businessmen wearing a suit and tie. Or, they might wear traditional clothing such as a buda, a loose-fitting shirt that extends to the knees.

As you greet business associates in Nigeria, remember that formal titles are very important. Be ready to address someone as “Chief,” “Prince,” or “Alhaji.” Respect for older persons is vital. It is offensive in Nigerian society to pass an elderly person without a greeting. Handshakes are the most appropriate greeting.

At the first meeting with a business contact, be patient and expect many ongoing greetings. At first the conversation might seem overly personal, because Nigerians like to know the people with whom they are doing business.

If you are having lunch with a business acquaintance, make sure you always use your right hand (or both hands) to pass and accept dishes. The left hand is taboo and is rarely used for interpersonal transactions. Left-handers are especially advised to practice the use of their right hand. Foods that you will likely encounter include yams, cassava (a starchy root), and rice. Meats you are offered might range from beef, chicken, and turkey to goat, goose, and fish.

Nigeria is one of the world’s largest oil producers. Due to political turmoil and unstable financial conditions, the country has continually faced economic difficulties. The informal economy (also called the underground economy) accounts for over half of the business activities in Nigeria. Extensive numbers of workers make their living in unregulated settings. The items they produce and sell create income not reported to the government.

**Think Critically**

1. How does doing business in Nigeria differ from doing business in other countries?
2. What are the benefits and concerns related to informal economic activities?
3. Conduct library or Internet research to obtain additional information about business and economic activities in Nigeria.
Budgeting Techniques

Goals
> Identify purposes of a budget.
> Describe steps for preparing a budget.
> Describe characteristics of successful budgeting.

Key Terms
fixed expenses
variable expenses
allowance
budget variance

Focus on Real Life
Jing Fang is a Chinese American who has been practicing his Chinese through written communication with relatives in Hong Kong. He also has taken several business courses in high school. Jing hopes to have a career in international business working in the Pacific Rim countries.

“I can’t wait to go to Taiwan next summer, but the trip is going to cost me a fortune! The air transportation, housing, food, and other living expenses will cost $4,000. My parents have agreed to pay half. Fortunately for me, I developed a plan to save money for this trip. I have well over the $4,000 I need to go to Taiwan. It’s going to be a great experience. Hey Josh, why don’t you go with me?”

“Are you kidding? I’m not as disciplined as you! I would never be able to save enough money. You are a pro at managing money. Maybe you can give me a few tips.”

BUDGET ACTIVITIES
A budget allows you to meet your personal goals with a system of saving and wise spending. By developing a plan for saving and spending income, you will be able to make wise and rewarding personal economic decisions. The main purposes of a budget are to help you do the following:

- Live within your income.
- Achieve your financial goals.
- Buy wisely.
- Avoid credit problems.
- Plan for financial emergencies.
- Develop good money management skills.

Having a written budget is a key phase of successful money management. Your budget may be a simple record of how much you make, how much you want to save. On the other hand, your budget may be a more detailed record with specific amounts to be spent in categories such as food, clothing, and transportation. A good budget should take very little of your time, but it should provide needed information on your spending and savings plans.

Make a list of items you buy regularly. How might you start spending less on these items?

CHECKPOINT
What are the main purposes of a budget?
THE BUDGET PROCESS

The process of creating and using a budget involves four main steps.

1. Set financial goals.
2. Plan budget categories.
4. Evaluate your budget.

Any individual, family, or organization can use these steps to aid them in using available financial resources.

Set Financial Goals

Setting financial goals is the first step for any financial action. Goals point to where you would like to be financially so you can develop your budget accordingly.

Writing down short-term and long-term goals will help you decide how to spend and save your money. If your goals include going to college, your budget will require more for savings. If you are currently working at a job that requires you to spend a large amount for transportation, you will likely budget more for this item.

Plan Budget Categories

Most financial advisers recommend that an amount be set aside for savings as the first part of a budget. If savings are not considered first, other expenses may use all available income.

After savings, two other types of living expenses must be considered: fixed and variable expenses. Fixed expenses are costs that occur on a regular basis and are for the same amount each time. Examples of fixed expenses are rent, mortgage payments, and insurance premiums.

Variable expenses involve living costs that differ each time and may not be as easy to estimate. These types of expenses include food, clothing, and utilities (such as telephone and electricity). Some variable expenses, such as medical and dental costs, occur less often and may be large when they do occur. Such expenses must be provided for in the budget.

The amount budgeted for savings and other expenditures is referred to as an allowance. An allowance is the amount of money you plan to use for a certain budget category. While the budget categories can vary for different situations, eight main divisions are commonly used.

1. Savings  Savings accounts, government bonds, stocks, and other investments
2. Food  Food eaten at home and meals eaten away from home
3. Clothing  Clothing, shoes, dry cleaning, and repairs
4. Household  Rent, mortgage, property taxes, insurance, utilities, furnishings, household supplies, painting, and repairs
5. **Transportation**  Auto payments, insurance, operating costs, maintenance, repairs, and public transportation

6. **Health and Personal Care**  Medical and dental expenses, medications, eyeglasses, health insurance, and personal care costs

7. **Recreation and Education**  Books and other reading materials, theater tickets, concerts, vacations, school expenses, hobbies, and club dues

8. **Gifts and Contributions**  Charitable contributions and personal gifts

At this point, ask yourself, “How much should I set aside for each category?” Planned spending for various budget categories will depend on income, family size, ages of children, cost of living in your area, and work-related expenses. It will also depend on personal values, needs, and goals. A cash flow statement can help you develop budget categories. This financial statement reports the categories in which your money has been spent. It provides a basis for your budget.

Other help for developing a budget can come from government reports on family spending or from articles in magazines, such as *Kiplinger’s Personal Finance* and *Money*. An example of a family budget for one month is shown in Figure 16-3.

---

**Figure 16-3**

What percentage of income have the Chungs budgeted for savings? Do you think that’s enough?

<table>
<thead>
<tr>
<th>Chung Household</th>
<th>Family Budget for One Month</th>
</tr>
</thead>
<tbody>
<tr>
<td>Monthly Budget</td>
<td></td>
</tr>
<tr>
<td>January, 20--</td>
<td></td>
</tr>
<tr>
<td><strong>Estimated Income</strong></td>
<td>** Estimated Expense**</td>
</tr>
<tr>
<td>Manuel's net income $4,225</td>
<td>Savings $2,225</td>
</tr>
<tr>
<td>Lydia's net income 4,350</td>
<td>Food 1,100</td>
</tr>
<tr>
<td></td>
<td>Clothing 475</td>
</tr>
<tr>
<td></td>
<td>Household 1,825</td>
</tr>
<tr>
<td></td>
<td>Transportation 1,275</td>
</tr>
<tr>
<td></td>
<td>Health &amp; personal care 450</td>
</tr>
<tr>
<td></td>
<td>Recreation &amp; education 800</td>
</tr>
<tr>
<td></td>
<td>Gifts &amp; contributions 425</td>
</tr>
<tr>
<td><strong>Total income</strong> $8,575</td>
<td><strong>Total Expenses</strong> $8,575</td>
</tr>
</tbody>
</table>

---

**FYI**

A once-popular system for family budgeting required envelopes marked with labels of different expenses such as “Food,” “Housing,” and “Automobile.” Each envelope contained the budgeted amount of money, and expenses were paid from the money in the envelopes. This system allows a person to see where the money is going. Unfortunately, a danger exists with keeping large amounts of cash at home.
Maintain Financial Records

After planning a budget, individuals and families should record their income and expenses to find out if the plan is working. An example is shown in Figure 16-4. The first line shows the monthly income available to the family ($8,575 after taxes and other paycheck deductions) and the budget allowances for each category.

During the month, entries for expenditures were recorded. Since the family pays most bills by check, a checkbook is an easy reference for the information needed to prepare the income and expense summary.

Evaluate Your Budget

All columns were totaled at the end of the month. Actual spending is compared with the budgeted amounts. Any difference between these amounts is a budget variance.

If actual spending is greater than planned spending, such as for the “Household” category, it is referred to as a deficit. When actual spending is less than the budgeted amount, as with the “Food” category, a surplus occurs.

A category-by-category comparison allows you to find areas where changes in the budget may be appropriate. A variance in the actual amount spent and the budgeted amount does not always mean a change in your spending plan is necessary.

Your budgeted amount may still be appropriate with a slight deficit or surplus occurring every few months in some categories. If you expect necessary higher or lower spending in a certain category, a change in your budget is probably needed.

SUCCESSFUL BUDGETING

Effective budgeting will be an ongoing learning process for you.

Characteristics of an Effective Budget

The following are common characteristics of a successful budget.

- **Must be realistic.** It should reflect current income and planned spending.
- **Should be flexible.** When unexpected expenses arise, your spending plan should be able to adapt for these living costs.
- **Should be evaluated regularly.** Every few months, evaluate the budget to determine whether it still is appropriate.
- **Must be well planned and clearly communicated.** All family members should discuss financial goals, wants and needs, and plans for spending.
- **Should have a simple format.** If it is too detailed and difficult to understand, family members may not be willing to use the spending plan.

What kinds of adjustments would you have to make to live within a budget?
In which categories did the Chung’s expenditures exceed the amount they had budgeted? In which were they less than the amount budgeted?

### Chung Household

#### Income and Expense Record

<table>
<thead>
<tr>
<th>Date</th>
<th>Explanation</th>
<th>Totals</th>
<th>Distribution of Savings and Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Receipts</td>
<td>Payments</td>
</tr>
<tr>
<td></td>
<td>Budget</td>
<td>$8,575.00</td>
<td>$2,225.00</td>
</tr>
<tr>
<td>January</td>
<td>Balance</td>
<td>1,300.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Manuel’s net income</td>
<td>2,112.50</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Lydia’s net income</td>
<td>2,175.00</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td></td>
<td>$2,225.00</td>
<td>$2,225.00</td>
</tr>
<tr>
<td>7</td>
<td></td>
<td>1,075.00</td>
<td>210.00</td>
</tr>
<tr>
<td>14</td>
<td></td>
<td>950.00</td>
<td>230.00</td>
</tr>
<tr>
<td>15</td>
<td>Manuel’s net income</td>
<td>2,112.50</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Lydia’s net income</td>
<td>2,175.00</td>
<td></td>
</tr>
<tr>
<td>17</td>
<td>Mortgage payment</td>
<td>1,200.00</td>
<td></td>
</tr>
<tr>
<td>21</td>
<td>Car payment</td>
<td>850.00</td>
<td></td>
</tr>
<tr>
<td>22</td>
<td></td>
<td>925.00</td>
<td>200.00</td>
</tr>
<tr>
<td>29</td>
<td></td>
<td>1,055.00</td>
<td>300.00</td>
</tr>
<tr>
<td>31</td>
<td>Totals</td>
<td>$9,875.00</td>
<td>$8,280.00</td>
</tr>
</tbody>
</table>

#### February

<table>
<thead>
<tr>
<th>Date</th>
<th>Explanation*</th>
<th>Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Balance*</td>
<td>$1,595.00</td>
</tr>
</tbody>
</table>

*Balance = January’s total receipts - total payments = $9,875.00 - $8,280.00
Types of Budgeting Formats
Most money management software programs have a budgeting feature. They allow you to develop a budget, keep track of your accounts, and pay your bills. They may also aid in financial planning. Such software often can be linked to income tax software programs so that annual tax forms can be completed faster.

While handwritten or computerized budgets are most common and usually the most appropriate, some people believe a checkbook is an effective budgeting system. Be aware that a checking account does not serve the purpose of planning for spending. Your checks are a record of purchases and paid bills. You still need a plan for using income.

Others say they keep their budgets in their heads rather than on paper. This simple system may work for an individual with limited income and few financial commitments. A family with a larger income and more living expenses would find it ineffective. A person with a mental budget also risks forgetting how much is to be spent or has been spent on certain items.

Assessment

1. True or False. Retirement planning is usually considered a short-term goal.
2. A major purpose of a budget is to
   a. assist with comparison shopping
   b. achieve financial goals
   c. reduce a person’s enjoyment of life
   d. gather data for using credit cards
3. The most uncertain aspect of the budgeting process involves
   a. estimating variable expenses
   b. determining net worth
   c. estimating fixed expenses
   d. setting financial goals
4. Math Mary and Fred James budgeted $340 a month for groceries. During the month, they spent $87, $93, $38, $61, and $52 at the supermarket.
   a. What was the total amount spent for food?
   b. Did Mary and Fred have a budget deficit or surplus? What was the amount?
5. Visual Art Talk to several people about various short-term and long-term goals they have had in their lives. Prepare a poster (or computerized presentation) with visuals, such as photos and other graphics, summarizing various types of goals, both financial and personal.
DEVELOPING A
FINANCIAL PLAN

To successfully reach financial goals, you must have a plan. Successful coaches have a game plan. Travel agents refer to vacation plans. Builders must have house plans. Successful consumers and businesspeople must have a financial plan. A financial plan is a report that summarizes your current financial condition, acknowledges your financial needs, and sets a direction for your future financial activities.

Financial planning includes evaluating one's financial position, setting financial goals, and guiding activities and resources toward reaching those goals. Everyone should have a carefully developed financial plan.

Your financial plan should include all that you know about good money management. This plan should be developed carefully. It should be evaluated and updated frequently. A well-developed financial plan can make your financial life more satisfying.

Focus on Real Life

“Hey Gloria, are you going to the Business Speakers Series monthly luncheon on Friday?”

“I really hadn’t given it much thought, Maria. Are you?”

“Yes! The speaker is from the local college and is supposed to be very dynamic and informative. The topic is financial planning, and if I am going to go to college, I need some help in planning right now! Why don’t you meet me there?”

“Great idea, Maria. I always thought of financial planning as something for people out of college. But it certainly makes sense to start now! I guess if I start planning early, I can get a head start on my future!”

Talk with an older person who started saving when he or she was your age. What can you learn from this person’s financial successes or mistakes?

Key Terms
- financial plan
- individual retirement account (IRA)
- estate planning

Goals
- Describe the financial planning process.
- Explain actions for implementing a financial plan.
- Identify actions for reviewing a financial plan.

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Describe the financial planning process.
Financial planning offers several specific advantages.

- Your financial uncertainties will be reduced.
- You will gain more control of your financial activities.
- Your family and household members will know more about your financial situation in case they need to assume control of your finances.
- Earning, spending, protecting, and saving your resources will be more systematic.

Financial Planning Process

Financial planning experts recommend the following steps.

1. **Analyze your current financial condition.** You should create a balance sheet and cash flow statement.
2. **Develop financial goals that are responsive to your vision.** What short-term and long-term objectives do you have? How much money will you need, and when?
3. **Create your financial plan.** This activity will require that you plan various actions for your saving and spending goals. This step may require help from a financial planner or other financial specialists.
4. **Implement the plan.** This may involve buying or selling property or investments, moving bank accounts, acquiring insurance, or any number of financial activities.
5. **Revise your financial plan.** As time goes on, you will frequently evaluate and revise your financial plan.

Financial Inventory

A financial inventory is a lot like a physician giving a physical exam. Just as the doctor’s exam calls for an assessment of your health, your financial inventory includes a careful review of your finances.

A financial inventory will usually include the creation of a personal balance sheet and cash flow statement. This process will provide information about your current financial position in terms of income, savings, investments, property, living expenses, insurance, and money owed.

Personal Financial Filing System

To keep your financial inventory and other records in order, you should create a personal financial filing system. Well-organized files are key to financial planning. These files should contain all of the documents and records related to such things as contracts, bills, receipts, bank balances, and legal papers. The files will become an invaluable resource to you as you progress with your financial planning. The contents may be organized in categories as shown in Figure 16-5 on the next page.

Financial Life Cycle

Most people’s lives follow a predictable pattern called a life cycle. Each stage of life is distinguished by unique characteristics, requirements, and expectations. For example, during the teen years, people are exploring career options, developing plans for independence, and evaluating future financial needs. In your twenties, you will likely train for a career, set up a household, and perhaps marry and have children.
A Filing System for Personal Financial Records

<table>
<thead>
<tr>
<th>Personal records</th>
<th>Money management records</th>
</tr>
</thead>
<tbody>
<tr>
<td>Birth certificate</td>
<td>Current budget</td>
</tr>
<tr>
<td>Social Security card</td>
<td>Personal balance sheet</td>
</tr>
<tr>
<td>Current resume</td>
<td>Cash flow statement</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Housing records</th>
<th>Tax records</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lease</td>
<td>Pay stubs, W-2 forms</td>
</tr>
<tr>
<td>Mortgage papers</td>
<td>Receipts for tax deductions</td>
</tr>
<tr>
<td>Property tax records</td>
<td>Income tax forms</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Consumer purchase records</th>
<th>Financial services and credit records</th>
</tr>
</thead>
<tbody>
<tr>
<td>Warranties</td>
<td>Bank statements</td>
</tr>
<tr>
<td>Receipts for major purchases</td>
<td>Certificates of deposit</td>
</tr>
<tr>
<td>Motor vehicle registration</td>
<td>Credit contracts</td>
</tr>
<tr>
<td></td>
<td>Monthly credit card statements</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Insurance records</th>
<th>Investment, retirement, and estate records</th>
</tr>
</thead>
<tbody>
<tr>
<td>Insurance policies</td>
<td>Investment account statements</td>
</tr>
<tr>
<td>Medical information</td>
<td>Pension plan information</td>
</tr>
<tr>
<td>Claim reports</td>
<td>Will, trust information</td>
</tr>
</tbody>
</table>

Later in life, you may decide to obtain additional career training or make plans for paying for children’s education. Then retirement plans, investing, and estate planning will likely become a priority.

Each life stage has financial matters that need attention. That attention can be provided through the development of a good financial plan. Remember, a good plan is one that is flexible and useful throughout several life stages.

**Using a Financial Planner**

Creating a financial plan is not a simple task. Doing your own financial planning requires time, information, and patience. Financial planners are professionals who can help you. A financial planner should have at least two years of training in securities, insurance, taxes, real estate, and estate planning and have passed a rigorous assessment.

Questions you might ask when choosing a financial planner include the following:

- What experience and training do you have?
- Are you willing to supply references from past clients?
- How are your fees determined?
IMPLEMENT A FINANCIAL PLAN

Implementing your plan may involve a wide variety of actions. You may need to move your savings to an account in which you will earn a higher interest rate. You may buy a bond. Maybe you will begin to work more hours at your part-time job to earn more money.

The list of financial planning actions can seem almost endless. For your plan to lead to achieving your financial goals, several common areas should be considered.

Insure Current Income
Protecting your income so that it contributes to your goals is a key financial planning action. Insurance is available that will provide an income to those who fear the two most common causes of loss of income: disability and unemployment.

Disability Income Insurance
To replace income that is lost when you cannot work because of an illness or injury, you can purchase disability income insurance. Many different disability income policies are available. Most disability income insurance will pay 60 to 70 percent of your salary while you are disabled. Before the benefits begin, there is usually a waiting period from one week to 90 days after you are disabled. Many employers provide this type of insurance.

Unemployment Insurance
Unemployment is another hazard to a financial plan. To reduce the financial hardship of unemployment, most states have an unemployment insurance program, operated in cooperation with the federal government. This coverage provides cash payments for a limited time to people who are out of work for a reason other than illness. A local unemployment office will provide guidance to help find a new job. If no suitable job is found, you may qualify for payments to replace part of your lost wages.

Plan for Future Income
The success of any financial plan also calls for a stream of future income. Once people retire, their salaries stop, but they continue to need money to cover living expenses. Workers can ensure that they will have enough income during their retirement years through Social Security, pensions, individual retirement accounts, and annuities.

Social Security
A key form of income protection comes through the federal government’s Social Security system called retirement, survivors, and disability insurance. This part of Social Security provides pensions to retired workers and their families, death benefits to dependents of workers who die, and benefits to disabled workers and their families.

Social Security benefits are funded by payroll taxes from both workers and employers. The taxes are deducted from employees’ paychecks. Employers match the amounts paid by their employees. Self-employed people, such as farmers and small business owners, pay the entire tax themselves.

When a worker retires, becomes disabled, or dies, monthly payments are made from the trust fund. The amount of benefits received depends on how long a worker was employed and how much a worker earned while employed.
Pensions  A pension is a series of regular payments made to a retired worker under an organized plan. Many employers offer plans that provide monthly payments to retired workers. Professional and trade associations or unions often establish similar plans. To qualify under most pension plans, you must work for the same organization for a minimum number of years. Many employees retire on pensions along with Social Security benefits.

Retirement Accounts  People can also develop their own retirement income plans. The most popular of these plans is the individual retirement account (IRA). An IRA is a tax-sheltered retirement plan in which people can annually invest earnings up to a certain amount. With traditional IRAs, contributions are tax-deductible. The investment gains are tax-deferred and the funds are taxed when they are withdrawn after age 59 ½.

With a newer version, called a Roth IRA, contributions are not tax-deductible. However, all funds, including any investment gains, are tax-free when withdrawn after age 59 ½.

Other types of retirement accounts include 401(k) and Keogh plans. The part of the U.S. federal tax code called 401(k) allows employers to offer a tax-deferred retirement plan. Tax-deferred means the investment earnings on this retirement plan will be taxed later, after retirement. A Keogh retirement plan is for self-employed workers and people who run their own businesses.

Annuities  An amount of money an insurance company pays (usually monthly) to a person who has previously deposited money with the company is called an annuity. This financial agreement is an investment plan for retirement income. You pay the insurance company a certain amount of money either in a lump sum or in a series of payments. In return, the company agrees to pay you a regular income beginning at a certain age and continuing for life or for a specified number of years.

REVIEW YOUR FINANCIAL PLAN
A financial plan must be flexible. View your financial plan as a changeable document. Your plan should be evaluated and adjusted on a regular basis to produce the outcomes you desire.

Revise Financial Goals
Once you have an understanding of changes in your financial or personal situation, you should consider changes in your financial goals. These goals may be short-term or long-term. They are usually stated in dollar amounts. An example of a short-term goal is “saving $1,000 in one year.”

CHECKPOINT
What are common sources of income during retirement?

How much money per month will you need to live comfortably when you are 65 years old? Where will this money come from?
This goal is simple, straightforward, and fairly short-term.

By contrast, long-term financial goals are often more complex and involve a longer period. These might include “owning my own home by age 30.”

Often, short-term goals may need to be given up in order to achieve long-term ones. For example, you may have to forgo buying a bicycle in order to save for an automobile.

**Review Financial Activities**

Changes in your goals will require changes in spending and saving habits. Although it seems a long time off, retirement is thought by many to be a vital part of financial planning. The chances are very good that you will spend many happy and healthy years in retirement. Those years will be happier and healthier if you have an adequate supply of money.

**Estate planning** involves the accumulation and management of property during one’s lifetime and the distribution of one’s property at death. These actions have two parts. The first consists of building your estate through savings, investments, and insurance. The second consists of planning for the transfer of your estate, at your death, in the manner that you wish.

**Remember to Save**

Money management and financial planning are ongoing activities. Every decision you make will affect both current spending and long-term financial security. The only way to have money in the future is to spend less than you receive. The overuse of credit and other poor spending habits are the basis for long-term financial disaster.

**Assessment**

**Key Concepts**

Determine the best answer.

1. A common source of retirement income is
   a. disability income insurance
   b. a mortgage
   c. pensions
   d. unemployment insurance

2. A long-term goal usually involves
   a. less than two years
   b. buying with a credit card
   c. using the services of a financial planner
   d. saving over many years

3. **Research** Use library or online research to determine common financial planning activities for different stages of life. Prepare a written summary or poster reporting your findings for people in their 20s, 30s, 40s, 50s, 60s, and older.

4. **Oral Communication** Conduct an interview with another student. Ask that person about her or his financial goals. Suggest actions to help the person achieve those goals.
Sharpen Your Life Skills

Effective Interviewing

As a job applicant, you will be interviewed. You will be asked questions to determine your experiences and knowledge. In contrast, your ability to interview others can be of value in several ways. Someday you may interview potential employees for a company. Or, you may interview people for information for class assignments or in work situations.

When conducting an interview to make a business decision or to obtain information, follow these guidelines.

1. Create four or five open-ended questions related to the topic to get the person talking.
2. Develop questions that cannot be answered with one or two words.
4. Listen for major themes or key ideas. Give the respondent time to answer. Don’t interrupt.
5. Use follow-up questions to obtain additional information.
6. Do not ask leading questions—ones that suggest an answer for which you are looking.

Probing and Clarifying

Two valuable interviewing techniques are probing and clarifying. Probing is a technique to obtain additional information from a respondent. Probing starts with careful questioning by the interviewer. Probing can be achieved with repeating a question. Probing phrases include:

- Anything else?
- Please tell me more.
- What do you mean by that?
- Why do you feel that way?

Clarifying is a process to get an explanation about an answer that has already been given. You want to know specifically what is meant by an answer. One clarifying technique is to ask, “What do you mean by...” and then repeat the respondent’s exact words. Another way to clarify is to ask the respondent to provide additional information about some response that has already been given.

Think Critically

1. What are situations in which your ability to interview others would be useful?
2. What actions could you take to improve your interview skills?
3. Conduct an interview to obtain information about a career, company, or country.
Business Notes

16-1 Personal Financial Statements
1. You can manage your money wisely by planning carefully, using information to help you better understand and take action on your money matters, comparing products and prices, and making wise decisions.

2. A balance sheet is a record of assets and liabilities at a point in time. Assets are items of value. Liabilities are amounts owed to others. Net worth is the difference between assets and liabilities.

3. A cash flow statement is a record of cash inflows (income) and cash outflows (payments for living expenses) for a given period, such as a month.

16-2 Budgeting Techniques
4. The main purposes of a budget are to help you live within your income, achieve your financial goals, buy wisely, avoid credit problems, plan for financial emergencies, and develop good money management skills. Having a written budget is an important phase of successful money management.

5. The process of creating and using a budget involves setting financial goals, planning budget categories, maintaining financial records, and evaluating your budget.

6. A successful budget will be realistic, flexible, evaluated regularly, well planned, clearly communicated to those involved, and in a simple format.

16-3 Your Financial Future
7. The five main steps in the financial planning process are to analyze your current financial condition, develop financial goals, create a financial plan, implement the plan, and evaluate and revise the plan over time.

8. Two key areas to consider when implementing a financial plan are protecting current income and providing for future income. Current income can be protected by disability income insurance and unemployment insurance. Sources of future income during retirement include Social Security, pensions, individual retirement accounts, and annuities.

9. When reviewing your financial plan, view it as a fluid, changeable document that will accommodate opportunity. You should revise financial goals as your financial or personal situation changes. Changes in your goals will require changes in spending and saving habits. Most importantly, remember to save. The only way to have money in the future is to spend less than you receive.

Communicate Business Concepts

1. Identify each of the following items as an asset or a liability:
   a. Money owed to the dentist
   b. An automobile
   c. Clothing
   d. Savings account
   e. Credit card balance
   f. Amount due for a personal loan
   g. 100 shares of stock

2. “If you only spend money on things you really need, you will always have money for the things you really want.” Do you agree with this statement? Explain your answer.

3. Describe the difference between short-term and long-term goals. Give two examples of each type.

4. What two actions could you take if your expenditures were consistently greater than your income?

5. Every week, Chris Thorson puts any amount he has not spent during the week into a savings account. If he needs more money than he has during a week, he withdraws it from his savings. Is Chris following a good money management plan? Explain.
6. Consider a family of four people: mother, a supermarket manager; father, a department store salesperson; and two children, ages 14 and 11.
   a. List four fixed expenses that this family would likely have each month.
   b. What are some variable expenses that they are likely to have?
   c. How are the family’s expenses different from those of other families with younger children or no children?
7. Why would you want to insure your income?
8. One financial planner has said, “Doing nothing about financial planning is equivalent to making a decision about financial planning.” What do you think she meant by this?

>> Develop Your Business Language

Match the terms listed with the definitions.

14. The difference between a person’s or family’s assets and liabilities.
15. A report that summarizes your current financial condition, acknowledges your financial needs, and sets a direction for your future financial activities.
16. Living costs involving differing amounts each time.
17. Accumulation and management of property during one’s lifetime and the distribution of one’s property at death.
18. Costs that occur regularly and are for the same amount each time.
19. A difference between actual spending and planned spending.
20. The financial statement that reports net wages and other income along with spending for a given period.
21. A tax-sheltered retirement plan in which people can annually invest earnings up to a certain amount. The earnings contributed and interest earned are tax-free until the funds are withdrawn.
22. Items of value.
23. The day-to-day financial activities associated with using limited income to satisfy your unlimited needs and wants.
24. The amount of money you plan to use for a certain budget category.

Key Terms
a. allowance
b. budget variance
c. cash flow statement
d. estate planning
e. financial plan
f. fixed expense
g. individual retirement account (IRA)
h. money management
i. net worth
j. personal assets
k. variable expense
> > Decision-Making Strategies

Joan Leitzel just graduated from college and got her first job as a speech therapist. Joan wants to make sure she manages her income wisely so that she can be independent and eventually buy a house on her own. She lives with her parents now, so her only expenses are payments on a college loan and an auto loan.

25. What advice would you give Joan if she wants to buy a house in the future?

26. When she eventually goes to the bank for a loan, how should Joan organize her financial information?

> > Make Academic Connections

27. **ECONOMICS** Use newspaper ads and web research to determine the current value of various assets such as homes, motor vehicles, jewelry, antiques, and rare coins.

28. **CULTURE** Conduct research using personal interviews and other sources to determine the main assets (possessions) of typical households in other countries.

29. **MATH** The Gage family’s assets total $268,400. Their total liabilities are $166,300. What is the amount of their owner’s equity? What actions could they take to increase their net worth?

30. **TECHNOLOGY** Conduct a web search for budget guidelines suggested for various categories of spending such as food, housing, transportation, clothing, health care, and others.

31. **RESEARCH** Locate in-store or online information about available money management software. Prepare a brief written summary comparing the prices and features of different programs.

32. **VISUAL ART** Create a flowchart to communicate the five steps of the financial planning process.

33. **RESEARCH** Conduct research to determine various professionals who might help you with your financial planning in the future. Prepare a summary table reporting the name, title, training and background, area of specialization, and cost of services for various financial planners.

34. **LAW** Obtain information about recent changes in Social Security taxes and benefits. Prepare a two- to three-paragraph summary.

35. **MATH** Use a spreadsheet analysis to calculate the value of $2,000 in savings a year for 10 years if the funds earn 8 percent a year. What would be the value of that savings after 40 years?

36. **HISTORY** Locate a copy of a budget or financial report for your school, church, city government, or a public company from at least five years ago, as well as a current copy. Compare the two budgets. Prepare a brief summary comparing assets, liabilities, and net income. Discuss what factors may have caused these differences.

37. **ECONOMICS** Interview fellow students, your parents, or other adults who are employed. Gather information about the deductions that are taken from their paychecks. Prepare a table listing the various deductions. Indicate which deductions are required and which are optional.

38. **PERSONAL FINANCE** Assume you have been given a three-year-old car. Research the monthly costs associated with owning a car, not including the cost of the car, as it was a gift. Include items such as insurance, license, local annual use taxes, cost of gasoline based on 10,000 miles per year, and regular maintenance costs.

39. **CULTURE** Select one city each in North America, South America, Europe, and Australia. Conduct web research to determine the per-person cost of an afternoon out with your friends in each city. Use the current exchange rate to convert the costs to U.S. dollars. Include items such as transportation (subway, taxi, or gas per gallon cost), lunch, a movie, and a new music CD. Present your findings in a table.
Linking School and Home

Talk with people in your home or neighborhood about their money management activities. What are their main budgeting concerns? How do they cope with these? What actions do they take to save money for the future? What types of investments do they recommend?

Portfolio Activity

To provide tangible evidence of your learning about money management and financial planning, do the following:

**COLLECT** examples of financial goals and financial planning activities for your life situation now and in the future.

**CREATE** a financial plan for your situation with the following sections: (1) a summary of current finances—assets, liabilities, monthly cash inflows, and monthly cash outflows; (2) a list of short-term and long-term financial goals; (3) a description of financial actions related to spending, saving, investing, and insurance. Show in a visual format (a flowchart or poster) the elements of your financial plan.

**CONNECT** your financial plan to other items already in your class portfolio, or relate the plan to an important concept you learned in another class. Make the connection by writing a one-paragraph discussion of how financial planning is affected by various economic, social, or political factors in our society.

Graphic Design Promotion

The banking industry has become highly competitive. Banks are constantly creating promotional brochures to attract the attention of new customers.

You have been hired by First Bank of America to design a promotional brochure telling about the bank's services. The bank offers free checking accounts for high school students and retired customers. Other customers who maintain a minimum balance of $500 at all times also receive free checking services.

Your bank provides money management and other financial services to customers. First Bank of America is open six days a week. The Monday-Friday hours are 9 a.m. – 7 p.m. and Saturday hours are 9 a.m. – 1 p.m.

Your final product may be black and white or color and printed on white or colored paper. All graphics must be computer generated. No copyright items may be used. Judges will have 10 minutes to ask participants about their brochures.

**Performance Indicators Evaluated**

- Use principles of design, layout, and typography in graphic design.
- Generate a promotional flyer for marketing purposes.
- Demonstrate knowledge of graphic design and rules for layout.
- Demonstrate effective use of color, lines, text, graphics, shapes, etc.
- Use appropriate artwork and design techniques to effectively illustrate a theme.
- Apply technical skills to manipulate graphics, artwork, and images.

For more detailed information about performance indicators, go to the BPA web site.

Think Critically

1. What do customers want from their banks?
2. Why have banking hours changed so dramatically?
3. Where is the best place to distribute promotional brochures for a bank?

http://www.bpa.org/
Chapter 17

Banking and Financial Services

17-1 Banks and Other Financial Institutions

17-2 Financial Services and Electronic Banking

17-3 Checks and Payment Methods
Planning a Career in...

Banking and Financial Services

The banking and financial services industry offers many career opportunities. Numerous financial workers are employed in commercial banks. Others work in specialized banks, savings and loan associations, credit unions, and finance companies. Work activities in the financial services industry range from serving customers and researching economic trends to planning marketing activities for financial institutions.

Employment Outlook

- Career opportunities in banking and financial services are expected to see continued growth.
- Slower growth is expected for certain banking jobs due to industry consolidation and technology.
- Employment of bank branch managers will grow very little as banks open fewer branches and promote electronic and Internet banking to cut costs.
- Electronic banking activities will also affect the need for employees with technology skills.

Job Titles

- Branch Manager
- Teller
- Head Teller
- Loan Officer
- Customer Service Representative
- Financial Services Sales Agent
- Financial Manager
- Information Processing Manager
- Economist

Needed Skills

- Entry-level jobs may require only a high school education, with college business courses needed for advancement.
- Bank officers, professional personnel, and executive positions require a college degree.
- Continuing education in cash management, financial analysis, and international banking should be considered.
- Interaction with customers requires strong communication skills and an ability to work well under stress.
- Accuracy, professional appearance, and computer competencies are vital for success.

What’s it like to work in...

Financial Services

Each morning, Ken Li goes online to see how various economic factors are affecting interest rates. He knows that when money is more expensive, borrowing by businesses and consumers declines. But if interest rates are lower, the use of credit will likely increase. This additional borrowing can result in higher earnings for banks.

Changing interest rates are just one area of research for Ken, who works for a bank with offices in 23 states. Today, he must also investigate current trends for employment, consumer spending, and retail sales. These economic indicators provide managers with information to better plan strategies for their banking organizations.

What about you? What knowledge of banking and financial services do you have that might be of value when selecting a career?
Banks and Other Financial Institutions

17-1

THE BANKING SYSTEM

Have you ever thought of a bank as a business and you as a customer? Many people do not think of banks in this way. Yet, a bank is a business just like a store or factory. As a business, a bank sells services such as checking and payment accounts, savings accounts, loans, and investments.

Banks are regulated more strictly than most other businesses. If a business fails, some people lose money. If a bank fails, thousands of people are affected.

The Federal Reserve System

One type of bank exists that will not allow you to make deposits. As an individual, you cannot open an account in a Federal Reserve Bank, which is a bank for banks.

The federal government set up the Federal Reserve System (Fed) to supervise and regulate member banks and to help banks serve the public efficiently. All national banks are required to join the Federal Reserve System, and state banks may join. Banks that join the

Focus on Real Life

“I finally got a job for the summer,” Gerri told Mike. “I can save money and go on that trip.”

“Where are you going to save your money?” asked Mike.

“At home, of course,” responded Gerri.

“Are you kidding?” Mike went on to say. “That’s dangerous! Your money can get lost, or you might spend it before summer comes.”

“Well, what should I do with my money?” asked Gerri.

“Deposit it in a bank,” answered Mike.

“Will it be safer?” asked Gerri.

“For sure,” said Mike. “Banks and other financial institutions provide safety and growth for your money. Plus they help their customers in many ways with other financial matters.”

“You’re kidding! I guess it’s time I learn about banking,” Gerri responded.

Key Terms

Federal Reserve System (Fed)
commercial bank
credit union
Federal Deposit Insurance Corporation (FDIC)
system are known as *member banks.* The United States is divided into 12 Federal Reserve districts, with a central Federal Reserve Bank in each district, as shown in Figure 17-1.

**Federal Reserve Activities**

A Federal Reserve Bank serves member banks and the economy in several ways. One service provided by the Fed is the holding of *reserves.* Banks cannot lend all of the money they receive from customers. They are required to keep a part of the money deposited by customers on deposit with the Federal Reserve System. The Fed holds these deposits in case the banks need additional funds to meet the daily customer demand.

As a result, a bank will lend only a certain percentage of deposited funds. It keeps the rest in reserve. This regulation is designed to help the banking system and the economy operate efficiently and to protect depositors.

For example, suppose a customer deposits $1,000 and the bank is required to hold 15 percent of all deposits in reserve. Since $\frac{100\%}{100} - 15\% = 85\%$, the bank can lend $\$850$ of the new deposit.

$$85\% \times \$1,000 = \$850$$

Another service of the Federal Reserve System is clearing checks in different cities. *Clearing* refers to the paying of checks among different banks in different cities. The Fed processes millions of checks each day to make sure that the correct amounts are added to and subtracted from the appropriate customer accounts.
Banking and the Economy
The actions of the banking system affect you in many ways. Several million people work in banks, savings and loan associations, credit unions, and other financial institutions. The following are some of the activities for which banking services are often used.
- Build homes
- Start new businesses
- Plant crops
- Finance educations
- Buy goods
- Pave streets
- Invest for retirement
- Build hospitals
- Buy new business equipment

The savings you and others deposit make banking services possible. Deposits do not remain idle in bank vaults. They are put to work. When you and others deposit money in a bank, you are helping to create jobs and economic growth that benefit your community and your society.

Check Point
What is the main purpose of the Federal Reserve System?

Types of Financial Institutions
When someone says, “I’m going to the bank,” the person might actually mean a credit union or a cash machine. There are many types of financial institutions that provide a wide range of products and services. Figure 17-2 shows how financial institutions are classified.

Deposit Institutions
Deposit institutions, also called depositary intermediaries, accept deposits from people and businesses and use them to finance their business.

Commercial Banks
The most common way for a bank to be organized is as a commercial bank. Commercial banks are often called full-service banks because they offer a wide range of financial services. Commercial banks offer checking accounts, provide savings accounts, make loans to individuals and to businesses, and offer other services. In large banks, different departments may handle these services. There may be a savings department, a trust department, a real estate department, and an investment department. Many banks have full-service branch offices in shopping centers and grocery stores.

Figure 17-2
Which of these types of institutions have you done business with?

Deposit & Non-Deposit Institutions

Deposit Institutions
- Commercial Banks
- Savings and Loan Associations
- Mutual Savings Banks
- Credit Unions

Non-Deposit Institutions
- Life Insurance Companies
- Investment Companies
- Consumer Finance Companies
- Mortgage Companies
- Check Cashing Outlets
- Pawnshops
Savings and Loan Associations  Traditionally, a savings and loan association (S&L) specialized in savings accounts and making loans for home mortgages. Recently, these financial institutions have expanded to offer a greater array of financial services. They have become more like banks. Today, many S&Ls use the words savings bank in their names.

Mutual Savings Banks  A mutual savings bank is a savings bank that is owned by, and operated for the benefit of, its depositors. The profits are distributed in proportion to the amount of business each participant does with the company. While a mutual savings bank provides a variety of services, it is organized mainly for savings and home loans. Mutual savings banks are located mainly in the northeastern United States.

Credit Unions  A user-owned, not-for-profit, cooperative financial institution is called a credit union. People in the same company, government agency, labor union, or profession often form credit unions. Serving members only, credit unions accept savings deposits and make loans for a variety of purposes. When a person deposits money in a credit union, he/she becomes a member because the deposit is considered partial ownership in the credit union. Today, credit unions also offer a wide range of financial services. The National Credit Union Administration (NCUA), a federal agency, regulates these financial institutions.

Non-Deposit Financial Institutions  The other major category of financial institutions is non-deposit institutions or non-depository intermediaries. They do not take or hold deposits. They earn their money selling specific services or policies.

Life Insurance Companies  People commonly buy life insurance to provide financial security for their dependents. Besides protection, many life insurance companies also offer financial services such as investments. Through careful investing in new and existing companies, life insurance companies help to expand business in the economy.

Investment Companies  People can choose investment opportunities for long-term growth of their money through investment companies. Many investors own shares of one of the more than 15,000 mutual funds worldwide. Investment companies make these mutual funds available.

Consumer Finance Companies  A business that specializes in making loans for long-lasting or durable goods, such as cars and refrigerators, and for financial emergencies is a consumer finance company. Because consumer finance companies make loans, they are a part of the financial services industry. Unlike banks and other financial institutions, consumer finance companies do not accept savings deposits.
Mortgage Companies  Buying a home is an important activity in society. Mortgage companies, along with other financial institutions, provide loans for buying a home or other real estate.

Check-Cashing Outlets  People who do not have bank accounts may use check-cashing outlets (CCOs) to cash paychecks and to obtain other financial services. CCOs offer a wide range of services such as electronic tax filing, money orders, private postal boxes, utility bill payment, and the sale of bus and subway tokens. Some services provided at a CCO are more expensive than at other businesses.

Pawnshops  Pawnshops make loans based on the value of some tangible object, such as jewelry or other valuable items. Pawnshops commonly charge higher fees than other financial institutions.

SELECTING A FINANCIAL INSTITUTION

To obtain the best value for your financial services dollar, comparison shop. You should think about the services offered, safety, convenience, fees and charges, and restrictions.

Services Offered

As financial institutions offer additional financial services, your choices may become confusing. There are four basic types of banking services you will use.

1. Savings accounts
2. Checking and payment accounts
3. Loans and other credit plans
4. Other services, such as safe deposit boxes, trusts, and investment advice

To work through this marketplace maze, determine what banking services you need. Select the checking account with the lowest fees. Locate the best interest rate on your savings. Find the lowest interest rate for loans. Do not be attracted by fancy financial product names or flashy services that you might never need or use.

Safety

The federal agency that helps to regulate banks and other financial institutions is the Federal Deposit Insurance Corporation (FDIC). It protects depositors’ money in case of the failure of a bank or financial institution that it regulates. The FDIC insures all accounts in the same name.
at each bank up to an amount of $100,000. Although the FDIC is a government agency, banks provide money for its operation. Almost 99 percent of all banks are FDIC members.

The National Credit Union Administration (NCUA) regulates credit unions. Similar to the FDIC, NCUA insures a depositor’s funds, up to $100,000, through its National Credit Union Share Insurance Fund. Some state-chartered credit unions use a private insurance program.

Most banks and financial institutions have federal deposit insurance. Do not assume that this is the case at every financial institution. Make sure that the institution where you keep your savings is insured.

**Convenience**
Do you want 24-hour banking services? Do you want branch offices near your home or work? These are some of the factors you will need to think about as you decide about convenience. There is usually a trade-off. While more convenience may mean higher costs, in recent years online banking has resulted in lower costs for many consumers.

### Fees and Charges
Financial services have costs. Compare your needs with the price you pay. Remember, seemingly low fees for using an ATM or having a checking account can add up to hundreds of dollars in a short time.

### Restrictions
Your costs are not always measured in money amounts. If you must keep $500 on deposit for a “free” checking account, you may be losing the chance to earn interest on those funds at another institution.

If you must keep money on deposit for two years to earn a higher rate, you are restricted from using those funds for some unplanned purpose. Always balance your needs with the conditions imposed upon you. When you are not satisfied, shop around!

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**17-1 Assessment**

#### Key Concepts

Determine the best answer.

1. The financial institution most likely to charge the highest rate for a loan would be a
   a. bank
   b. pawnshop
   c. credit union
   d. mortgage company

2. If deposit insurance is most important to you when selecting a financial institution, you are most concerned with
   a. safety
   b. convenience
   c. services
   d. fees

#### Make Academic Connections

3. **Research** Conduct library and online research about the Federal Reserve System. When and why did it start? What are the main actions of the Fed?

4. **Technology** Go to the web site of the Federal Deposit Insurance Corporation to obtain current information on deposit insurance. What other information on the FDIC web site would be of value to consumers?
Financial Services and Electronic Banking

### Types of Financial Services

Whatever your needs, a financial institution can provide services for various personal and business activities.

**Savings Services**

Safe storage of funds for future use is a common need. One of the main services that financial institutions offer is accepting money from customers for safekeeping. A range of savings plans is available for this purpose.

**Payment Services**

The ability to transfer money to others is necessary for daily business activities. Types of payment services include checking accounts, debit cards, and online payments and automatic withdrawals.

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**Focus on Real Life**

“Sixteen dollars for cash machine fees!” exclaimed Hans George as he opened his bank statement. “I guess the cost of those cash withdrawals adds up fast!”

Hans George has a routine of using his cash card at an automatic teller machine several times a week. He really likes the convenience of obtaining cash.

Hans also finds that when getting cash is easy, he easily overspends. While automatic teller machines are easy to use, you must also consider fees and the potential for impulse buying. In recent years, cash machine fees have risen from nothing to $1 or $2 per withdrawal.

How much can cash machine transaction fees cost? If you have two $1 transaction fees a week, you will pay $104 in fees over a year.

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**Key Terms**

- safe-deposit box
- service charge
- debit card

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**Goals**

- Identify the financial services used by consumers.
- Explain types of checking accounts.
- Describe electronic banking activities.

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**Focus on Real Life**

“What can you do to reduce or eliminate bank fees?”
### Lending Services

Most people, businesses, and governments borrow money at some time. A business may want to borrow money to build a new warehouse or buy products to resell. Individuals may borrow to buy a car or pay college tuition. Banks make loans since most of their income is from the interest they charge borrowers.

Banks offer many types of lending services. These include auto loans, business loans, and mortgages. Credit cards allow a person to buy items without having the cash. When paying with a bank credit card, you are borrowing money from the bank.

Another way that banks lend money is by sending several checks with a customer’s credit card statement. This allows the customer to use one of the checks to obtain cash or to pay a bill. If the customer uses the checks, the bank charges the amount of each check to the customer’s credit card account. In effect, the amount of the check is a loan.

### Electronic Banking

**Electronic funds transfer (EFT)** refers to the use of computers and other technology for banking activities. Electronic banking services include the use of automated teller machines (ATM), point-of-sale transactions, direct deposit, and automatic bill payment. Online computer banking allows a customer to access many financial services.

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### Technology Topics

#### Online Banks and E-Cash

Most financial institutions offer online banking services. Now *Web-only* banks have also started. E*Trade Bank operates only online, and customers have access to ATMs. Web-based banks allow customers to see their most current loan and savings rates. Users may also apply for loans and access other services online.

Electronic banking is replacing cash. PayPal is one online payment system. These Web companies provide fast payments for e-commerce transactions. Their services reduce risk for both the buyer and seller in exchanging payments and purchasing products. To use these payment services, a person gives a name, address, phone number, checking account or credit card information, and a password. E-mail, banking, and credit card networks provide the infrastructure for processing payments.

E-cash (electronic cash) is the latest type of money. Money has evolved from gold and silver to paper (currency and checks), and now to online electronic exchanges. These digital money systems will likely be used almost everywhere. As technology improves, e-cash will be cost-effective even for transactions of 10 or 25 cents.

E-cash adds to the globalization of business. Online buyers and sellers can instantly convert transaction amounts to any currency. While the use of online payments and e-cash will expand, coins and paper money are likely to continue to exist in many settings for a long time.

#### Think Critically

1. What are the benefits and concerns of online banking and e-cash payment systems?
2. Conduct research about online payment systems. Obtain information about various forms of cyber cash that are being used to transfer payments between customers and online businesses.
Storage of Valuables
Banks offer safe-deposit boxes for storage of valuables. Because these safe-deposit boxes are in well-guarded vaults, they are very safe places to keep jewelry, rare coins, investment certificates, birth records, a list of insurance policies, and other valuable documents.

Only you or someone to whom you have given the right to open the box may open it. Not even a bank has the right to open your safe-deposit box unless it is ordered to do so by a court. You rent safe-deposit boxes by the year. They come in a variety of sizes.

Investment Advice
Many financial institutions help customers by offering financial advice and investment services. These advisors can assist customers about whether it is wise to buy a certain house, how to manage money better, or how to exchange U.S. funds for foreign currency.

Most banks offer advice on investments. This involves savings that are put to work to earn more money. Types of investments include government bonds, stocks, and mutual funds.

Management of Trusts
Many banks manage investments on behalf of customers. When they do this, the money or other property that is turned over for the bank to manage is said to be held in trust. This service can be offered through a trust company or through trust departments in banks.

Trusts are used by people of all ages. They are especially useful for very young people and for some elderly people. A young person who inherits money may not have the skill and experience to manage it wisely. Elderly people who are ill may ask the trust department of a bank to manage their money. The bank makes investments and keeps the customers informed about what is happening to their money.

CHECKPOINT
What are the main financial services used by consumers?

TYPES OF CHECKING ACCOUNTS
While checking accounts vary from one bank to another, three types are most common.

Regular Checking Accounts
If you write a lot of checks each month, consider a regular checking account. A service charge is a fee a bank charges for handling a checking account. With most banks, there is no service charge for a regular checking account as long as you maintain a certain minimum balance. This amount varies and is often $300 or higher. A checking account at a credit union may be called a share draft account since the members are called shareholders.
Interest-Earning Checking Accounts

Many financial institutions offer checking accounts that earn interest. These accounts may require a higher monthly balance than regular checking accounts. If the account falls below the required amount, the bank usually pays no interest and may add a service charge.

The rates of interest that banks pay their customers also vary. Usually, a bank will offer a higher rate of interest when a higher balance is kept in the account. Very often, interest rates on checking accounts are quite low. When you are depositing larger amounts of money, consider other savings alternatives.

Special Checking Accounts

If you only write a few checks each month, consider a special checking account. Also called activity accounts, banks charge customers about 10 to 20 cents for each check written. A monthly service charge may also be added.

Comparing Checking Accounts

When selecting a checking account, evaluate the following items.

- Minimum balance
- Interest rate earned, if any
- Monthly service charge
- Fees for other services, such as printing checks and stop payment orders
- Other restrictions

When choosing a checking account, be careful. A bank may attract you with a low minimum balance, but fees can result in a higher total cost.

Electronic Banking Services

Obtain cash.
View account history and check balances.
Transfer funds:
- From savings to checking account
- From savings to loan account
- From checking to loan account
- From checking to savings
Direct deposit of paychecks and government payments.
Preauthorized payments for insurance, mortgage, utilities, or other bills.
Pay bills online.
Debit card retail purchases.
Web banking to apply for loans, manage investments, and other services.

E-Banking Services

Each day, the use of electronic banking services grows. You can do your banking from an ATM, from a home computer, or from a wireless Internet connection on your cell phone.

Has electronic banking made it easier for you to manage your finances?

Figure 17-3

Describe electronic banking activities.
**Automatic Teller Machines**

Commonly called a *cash machine*, an automatic teller machine (ATM) allows many banking services. A *debit card*, or *cash card*, is used for ATM transactions. A debit card is different from a *credit card*. With a debit card issued by your bank, you are using money that is in your account. With a credit card, you are borrowing from the bank to pay later.

A lost or stolen debit card can be expensive. If you notify the financial institution within two days of the lost card, your liability for unauthorized use is $50. After that, you can be liable for up to $500 of unauthorized use for up to 60 days.

ATM services have expanded to provide other types of transactions. You can use these machines to buy bus passes, postage stamps, and gift certificates.

Be aware that many banks charge fees for ATM usage. To minimize ATM fees, compare rates at several financial institutions. Use your bank’s ATMs to avoid surcharges. Withdraw larger amounts to avoid fees on several small transactions.

**Payments at the Point-of-Sale**

In a *point-of-sale transaction*, a merchant accepts a debit card to pay for purchases. Most gas stations, stores, and restaurants accept this type of payment. Vending machines that accept debit cards are also becoming more common.

**Direct Deposit**

A major portion of society uses *direct deposit* of paychecks and government payments. Funds are deposited electronically and available automatically for your use.

**Automatic Bill Payments**

Each month, many people pay their rent, mortgage, loans, utilities, and other bills without doing anything. *Automatic bill payment* requires a bank customer to authorize preset amounts of monthly expenses. The bank deducts the payments from your account and transfers them to the appropriate companies. With automatic bill payments, be sure to check each month that the correct amounts have been deducted.

**Electronic Payment Options**

The use of cash, checks, and credit cards is declining. These payment methods are being replaced by newer electronic alternatives.

**Debit Card Transactions**

Most stores, restaurants, and other businesses accept debit cards issued by Visa and MasterCard. You may also know these cards as *check cards*. When the debit card transaction is processed, the amount of the purchase is deducted from your checking account.

Debit cards are used in one of two ways.

1. You sign a receipt, similar to when you use a credit card.
2. You are asked to provide your *personal identification number* (PIN), similar to when you use an ATM.

**Online Payments**

Various web companies and banks now provide online bill payment services between buyers and sellers. When using these services, be sure to think about the monthly charge as well as online security and customer service availability.
Also on the Web are “cybercash” or “e-cash” services designed to serve as financial intermediates. These organizations create their own e-money that serves as a medium of exchange for online transactions.

**Stored-Value Cards** Prepaid cards for phone service, transit fares, highway tolls, laundry service, and school lunches are common. Some stored-value cards are disposable. You can recharge others with an additional amount.

**Smart Cards** These “electronic wallets” are similar to ATM cards. Their imbedded microchip stores prepaid amounts as well as account balances, transaction records, insurance information, and medical history.

**Banking in the Future**
The way you use banks and money will continue to change. Electronic financial services will be combined with wireless technology. You will be able to do almost any transaction away from the financial institution.

An access card or a handheld device will provide a large number of services. The technology will create a personalized system for obtaining, transferring, and using funds. Expanded information related to financial activities, health care, education, careers, travel, and recreation will also be a key element.

**FYI**
Stores may process a check at the time of purchase using an electronic check conversion (ECC) system. The check moves through an ECC reader to obtain the amount, account, and bank information. After processing, the paper check is returned to the customer marked “void.”

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**17-2 Assessment**

**Key Concepts**
Determine the best answer.

1. True or False. Using a debit card is similar to writing a check.
2. A safe deposit box is best used for storing
   a. large amounts of cash
   b. home ownership documents
   c. credit card statements
   d. antique furniture
3. What type of checking account usually requires the highest balance to be kept on deposit?
   a. an activity account
   b. a share-draft account
   c. a regular account
   d. an interest-earning account

**Make Academic Connections**

4. **Visual Communication** Conduct a survey of 20 students to determine the types of financial services they use. Create a table or graph on a poster or spreadsheet program to report how many people use various types of financial services.
5. **Technology** Locate examples of online payment services and “cybercash” companies. What services are provided? What concerns might be associated with these services?
Microfinance

How could a loan of $50 result in a life-changing experience? In countries such as Bangladesh, Nepal, the Philippines, and Zimbabwe, microfinance has helped improve the economy and society.

Microfinance, also called microlending and microcredit, involves programs of small loans to people for self-employment projects. The business activities generate enough income to provide for life necessities and family needs. Most microcredit efforts involve nonprofit organizations, which helps avoid political influences.

Most microfinance clients are low-income persons with no access to formal financial institutions. They are usually self-employed, often household-based entrepreneurs. In rural areas, clients are small farmers or food-processing workers. In urban areas, microfinance activities include shopkeepers, service providers, artisans, and street vendors.

In southeastern Bangladesh, one of the poorest regions in the world, BRAC (formerly the Bangladesh Rural Advancement Committee) helps women obtain loans. Loans help them farm fish, keep cows for milk production, grow vegetables, raise poultry, buy rickshaws, and sew clothing. While the women pay 15 percent simple interest on loans, this is much less than they would have to pay to loan sharks. The banking is done in the village through an agent of the microfinance institution. Loans are not secured through collateral. Repayment is in 52 weekly installments in a year’s time, and simple interest is used rather than compound interest.

BRAC also works to improve the health of women and children. Over 30,000 volunteers have been trained by BRAC to recognize and treat 10 common illnesses.

Think Critically
1. What are the main benefits of microfinance programs?
2. What are some possible concerns of microfinance?
3. Conduct an Internet search to find other examples of microfinance around the world.
OPENING A CHECKING ACCOUNT

The following are some of the benefits that checking accounts provide for consumers.

- Convenience and ease of making payments
- Safety to make payments with less risk than using cash
- Proof of payment
- A record of finances for managing your money

The First Deposit

Opening a checking account starts with signing a signature card. This document is used to verify your signature. The bank compares the signature on checks to the one on the signature card. A sample signature card is shown in Figure 17-4.

Sometimes two or more people have an account together called a joint account. Each person who will write checks on the account must sign the signature card. Any signer of the card in a joint account can write checks.

Focus on Real Life

Alicia Garcia made her first deposit in her new checking account. Her friend Joni asked her, “If I write you a check, could you give me the cash? You can deposit my check in your account later.”

“How do I know your check is good?” Alicia asked.

“What! We’ve been friends for over 10 years,” Joni responded. “Don’t you trust me?”

“Of course I trust you,” said Alicia. “Just remember that if a check isn’t good, it can result in some expensive service fees.”

The next day, Laura came up to Alicia and said, “I can’t wait to mail away for this sweater, but the ad says ‘no personal checks.’ How can I pay for it?”

“Let me tell you about money orders,” responded Alicia.

Figure 17-4

Do you understand how a signature card protects you and the bank?

Signature Card

Second National Bank
PERSONAL CHECKING ACCOUNT

<table>
<thead>
<tr>
<th>JOINT AND SEVERAL (Payable to the order of either or the survivor)</th>
<th>Individual (If payable on death to named survivors, fill in section below)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indicate number of signatures required</td>
<td></td>
</tr>
</tbody>
</table>

Alicia Garcia
SIGNATURE

Alicia Garcia
SIGNATURE

19684 Absaroka Dr., Houston, TX 77083-5549
2 years

ADDRESS
CITY AND STATE
ZIP CODE
HOW LONG? MO. YRS.

555-6409

HOME PHONE
DRIVERS LICENSE NO./STATE

PAYABLE ON DEATH OF DEPOSITOR TO SUCH OF THE FOLLOWING NAMED AS SURVIVE DEPOSITOR:

(PRINT OR TYPE NAME — DESIGNATION BY OTHER MEANS IS NOT SUFFICIENT)

Office: ___________________________ Date: April 10, 20--

201-24-1590

OFFICER APPROVAL
SOCIAL SECURITY NUMBER

1648-721A

ACCOUNT NUMBER
on the account as if he or she were the only owner.

When you deposit money in a checking account, you fill out a deposit slip. This form lists all items you are depositing—currency, coins, or checks. The deposit slip shows your name, account number, the date, the items deposited, and the total amount of the deposit.

**Types of Endorsements**

Before you can deposit a check, it must be endorsed. This involves writing your name on the back of the left end of the check. An endorsement is written evidence that you received payment or that you transferred your right of receiving payment to someone else.

When you endorse a check, your responsibilities are almost as great as if you had written the check yourself. As an endorser, you are actually making this promise: “If this check is not paid by the bank, I will pay it.”

Your endorsement must be made in the 1 1/2-inch space on the left side of the check. If you write outside this limit, the bank may return the check. Different endorsements have different purposes. Figure 17-5 shows some examples.

**Blank Endorsement** An endorsement that consists of only the endorser’s name is a blank endorsement. To endorse a check, sign your name in ink exactly as it is written on the face of the check. If the name on the check is different from your official signature, you will need to endorse the check twice. First, use the name as given on the check. Then, write your name as it appears on the account.

A blank endorsement makes a check payable to anyone who has the check. While you can use this endorsement to transfer any check, sometimes another type of endorsement is better.
**Full Endorsement** The use of a *full endorsement*, also called a *special endorsement*, allows you to transfer a check to another person. You write the words “Pay to the order of . . .” followed by the name of the person or business to which the check is being transferred. This is followed by your signature. This phrasing results in only the specified person being able to sign and cash the check.

**Restrictive Endorsement** A *restrictive endorsement* limits the use of the check to the purpose given in the endorsement. For example, you may have several checks that you want to mail to the bank. You could write “For deposit only” above your signature, followed by your account number. This endorsement restricts use of the check so it can only be deposited to your account.

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**Checkpoint**

What are the three types of endorsements?

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**Why is the amount of this check written twice?**

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**Parts of a Check**

- **Printed name and address of account owner (Drawer):** Alicia Garcia 19684 Absaroka Drive Houston, TX 77083-5549
- **Payee:** The Complete Ski Shop
- **Date check is written:** April 13
- **Check number:** 101
- **Amount in figures:** $39.95
- **Name of bank (Drawee):** Second National Bank Houston, TX 77083-9073
- **Purpose of check:** For classroom use only
- **Bank's identification code for electronic sorting and routing:** 80-1711130
- **Drawer's account number for electronic sorting (MICR):** 1130
- **Drawer's signature:** Alicia Garcia

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**USING A CHECKING ACCOUNT**

Checking accounts are an easy way to access funds. Still, to use a checking account correctly, you must understand certain information and follow some simple procedures.

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**Check-Writing Procedures**

Some checks are light blue or green in color. Others have a picture of a forest, a sports team logo, or an inspirational quote. No matter what they look like, all checks contain essentially the same information.

**Elements of a Check** Figure 17-6 shows some terms that are used to identify the parts of a check. Three parties are shown on each check:

- The *drawer* is the owner of the account who signs the check.
- The *payee* is the person to whom the check is written.
CHAPTER 17 Banking and Financial Services

The drawee is the bank or other financial institution that pays the check.

The Check Register Your checkbook will have a place for recording account activities. One of three formats may be used for this purpose. The check stub is a form attached to the check by a perforated line. A check register is a separate book, usually the same size as the checkbook. Note that both forms provide blanks to fill in the same type of information about the check. A duplicate copy of the check may also be automatically created when you write the check.

Always fill out the stub or register first. If you write the check first, you may forget to record the information before you transfer the check.

Writing a Check Fill out the check completely and carefully using the following seven steps.

1. Write checks in order by number so you know which checks have been paid.
2. Write the date in the proper space.
3. Write the payee’s name on the line following Pay to the Order of.
4. Write the amount of the check in figures after the printed dollar sign. Write the amount close to the dollar sign to prevent someone from altering your check. Write the cents figures close to the dollar figures so that additional numbers cannot be inserted.
5. Write the dollar amount in words on the line below the payee’s name. Write the cents in figures as a fraction of a dollar. Begin writing at the far left end of the line. Draw a line from the fraction to the printed word Dollars to fill all unused space.
6. Write the purpose of the payment on the line at the bottom of the check.
7. Sign your checks with the same signature you wrote on your signature card.

Proper Check Writing Poor check writing can cause problems and financial difficulties. Follow these tips to avoid trouble.

1. Write checks only on the forms provided by your bank. Checks can be written on just about anything—even a paper bag—but sorting and processing can be delayed when you do not use the proper form.
2. Write checks in ink. This prevents someone from altering the amount.
3. Only write checks if money is available. Writing a check for more than is in your account can result in an overdrawn account. The bank may not pay the check and you will most likely be charged a fee.

Why is it important to fill out a check properly?
4. **Use the current date.** A *postdated* check is one that is dated later than the date on which it is written. This business practice is unwise and can result in additional service charges.

5. **Avoid making checks payable to “Cash” or to “Bearer.”** Such a check can be cashed by anyone. Instead, make the check out to yourself or to the bank as payee.

6. **Always fill in the amount.** If you leave it blank, you may be held responsible for amounts filled in by others.

7. **Void checks on which you make errors.** Do not try to erase or retrace your writing. Write “Void” across the check. Make note of the voided check in the check register.

8. **Record every payment from your checking account, whether the payment is by check or EFT.** Some people carry a few blank checks. When one of these checks is used, make a note of it and record it in the register. Also, promptly record all transactions made at an ATM.

### Stopping Payment

In certain situations, you may not want your bank to pay a check that you have written. To do so, you will fill out a **stop payment order**, a written notice that tells the bank not to pay a certain check. Because banks charge a high fee for stopping payment on a check, use this process only for good reason. You may learn, for example, that a check you have written to pay a bill was lost in the mail. A check you have written may have been stolen. Before you write a new check, you should stop payment on the one that was lost or stolen.

### THE RECONCILIATION PROCESS

As a depositor, you will need to review the record of your account that the bank keeps. At regular intervals, usually monthly, the bank will send you a report on the status of your account known as a **bank statement**.

#### Bank Statement Information

While bank statement formats vary, most present the following information:

- The balance at the beginning of the month.
- The deposits made during the month.
The checks paid by the bank during the month.
Any automated teller transactions made during the month.
Any electronic fund transfers (EFT) or special payments the bank has made.
Service charges for the month, including charges for such special services as stopping payment on a check.
Any interest earned on the account.
The balance at the end of the month.

Some examples of these items are shown on the bank statement shown in Figure 17-7.

**Determine Checks Paid**

When you receive your bank statement, compare the checks you have written to those that have been paid by your bank. Banks might not return the actual canceled checks that have been paid. Instead, banks can make use of a substitute check, which is a digital reproduction of the original paper check.

Your check register is your payment record. Sometimes you may need additional proof. In most cases, information on the statement will be sufficient to prove payment. If the check showing the endorsement is needed, the digital image (provided by the bank) is now considered a legal equivalent of the original check.

**Monthly Account Statement**

<table>
<thead>
<tr>
<th>BALANCE</th>
<th>NO. OF WITHDRAWALS</th>
<th>TOTAL AMOUNT</th>
<th>NO. OF DEP.</th>
<th>TOTAL DEPOSIT AMOUNT</th>
<th>SERVICE CHARGE</th>
<th>BALANCE THIS STATEMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.00</td>
<td>14</td>
<td>433.85</td>
<td>4</td>
<td>826.95</td>
<td>3.00</td>
<td>390.06</td>
</tr>
</tbody>
</table>

**Checks and Other Debits**

<table>
<thead>
<tr>
<th>DATE</th>
<th>BALANCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>331.85</td>
<td>4/10</td>
</tr>
<tr>
<td>291.90</td>
<td>4/13</td>
</tr>
<tr>
<td>241.90</td>
<td>4/15</td>
</tr>
<tr>
<td>241.90</td>
<td>4/16</td>
</tr>
<tr>
<td>258.93</td>
<td>4/22</td>
</tr>
<tr>
<td>258.06</td>
<td>4/23</td>
</tr>
<tr>
<td>208.06</td>
<td>4/24</td>
</tr>
<tr>
<td>191.76</td>
<td>4/24</td>
</tr>
<tr>
<td>165.98</td>
<td>4/24</td>
</tr>
<tr>
<td>340.98</td>
<td>4/24</td>
</tr>
<tr>
<td>275.65</td>
<td>4/26</td>
</tr>
<tr>
<td>242.19</td>
<td>4/27</td>
</tr>
<tr>
<td>217.86</td>
<td>4/27</td>
</tr>
<tr>
<td>212.06</td>
<td>4/27</td>
</tr>
<tr>
<td>199.21</td>
<td>4/27</td>
</tr>
<tr>
<td>469.31</td>
<td>4/29</td>
</tr>
<tr>
<td>465.06</td>
<td>4/29</td>
</tr>
<tr>
<td>390.06</td>
<td>4/30</td>
</tr>
</tbody>
</table>

**Figure 17-7**

How many checks were paid by the bank and posted to Alicia's account?
Find Differences
You keep your own record of your checking account, usually in a check register. The bank statement is the bank’s record of your account.

The document created to show how the two balances were brought into agreement is called the **bank reconciliation**. Bringing the balances into agreement is known as **reconciling the bank balance**. The bank often prints forms for reconciling on the backs of bank statements. Figure 17-8 shows an example of a bank reconciliation.

The balances shown on your records and the bank statement may be different. Following are some of the most common reasons for the difference.

- Some of the checks you wrote may not have **cleared** (been paid). These checks, which have not been deducted from the bank statement balance, are called **outstanding checks**.
- You may have forgotten to record a transaction in your register, such as an ATM deposit or automatic bill payment.
- A service charge may appear on the bank statement.
- You may have mailed a deposit to the bank that has not yet been received.
- Interest earned may have been added.
- You may have recorded the amount of a check incorrectly in the check register. You may have added or subtracted incorrectly.

### Reconciliation Form

YOU CAN EASILY BALANCE YOUR CHECKBOOK BY FOLLOWING THIS PROCEDURE

| BALANCE SHOWN ON BANK STATEMENT | $390.06 |
| ADD DEPOSITS NOT ON STATEMENT | $ |
| TOTAL | $390.06 |
| SUBTRACT CHECKS ISSUED BUT NOT ON STATEMENT | $ |
| 108 | 10.00 |
| 115 | 21.00 |
| 116 | 17.50 |
| TOTAL | $416.56 |
| ADD ANY DEPOSITS NOT ALREADY ENTERED IN CHECKBOOK | $ |
| SUBTRACT SERVICE CHARGES AND OTHER BANK CHARGES NOT IN CHECKBOOK | $3.00 |
| TOTAL | $75.00 |
| BALANCE | $341.56 |

These totals represent the correct amount of money you have in the bank and should agree. Differences, if any, should be reported to the bank within ten days after the receipt of your statement.
Calculate Adjusted Balance
To determine the true balance in your account, take the following steps.

1. Subtract the total of the outstanding checks from the bank statement balance.
3. Subtract service charges, fees, and automatic payments from your checkbook balance.
4. Add any interest earned to your check register balance.

At this point, if the balances do not agree, either you or your bank has made an error. You should check each of the steps again. Then, carefully go over the calculations in your check register. If you do not find an error in your calculations, contact your bank.

After you have reconciled your bank statement, correct any errors that you made on your register. The new balance now agrees with the bank statement. With your account updated, you can write checks on the new balance.

OTHER TYPES OF PAYMENTS
Often, you might need to make a payment in a situation when a personal check is not acceptable. Several payment alternatives are available.

Certified Checks
A certified check is a personal check for which a bank has guaranteed payment. The certification is stamped on the face of the check and is signed or initialed by a bank officer.

Cashier’s Checks
A bank usually keeps funds in an account of its own on which it writes its own checks. A cashier’s check is a check that a bank draws on its own funds. A cashier’s check costs the amount of the check plus a service fee. These banker’s checks are more acceptable than the personal checks of an individual whom the payee may not know.

Traveler’s Checks
Carrying a large sum of money when you travel is risky. In addition paying traveling expenses with personal checks may be difficult. Traveler’s checks are special forms designed for making payments when away from home. You can buy them at banks, credit unions, and travel bureaus. Traveler’s checks are sold in several denominations such as $10, $20, $50, and $100. In addition to the value of the checks, a fee of one percent may be charged. This means that $100 worth of traveler’s checks will cost $101.

Traveler’s checks require your signature in two places. First, you sign each one when they are bought. Then, when
you cash a check or pay for a purchase with it, you sign it again in the presence of the person accepting it. Businesses throughout the world commonly accept traveler’s checks.

**Money Orders**

A person who does not have a checking account and wants to send a payment through the mail may purchase a money order. A *money order* is a form of payment that orders the issuing agency to pay the amount printed on the form to another party.

Several types of organizations commonly sell money orders.

- A *bank money order* is sold by a bank stating that money is to be paid to a specific person or business.
- A *postal money order* purchased from the U.S. Post Office can be sent safely through the mail. It can be cashed only after the payee signs it.
- An *express money order* is issued by various organizations including traveler’s check companies, travel agencies, and many supermarkets, pharmacies, and convenience stores.
- A *telegraphic money order* involves buying a message to direct a telegraph office to pay a sum of money to a certain person or business.

If a money order is lost or stolen, the receipt copy that you receive may be used in making a claim.

**FYI**

The Check Clearing for the 21st Century Act (known as Check 21) shortens the processing time of checks using electronic systems. The actual paper check will no longer be processed.

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**17-3 Assessment**

**Key Concepts**

Determine the best answer.

1. The first document that must be completed when opening a checking account is the
   a. deposit slip
   b. reconciliation statement
   c. check register
   d. signature card

2. A personal check with guaranteed payment is a
   a. cashier’s check
   b. money order
   c. certified check
   d. traveler’s check

**Math**

Service charges for Tom Harding’s regular checking account at Second National Bank are based on the bank’s rate schedule:

<table>
<thead>
<tr>
<th>Minimum Balance</th>
<th>Charge</th>
</tr>
</thead>
<tbody>
<tr>
<td>0–$199</td>
<td>$6</td>
</tr>
<tr>
<td>$200–$399</td>
<td>$4</td>
</tr>
<tr>
<td>$400 and over</td>
<td>no charge</td>
</tr>
</tbody>
</table>

During a recent six-month period, Tom’s balances were: April, $148.00; May, $201.97; June, $101.61; July, $418.53; August, $248.29; and September, $154.36.

a. How much was Tom’s service charge for each month?

b. What was the total service charge for the six-month period?
Business Notes

17-1 Banks and Other Financial Institutions
1. The Federal Reserve System serves member banks by accepting their deposits, lending them money, clearing checks, and providing other services.
2. The main deposit-type institutions are commercial banks, savings and loan associations, mutual savings banks, and credit unions. Non-deposit financial institutions include life insurance companies, investment companies, consumer finance companies, mortgage companies, check-cashing outlets, and pawnshops.
3. To obtain the best value for your financial services dollar, investigate and compare services offered, safety, convenience, fees and charges, and restrictions.

17-2 Financial Services and Electronic Banking
4. The most common services offered by financial institutions are accepting deposits, transferring funds, lending money, electronic banking, storing valuables, providing financial advice, and managing trusts.
5. The main types of checking accounts are regular checking accounts, interest-earning checking accounts, and special checking accounts.
6. Electronic banking services include the use of automated teller machines (ATM), point-of-sale transactions, direct deposit, automatic bill payment, online payments, stored value cards and smart cards.

17-3 Checks and Payment Methods
7. The purpose of an endorsement is to allow the recipient of the check to cash, deposit, or transfer it to someone else. A blank endorsement consists of only the endorser’s name. A full endorsement, also called the special endorsement, allows you to transfer a check to another person. A restrictive endorsement limits the use of the check to the purpose given in the endorsement.
8. Reconciling a checking account involves finding the differences between the balance on the bank statement and the balance in your checkbook.
9. Other types of payment methods include certified checks, cashier’s checks, traveler’s checks, and money orders.

Communicate Business Concepts

1. Some people believe that banks need more regulations and control by the government. Others would like fewer regulations for banks. What are some arguments for each point of view?
2. What factors might affect whether you use a commercial bank or a credit union for your banking activities?
3. List the type of banking service that you think each person would be most likely to use. Explain your answer.
   a. A person planning to open a fitness center
   b. A musical group
   c. A wealthy senior citizen
   d. A buyer of a van
   e. A high school recycling club
4. Jake Olsen has decided to put $1,000 in the bank. List several questions Jake might want to ask before choosing whether to put the money in a checking or a savings account.
5. Cher Alonso often makes deposits and withdrawals at the ATM that she passes on her way to work. She frequently forgets to record these banking activities in her check register and never seems to know how much money she has in the bank. In addition, she has overdrawn her account twice and has had to pay a
fee each time. Can you suggest a plan for Cher to follow that would allow her to use the automatic teller services and still be sure of having an accurate record?

6. Name items that a person might keep in a safe-deposit box.

7. While using a debit card increases the speed and efficiency of business transactions, what effect can this have on a person’s money management skills?

8. Isaac Ahlred has received his bank statement for the month of May. The bank statement shows a balance of $401.19, but his check register shows a balance of only $364.52.

   a. What is the most likely reason that the bank balance is larger than Isaac’s?

   b. What steps should Isaac take to bring his balances into agreement?

9. While on a trip, the Mendoza family decided to buy furniture, which cost $500. The dealer would not accept a personal check or credit cards. What method could be used to pay for the furniture?

10. “You should shop for the best place to open a checking account as carefully as you shop for the best buy in any product or service.” Give two reasons to support this statement.

11. Matt Huffman believes that it is a waste of time to record information on check stubs. “The bank sends me a statement each month. That’s all I need,” he says. How could you convince Matt that he should keep records?

>> Develop Your Business Language

Match the terms listed with the definitions.

12. A bank that offers a full range of financial services.

13. A nationwide banking plan set up by the federal government to supervise and regulate member banks.

14. A written notice telling the bank not to pay a certain check.

15. A separate form on which the depositor keeps a record of deposits and checks.

16. A device used for cash machine transactions.

17. A secured area in a bank vault for storing valuables.

18. Written evidence that you received payment or that you transferred your right of receiving payment to someone else.

19. A report sent by the bank to a depositor showing the status of his or her account.

20. A federal agency that protects deposited money in case of the failure of a bank or financial institution that it regulates.

21. A fee a bank charges for handling a checking account.

22. Checks that have not been deducted from the bank statement balance.

23. A not-for-profit financial institution formed by people who have like occupations or live in the same community.

24. A statement showing how the checkbook balance and the bank statement were brought into agreement.

Key Terms

a. bank reconciliation
b. bank statement
c. commercial bank
d. check register
e. credit union
f. debit card
g. endorsement
h. Federal Deposit Insurance Corporation (FDIC)
i. Federal Reserve System
j. outstanding checks
k. safe-deposit box
l. service charge
m. stop payment order
> > Decision-Making Strategies

Fran and Bill Hamilton recently moved to a new community. They are having trouble deciding whether to use a financial institution near their workplaces or near their home. The Hamiltons have the opportunity to do business with a credit union, a national bank with many branches, a local bank with strong personal service, or a savings and loan association.

25. What factors should the Hamiltons consider when selecting a financial institution?

26. How could Fran and Bill obtain information about the financial institution that would best serve their needs?

> > Make Academic Connections

27. Geography Locate a map of the United States. Use this map to show the districts of the Federal Reserve System. Look at several U.S. one dollar bills. Which Federal Reserve Banks are noted on the seal of this currency?

28. Culture Research financial services and payment methods commonly used in various countries around the world.

29. Communication Collect advertisements and promotional information from several financial institutions. Analyze these materials to determine information that is useful for consumers. Create a poster to highlight and report your findings.

30. History Investigate the availability of credit unions in your community. Who may join? What services are offered?

31. Law Check cashing outlets and pawnshops frequently charge fees and rates much higher than other financial institutions. Research laws that regulate these financial institutions. Prepare a one-page summary of your findings.

32. Research Obtain information about various types of checking accounts available in your area and online. Create a comparison table showing the name, address, phone, and web site of the financial institution. Report the minimum balance, monthly service charge, other fees, interest earned (if any), and other services available for each checking account.

33. Math On June 1, Susan Pohnik had a checking account balance of $140. She has her paychecks automatically deposited into her account. Her earnings for June were $1,080. During the month, she wrote checks for $87, $146, $29, and $292. She had $120 automatically transferred from her checking account to her savings account. In addition, she used her ATM card to withdraw $60 in cash. The bank charges 75 cents for each EFT transfer or withdrawal. Find Susan’s bank balance after these transactions.

34. Economics Select various economic measurements of the economy, such as interest rates and consumer prices. Describe how changes in these economic factors might affect the use of financial services.

35. Technology Research recent developments in electronic banking services. Describe some new services that were not available a few years ago.

36. Research Several states require that banks offer basic checking accounts for low-income consumers. In Illinois, Massachusetts, Minnesota, New Jersey, New York, Rhode Island, and Vermont, checking services with minimal fees must be made available for consumers who make a limited number of transactions. These are called life-line accounts. Research the availability of this service in your area.

37. Communication Present role-playing situations to describe when you might use a certified check, a cashier’s check, traveler’s checks, and a money order.

38. Math In October, Tom Jarez received his bank statement that showed a balance of $378.65. The service charge was $3. In examining his statement, he found that the following checks were outstanding: No. 31, $7.16; No. 34, $15.10; and No. 35, $9.95. His checkbook balance at the end of the month was $349.44. Reconcile his bank statement.
> > Linking School and Home

Talk to people in your household or neighborhood about the financial institutions and financial services they use. Which of these have you learned about in this chapter? Are there other financial services that you need to learn about? Create a two-paragraph summary of your findings.

> > Portfolio Activity

To provide tangible evidence of your learning about electronic banking services, do the following:

**COLLECT** pictures, advertisements, articles, and web site information about the main types of electronic banking services.

**CREATE** a flowchart (with visuals) that communicates the flow of electronic funds from one person (or business) to another. Use visuals to show various types of technology used in electronic banking activities.

**CONNECT** your visual to other items already in your class portfolio, or relate the flowchart to an important concept you learned in another class. Make the connection by writing a one-paragraph discussion of how electronic banking affects various aspects of the economy and society.

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**Presentation Management Individual Event**

This event will assess your use of current desktop technologies and software to prepare and deliver an effective multimedia presentation.

You will design a multimedia presentation. You have 15 minutes for preparation and setup. The presentation will last a minimum of 7 minutes and a maximum of 10 minutes. Up to 5 minutes will be allowed for questions from the judges. The contestant must make effective use of current multimedia technology in the presentation. In preparation of the presentation, contestants should use space, color, and text as design factors. No VCR or laserdisc may be used in the presentation. Charts and other graphics should be used in the presentation. The student is responsible for securing a release form from any individual whose name, photograph, and other information is included in the presentation.

**Topic:** Banks are encouraging customers to do business using the Internet. They stress the convenience of paying bills online. Many individuals are suspicious of handling their banking business online. Computer fraud and theft of identity are issues that some customers feel override the convenience of banking online.

You must prepare an electronic presentation that encourages customers to bank online. Factors to emphasize include convenience, security, and timeliness. Your presentation should show how the positive aspects outweigh the negative concerns of banking online.

**Performance Indicators Evaluated**

- Demonstrate knowledge of multimedia software and components.
- Demonstrate effective oral communication.
- Apply technical skills to create a multimedia presentation that enhances the oral presentation.

You will be evaluated for your:

- Knowledge of the topic
- Organized presentation of the topic
- Confidence, quality of voice, and eye contact
- Relationship of the topic to business strategy

For more detailed information about performance indicators, go to the BPA web site.

**Think Critically**

1. List three advantages for banking online.
2. List three disadvantages for banking online.
3. What can the bank do to make customers more comfortable with banking online?

http://www.bpa.org/
Chapter 18

Consumer Credit

18-1 Credit Fundamentals
18-2 Cost of Credit
18-3 Credit Application and Documents
18-4 Protection of Credit Rights
Credit is important in most economies. Many individuals and businesses use credit for various purchases. Consumer credit involves loans for housing, motor vehicles, and college expenses. Business loans are vital for companies to start operations, purchase inventory, and buy equipment. As a result, many workers are employed with banks and credit card companies in approving, processing, servicing, and collecting credit transactions. Workers in consumer credit also find jobs in credit counseling, helping people regain control of their finances and plan for their financial future.

**Employment Outlook**
- Most occupations in the credit industry will have average growth.
- Slower growth is expected for loan officers since technology is making loan processing simpler and faster.
- Demand for bill collectors and loan counselors can increase when people do not make wise credit and buying choices.

**Job Titles**
- Bill and Account Collector
- Credit Authorizer
- Credit Clerk
- Loan Officer
- Interviewer
- Credit Analyst
- Loan Counselor
- Information and Record Clerk
- Customer Service Representative

**Needed Skills**
- Four-year college degree with an emphasis in finance and economics
- On-the-job training and industry courses for loan officers and other credit workers
- Computer skills, especially in spreadsheet and database application programs
- Excellent communication skills for interaction with customers

**What's it like to work in ... Consumer Credit**

“We’re not sure where our money goes each month. We just know we owe over $8,000 in credit card bills,” was the response of Joan and Hank Salvatore.

Joan and Hank have a monthly income of $3,750, but their expenses (including credit card payments) are more than $4,400. That’s why they came to the community credit counseling service. Joan and Hank were assigned to Bev Gonzalez. Bev worked for a consumer loan company for more than 15 years. Today, instead of granting credit to people, she helps them with credit problems.

Bev recommends that the Salvatores reduce spending. Joan and Hank can eat at home more often than in restaurants and reduce other expenses, too. The extra money can be used to pay off their debt. These actions may not be pleasant, but the results will be satisfying. No more arguing about money and no more calls about late bill payments.

**What about you?** What work activities in the consumer credit field appeal to you? What will you have to do to achieve success in this career field?
Credit Fundamentals

USING CREDIT

Credit is the privilege of using someone else’s money for a period of time. That privilege is based on the belief that the person receiving credit will honor a promise to repay the amount owed at a future date. Two parties are involved in a credit transaction. Anyone who buys on credit or receives a loan is a debtor. The one who sells on credit or makes a loan is the creditor.

Although the credit system uses forms and legal documents, it also depends on trust between the debtor and creditor. This trust means that the creditor believes that the debtor will honor the promise to pay. Without that trust, the credit system could not operate.

When you borrow a large amount of money or buy on credit from a business, you will usually be asked to sign a written agreement. The agreement states that you will pay your debt within a certain period.

Focus on Real Life

In most economies, consumers, businesses, and governments use credit. For example, a person buys gas with an oil company credit card. A student applies for and receives a government loan to help with college expenses.

A business receives a $2 million loan to build a new store. Another company borrows $150,000 to finance the purchase of additional inventory.

The state of Louisiana may borrow $35 million through a bond issue to build new college buildings. A county board might borrow $250,000 to make emergency road repairs.

What do these people, businesses, and governmental institutions have in common? They all have wants, but lack the money to satisfy those wants. All of them borrow money to satisfy those wants. If they borrow, they will be using credit.

Besides a student loan, what other types of loans might you need to apply for in the next few years?
Types of Credit

Businesses use trade credit. *Trade credit* occurs when a company receives goods from a supplier and pays for them later.

Businesses may secure long-term loans for land, equipment, and buildings. They may also borrow money for shorter periods, usually for 30 to 90 days, to meet short-term needs for cash.

Local, state, and federal governments often use credit to provide goods and services that benefit the public. Governments may use credit to buy items such as cars, aircraft, and police uniforms. They may also borrow funds to build hospitals, highways, parks, and airports.

Most consumers use credit for various purposes. You may use credit to buy expensive products that will last a long time. You may also use credit for convenience in making smaller purchases.

If you borrow money to use for some special purpose, you are using *loan credit*. Loans are available from several kinds of financial institutions. Loan credit usually involves a written contract. The borrower agrees to repay the loan in specified amounts, called *installments*, over a period of time.

If you charge a purchase at the time you buy the good or service, you are using *sales credit*. Most businesses offer sales credit. Sales credit involves the use of charge accounts and credit cards by consumers.

Charge Accounts

A charge account represents a contract between the firm offering the account and the customer. Three types of charge accounts are generally available: regular, budget, and revolving.

**Regular Accounts** A regular charge account requires the buyer to make full payment within a stated period—usually 25 to 30 days. The seller may set a limit on the total amount that may be charged during that time. People use regular accounts for everyday needs and small purchases. Service providers, such as doctors, dentists, lawyers, and plumbers, commonly offer this type of credit.

**Budget Accounts** Some stores and utility companies offer *budget charge accounts*. This credit agreement requires that a customer make payments of a fixed amount over several months. One budget plan that businesses offer is the 90-day, three-payment plan. Under this plan, you pay for your purchase over a 90-day period, usually in three equal monthly payments.

FYI

*Trade credit terms are often stated “2/10, n/30.” This means that the business can take a 2 percent discount if the bill is paid within 10 days from the billing date. The full or net amount must be paid within 30 days.*

What are some reasons that a business would borrow funds?
With a utility company budget plan, the company makes an estimate for gas or electricity charges during a certain period, such as a year. You then agree to pay a certain amount each month to cover those charges. This plan avoids large payments during some times of the year. You pay the same amount each month.

**Revolving Accounts** The most popular form of sales credit is the revolving account. You may charge purchases at any time, but only part of the debt must be paid each month. Features of revolving credit include the following.

- A maximum amount may be owed at one time, called a *credit limit*.
- A payment is required once a month, but the total amount owed need not be paid at one time.
- A finance charge is added if the total amount owed is not paid. A *finance charge* is the total dollar cost of credit including interest and all other charges. You must pay this additional amount for the convenience of using credit.

Revolving charge accounts are convenient, but they can make overspending easy. The finance charges on unpaid balances can be quite high, sometimes \(1 \frac{1}{2}\) percent per month (18 percent per year) or higher. There is rarely a finance charge if balances are paid in full within a specified period, such as within 25 days.

**Credit Cards**

Charging purchases with credit cards is common. Most credit cards issued today are multipurpose cards. Consumers can use them at thousands of stores, hotels, airlines, and other businesses.

**Bank Cards** Bank credit cards have become very popular all over the world. MasterCard and VISA are two of the best known. Sometimes an annual fee must be paid for the privilege of using these cards.

Banks and various merchants make agreements to accept the credit cards. When you use your bank credit card, a credit card sales receipt is generated. At the end of the day, the store collects all credit card sales receipts and sends them to the bank. Next, the bank totals all of the credit sales receipts received from a business. The bank then pays the business for the sales amount minus a service fee.

This fee covers the bank’s expenses of processing the sales receipts and collecting amounts owed from customers. The bank is doing the work that the business’ own credit departments would have to do otherwise.

Business owners like bank credit cards since the bank takes on the liability and expense of granting credit. Customers like bank charge cards because they are accepted by many businesses all over the world.
Travel and Entertainment Cards  Carte Blanche, Diners Club, and American Express are widely used travel and entertainment (T&E) cards. Subscribers pay a yearly membership fee, usually higher than the fee for bank cards. Cardholders are not given a spending limit. They are usually expected to pay the full balance each month.

Business travelers like to use T&E cards because the detailed records they receive are useful for business and tax record keeping. They offer proof of travel expenses.

Oil Company Cards  Some major oil companies issue their own credit cards. Other oil companies have found that it costs them too much to offer credit. Instead, they issue cards affiliated with bank card companies. These credit cards are co-branded accounts.

Retail Store Cards  Many retail stores offer their own credit cards to customers. These cards show the name of the store that issues them. Customers can only use these cards at the issuing stores.

Installment Credit
For some expensive purchases, consumers often use a different type of credit. Installment sales credit is a contract issued by the seller that requires periodic payments at specified times. The seller adds finance charges to the cost of the items purchased. The credit agreement shows the total amount to be paid. Consumers often purchase furniture and household appliances with installment sales credit.

Using installment sales credit differs from using credit cards. The following are some features of installment credit.

- Signing a sales contract that shows the terms of the purchase.
- Receiving the purchased item at the time of the sale. Be aware that the seller has the right to repossess, or take back, an item if payments are not made on time.
- Making a down payment, which is a payment of part of the purchase price. It is usually made at the time of the purchase.
- Paying a finance charge on the amount owed.
- Making regular payments at stated times, usually weekly or monthly. For example, if a total of $120 is to be repaid in 12 monthly installments, $10 is paid each month.

In some cases, the seller charges a penalty if a payment is received after the due date. In others, all remaining payments may become due at once if only one payment is missed.

Consumer Loans
A loan is an alternative to charge account buying or installment sales credit. The terms of the loans and the requirements for securing the loans differ.

An installment loan is one in which you agree to make monthly payments in specific amounts over a period of time. The payments are installments. The total amount you repay includes the amount you borrowed plus the finance charge on your loan.

Another kind of loan is a single-payment loan. With this type of credit, you do not pay anything until the end of the loan period, possibly 60 or 90 days. At that time, you repay the full amount you borrowed plus the finance charge.

A lender needs some assurance that each loan will be repaid. If you are a
good credit risk, you may be able to sign a promissory note. A promissory note is a written promise to repay based on a debtor’s excellent credit history. The amount borrowed, usually with some interest, is due on a certain date. Figure 18-1 shows the names given to the different parts of a promissory note.

In some cases, the lender may ask you to offer some property you own, such as a car, a house, or jewelry, as security. Property that is used as security is called collateral. You give the lender the right to sell this property to get back the amount of the loan if you do not repay it. This type of loan is a secured loan.

What if you do not have an established credit history or any property to offer as security? You may be able to get a relative or friend who has property or a good credit history to sign your note. They become the legal cosigner. The cosigner of a note is responsible for payment of the note if you do not pay as promised.

**Figure 18-1**

Promissory Note

<table>
<thead>
<tr>
<th>Principal</th>
<th>the amount that is promised to be paid; the face of the note.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>the date on which a note is issued.</td>
</tr>
<tr>
<td>Time</td>
<td>the days or months from the date of the note until it should be paid.</td>
</tr>
<tr>
<td>Date of maturity</td>
<td>the date on which the note is due.</td>
</tr>
<tr>
<td>Payee</td>
<td>the one to whom the note is payable.</td>
</tr>
<tr>
<td>Interest rate</td>
<td>the rate paid for the use of the money.</td>
</tr>
<tr>
<td>Maker</td>
<td>the one who promises to make payment.</td>
</tr>
</tbody>
</table>

---

**Describe the benefits of using credit.**

**BENEFITS OF CREDIT**

Both businesses and consumers can benefit from credit use. The main advantages of credit for consumers include the following.

- **Convenience** Credit can make it easy for you to buy. You can shop without carrying much cash.

- **Immediate Possession** Credit allows you to have the item now. A family can buy a dishwasher on credit and begin using it at once.

- **Savings** Sometimes credit allows you to buy an item on sale at a good price. Some stores, especially department and furniture stores, send notices of special sales to credit customers.

- **Credit Rating** A person’s reputation for paying bills on time is known as a credit rating. If you buy on credit and pay your bills on time, you gain a reputation for being dependable. In that way, you establish a favorable credit rating. A credit rating is valuable when you might need to borrow money or when you want to make a major purchase.
• **Useful for Emergencies** Access to credit can help in unexpected situations. Sometimes you may not have enough cash and have an urgent need for something. For example, your car might need repairs.

**CHECKPOINT**

What are the main advantages of consumer credit?

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**CREDIT CONCERNS**

Buying on credit is convenient and can be beneficial. There are also some disadvantages if you are not careful.

• **Overbuying** A common spending hazard of credit involves buying something that is more expensive than you can afford. Attractive store displays and advertisements invite you to make further purchases.

• **Careless Buying** If you become lazy in your shopping, you may not shop carefully. You may fail to make comparisons, causing you to buy at the wrong time or the wrong place. Credit can tempt you not to wait for a better price on an item you want now.

• **Higher Prices** Stores that only accept cash may sell items at lower prices than stores that offer credit. Extending credit is expensive for stores. When customers do not pay as agreed, there are collection costs. Sometimes businesses must write off consumer debts as uncollectible. These increased costs often result in higher prices.

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**Technology Topics**

**Databases, Personal Privacy, and Identity Theft**

Information about you is readily available to many people. Businesses and governments all over the world use computer databases and electronic networks to store and exchange this information about you.

How is this information obtained? Most databases are created from information given voluntarily. For instance, you offer information when you apply for credit, obtain telephone service, apply for a driver’s license, obtain insurance, and answer survey questions.

Privacy is a basic right to have information about you kept confidential. Like most consumers, you are probably concerned about your privacy. While there is some reason to be concerned about databases and personal privacy, protections exist. Decisions about granting credit or obtaining insurance are most often based on accurate, up-to-date information. The information gathered is used for legitimate business reasons.

Various state and federal privacy laws continue to be under review. Government officials must decide what is private information and whether consumers should be asked to give permission before any credit or medical reports are released to others. In recent years, stronger privacy protection laws have been enacted. Identity theft is the fastest-growing financial crime. That’s the bad news. The good news is that the technology that is used to steal a person’s identity can also be used to protect it. Each year, credit card companies, retail stores, and online businesses are using improved security systems. These efforts help to ensure that your personal information and financial data will not be viewed or used by unauthorized individuals or companies.

**Think Critically**

1. What dangers are involved with having private information easily accessible to others?
2. Conduct a web search to determine actions you can take to protect your privacy.
• **Overuse of Credit** Buying now and paying later may sound like a good idea. If too many payments need to be made later, the total amount due can become a problem. Consumers must keep records of the total amount owed so that they do not have monthly payments that exceed their ability to pay.

**Questions to Ask**

Before making a final decision about whether to buy on credit, think about these important questions.

- How will you benefit from this use of credit?
- Is this the best buy you can make or should you shop around?
- What will be the total cost of your purchase, including the finance charges?
- What would you save if you paid cash?

**Assessment**

**Key Concepts**

Determine the best answer.

1. Large purchases (such as appliances and automobiles) are commonly bought using
   a. a bank credit card
   b. installment credit
   c. a charge account
   d. trade credit

2. Signing a promissory note occurs when using
   a. a credit card
   b. a charge account
   c. a loan
   d. trade credit

3. Which of the following is an advantage of using credit?
   a. overbuying
   b. convenience
   c. higher prices
   d. lower credit rating

**Make Academic Connections**

4. **Marketing** Collect advertisements from newspapers, magazines, and web sites for companies that offer credit. What types of credit are offered? Is the company selling credit as its primary product or using credit to promote the sale of other goods and services?

5. **Economics** Prepare a written or oral summary of the benefits and costs of consumer credit for a country’s economy.
**FINDING INTEREST**

Borrowing money has a cost. Interest, $I$, is the cost of using someone else’s money. The amount of interest paid on a loan or charge account should be clearly understood. To determine this amount, you need to know the following.

1. **Principal, $P$** Amount of the loan.
2. **Interest Rate, $R$** Percent of interest charged or earned. Remember that a percent can also be expressed as a decimal or a fraction. The symbol for percent is $\%$.
3. **Time, $T$** Length of time for which interest will be charged, usually expressed in years or parts of a year.

**Simple Interest**

On single-payment loans, interest is usually *simple interest*. The formula for computing simple interest is

$$I = P \times R \times T$$
Suppose you borrow $100 (P) at 12% (R) for one year (T). To calculate the amount of interest, first change 12% to a decimal, 0.12. Using the formula, the interest is $12.

\[ I = P \times R \times T \]
\[ I = $100 \times 0.12 \times 1 = $12 \]

If you borrow $100 at 12% for two years, you pay twice as much interest, or $24.

\[ I = P \times R \times T \]
\[ I = $1,000 \times 0.12 \times 2 = $24 \]

If you borrow the money for three years, you pay $240, and so on.

**Time in Months** Your loan may be for one month instead of one year. How is simple interest calculated for less than a year? The amount of interest is based on the portion of the year. There are 12 months in a year, so one month is one-twelfth of a year, regardless of the number of days in the particular month.

If you borrow $100 at 12% for one month, the interest is

\[ I = P \times R \times T \]
\[ I = $100 \times 0.12 \times \frac{1}{12} = $1 \]

**Time in Days** A loan may be for a certain number of days such as 30, 60, or 90 days. To make the computation easy, a year is often considered as 360 days. The interest on a loan of $100 at 12% for 60 days is $2.

\[ I = P \times R \times T \]
\[ I = $100 \times 0.12 \times \frac{60}{360} = $2 \]

**Maturity Dates**
The date on which a loan must be repaid is the **maturity date**. When the time of the loan is stated in months, the date of maturity is the same day of the month as the date on which the loan was made. A one-month loan made on January 15 will be due February 15. A two-month loan will be due March 15, and so on.

When the time is in days, you must count the exact number of days to find the date of maturity. First, determine the number of days remaining in the month when the loan was made. For example, if the loan was made on January 10, there would be 21 days counted in January, since there are 31 days in January. Then add the days in the following months until the total equals the required number of days.

Suppose you want to find the date of maturity of a 90-day loan made on March 4. First find the number of days remaining in March. Then add the days in the following months until you reach 90 days.

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>March</td>
<td>27 days (31–4)</td>
</tr>
<tr>
<td>April</td>
<td>30 days</td>
</tr>
<tr>
<td>May</td>
<td>31 days</td>
</tr>
<tr>
<td>June</td>
<td>2 days</td>
</tr>
<tr>
<td>Total</td>
<td>90 days</td>
</tr>
</tbody>
</table>

Therefore, the due date is June 2.
Installment Interest

When you borrow money, you usually make several partial payments instead of one large single payment. A loan that you repay in partial payments is an installment loan (or consumer loan). Each payment is an installment.

Banks, credit unions, and consumer finance companies all offer installment loans. With an installment loan, the bank gives the borrower a schedule of payments. It shows how much the borrower must pay each month.

With some loans, the lender adds the amount of the interest to the amount you borrow. You sign a promissory note for the total amount. You then repay the note in equal monthly installments.

Suppose you borrow $100, sign a note for $110, and agree to repay the loan in 12 monthly installments of $9.17 each. If you had borrowed $100 for one year and paid $110 at maturity, the interest rate would be 10%.

$10 ÷ $100 = 0.10 or 10%

However, you paid off just part of the loan each month. You had the use of the entire $100 for one month and a smaller amount each succeeding month as you repaid the loan. In this case, the true interest rate amounts to 18.5%.

Decreasing Loan Payments

On some installment loans, interest is calculated on the amount that is unpaid at the end of each month. Suppose that a person borrowed $120 and agreed to repay the loan at $20 a month plus 11.2% interest each month on the unpaid balance. Figure 18-2 shows the schedule of decreasing payments.

### Decreasing Loan Payment Schedule

$120 loan, 18% interest rate, monthly payments are $20 plus interest

<table>
<thead>
<tr>
<th>Months</th>
<th>Unpaid Balance</th>
<th>Interest Paid</th>
<th>Loan Repayment</th>
<th>Total Payment</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>$120</td>
<td>$1.80</td>
<td>$20</td>
<td>$21.80</td>
</tr>
<tr>
<td>2</td>
<td>100</td>
<td>1.50</td>
<td>20</td>
<td>21.50</td>
</tr>
<tr>
<td>3</td>
<td>80</td>
<td>1.20</td>
<td>20</td>
<td>21.20</td>
</tr>
<tr>
<td>4</td>
<td>60</td>
<td>0.90</td>
<td>20</td>
<td>20.90</td>
</tr>
<tr>
<td>5</td>
<td>40</td>
<td>0.60</td>
<td>20</td>
<td>20.60</td>
</tr>
<tr>
<td>6</td>
<td>20</td>
<td>0.30</td>
<td>20</td>
<td>20.30</td>
</tr>
<tr>
<td>Totals</td>
<td></td>
<td>$6.30</td>
<td>$120</td>
<td>$126.30</td>
</tr>
</tbody>
</table>

Why is it important to know the amount of interest you will pay on a loan?
Another person obtained a loan for $1,000 and agreed to repay $100 per month. The lender applies the payment to principal and interest. The borrower makes payments each month on a level payment schedule. Figure 18-3 shows this repayment schedule. Loan transactions use both kinds of payment schedules.

**FINANCE CHARGES**

Before you borrow money or charge a purchase, you should know the exact cost of using credit.

**Annual Percentage Rate**

The annual percentage rate (APR) is a disclosure required by law. It states the percentage cost of credit on a yearly basis. All credit agreements, whether for sales credit or loan credit, require disclosure of the APR.

In addition to interest, the APR includes other charges that may be made. Service fees involve the time and money it takes a creditor to investigate your credit history, process your loan or charge account application, and keep records of your payments and balances.

The costs of collecting from those who do not pay their accounts may also be passed on to other borrowers. Uncollectible accounts are frequently referred to as bad debts or doubtful accounts.

Lenders may also add an amount to cover the cost of credit insurance. This coverage repays the balance of the

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**Level Loan Payment Schedule**

$1,000 loan, 12% interest rate, monthly payments are $100

<table>
<thead>
<tr>
<th>Payment</th>
<th>Interest</th>
<th>Applied to Principal</th>
<th>Loan Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>$100.00</td>
<td>$10.00</td>
<td>$90.00</td>
<td>$910.00</td>
</tr>
<tr>
<td>100.00</td>
<td>9.10</td>
<td>90.90</td>
<td>819.10</td>
</tr>
<tr>
<td>100.00</td>
<td>8.19</td>
<td>91.81</td>
<td>727.29</td>
</tr>
<tr>
<td>100.00</td>
<td>7.28</td>
<td>92.72</td>
<td>634.57</td>
</tr>
<tr>
<td>100.00</td>
<td>6.35</td>
<td>93.65</td>
<td>540.92</td>
</tr>
<tr>
<td>100.00</td>
<td>5.41</td>
<td>94.59</td>
<td>446.33</td>
</tr>
<tr>
<td>100.00</td>
<td>4.46</td>
<td>95.54</td>
<td>350.79</td>
</tr>
<tr>
<td>100.00</td>
<td>3.51</td>
<td>96.49</td>
<td>254.30</td>
</tr>
<tr>
<td>100.00</td>
<td>2.54</td>
<td>97.46</td>
<td>156.84</td>
</tr>
<tr>
<td>100.00</td>
<td>1.57</td>
<td>98.43</td>
<td>58.41</td>
</tr>
<tr>
<td>58.99</td>
<td>0.58</td>
<td>58.41</td>
<td>--</td>
</tr>
</tbody>
</table>
amount owed if the borrower dies or becomes disabled.

**Total Dollar Charges**
To make you aware of the total cost of credit, federal law requires that the lender must tell you the finance charge. The *finance charge* is the total dollar cost of credit, including interest and all other charges. Either your contract or your charge account statement must state this finance charge.

**Compare Credit Costs**
If you have to borrow money or buy on credit, be sure to compare the total cost of credit among alternative sources. Check with several lenders and compare the APRs.

If you make a purchase with a credit card, know which card has the lowest APR. If an installment sales contract is required, think about whether an installment loan from a financial institution may be cheaper for you.

When getting a loan, shop around just as carefully as you would for any major purchase. Borrowing money is costly, so make sure that you get the best loan. Some of the things you should check include the annual percentage rate, the amount of the monthly payments, and the finance charge.

Always remember that when you use credit, you are spending future income. If you decide to use credit, the benefits of making the purchase now should outweigh the costs of using credit.

Effectively used, credit can help you have more and enjoy more. Misused, credit can result in too much debt, loss of reputation, and even bankruptcy.

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**18-2 Assessment**

**Key Concepts**

> Determine the best answer.

1. True or False. The principal of a loan is the total amount of interest that will be paid.
2. True or False. Interest rates are stated on the basis of one year even if a loan is for several years.
3. The most valuable number to consider when comparing credit among various borrowing sources is the
   a. total finance charge
   b. maturity date
   c. annual percentage rate
   d. principal

**Make Academic Connections**

4. **Math** Calculate the amount of interest for each of the following loans.
   a. $6,000 borrowed for 1 year at 7%
   b. $2,000 borrowed for 4 months at 8%
   c. $1,100 borrowed for 2 1/2 years at 6%

5. **Economics** Several types of interest rates exist in every economy. Use library materials or an Internet search to determine common reported interest rates. Which of these rates are related to consumer credit?
Trust between a borrower and lender is vital if credit is to be granted. To obtain a loan or credit card, you must prove that you are a good credit risk. Not everyone who desires credit will receive it. Lenders need certain information in order to make a decision about whether to grant credit. They want to be assured of two things: your ability to repay a debt and your willingness to do so.

The Three Cs of Credit

In deciding whether to grant you credit, businesses consider three main factors, known as the three Cs—character, capacity, and capital.

Character refers to your honesty and willingness to pay a debt when it is due. If you have a reputation for paying bills on time, you will meet an important condition for being considered a good credit risk.

Capacity refers to a person’s ability to pay a debt when it is due. The lender or seller must decide whether your income is large enough to permit you to pay your bills. If your income is too small or unsteady, granting you further credit may not be wise. In contrast, your income may be high, but if you have other debts, you may not be able to handle more payments.

Capital is the value of the borrower’s possessions. Capital includes the money and property you own. Your capital may include a car that is paid for and a house on which a large amount has been paid. A checking account and savings also add to your capital. On the other hand, you may have nothing except your present income. The amount of capital gives the lender some assurance that you will be able to meet your credit obligations.

Credit Applications

When you apply for credit or a loan, the lender will ask you to fill out an application. A credit application is a form on which you provide information needed by a lender to make a decision about granting credit. See Figure 18-4.
One of the most important parts of a credit application is your credit references—businesses or individuals who are able and willing to provide information about your creditworthiness. Your signature on the application

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**CREDIT CARD APPLICATION**

**Important:** Fill in all information requested below.

1. **Information About Yourself** *(Name of person in whose name card will be issued)*

   - **Mr.**
   - **Mrs.**
   - **Miss**
   - **Ms.**

   **First Name**
   **Middle**
   **Last Name**

   *(Courtesy titles are optional)*

   **Home Address**
   **Apt. City State ZIP Code**
   **How Long?**
   **Years Mo.**

   **Previous Address** *(if less than 2 years at present address)*
   **Apt. City State ZIP Code**

   **Home Telephone**
   **Business Telephone**
   **Social Security Number**
   **Date of Birth**
   / /
   **No. of Dependents** *(Exclude Yourself)*

   **Are You a U.S. Citizen?**
   **Yes**
   **No**

   **If No, Explain Immigration Status**

   **Are You a Permanent Resident?**
   **Yes**
   **No**

   **Do You:**
   **Monthly Rent or Mortgage $**

2. **Employment Information** *(Your total yearly income from all sources)*

   **Employer**
   **Address**
   **City State ZIP Code**

   **Former Employer** *(if less than 1 year with present employer)*
   **Address**
   **City State ZIP Code**

   **Occupation**
   **Yearly Gross Salary $**

   **Other Income**
   **Source**

   **No. of Dependents** *(Exclude Yourself)*

   **Years**
   **Mos.**

   **How Long?**

   **Former Employer**

3. **Other Credit**

   **Major Credit Cards** *(Visa, MasterCard, etc.)*
   **Account Number**

   **Other Credit Cards** *(Dept. Stores, etc.)*
   **Account Number**

   **Other Credit**
   **Account Number**

4. **Banking Information**

   **Checking**
   **Name of Bank**
   **City**
   **Account Number**

   **Savings**
   **Name of Bank (if different from above)**
   **City**
   **Account Number**

   **Other (Check here if you have any of the following):**
   **IRA**
   **Money Market Account**
   **Investments**
   **CD**
   **Stocks/Bonds**
   **Cash Management Account**

5. **Joint Account Information** *(Complete for joint account or if you are relying on the income of another person to qualify for an account)*

   **First Name**
   **Middle**
   **Last Name**
   **Relation**

   **Employer**
   **Address**
   **City State ZIP Code**

   **How Long?**
   **Years Mo.**

   **Former Employer**

6. **Additional Cards** *(Complete this section if you want cards issued to additional buyers on your account)*

   **1. Spouse**
   **First Name**
   **Middle**
   **Last Name**

   **2. Other**
   **First Name**
   **Middle**
   **Last Name**

7. **Signatures**

   - **Applicant’s Signature**
   - **Joint Applicant’s Signature**

   *(I authorize the Second National BankCorp to check my credit record and to verify my credit, employment and income references. I have read the important information on the reverse side. I understand Second National BankCorp may amend the account terms and charges specified in the Cardmember Agreement in the future.)*

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**Figure 18-4**

Why is it important to fill in the blanks and to do so accurately?
Building a good record of creditworthiness can be important. You can begin while you are still in school. Trust and reliability are important in matters of credit. You can help to establish yourself by having a good record of grades and attendance. Both employers and lenders know that school behavior patterns tend to carry on later in life.

In addition, start a checking and savings account. If you keep a balance in each account, a lender can see that you can handle money. Making regular deposits to your savings account also suggests that you will be a good credit risk.

Some people establish credit records by charging small purchases. You may buy a sweater on credit and make the payments according to the agreement. This action is an important step toward proving you are a good credit risk. You may want to pay off your account within 30 days and avoid an interest charge. Either way, you will be building a good credit record.

Having a good part-time or full-time employment record also helps to start a favorable credit record. Changing jobs often does not look good. Being on a job for two or more years is a positive part of a good credit record.

Other information that lenders will want to know relates to your finances. You will need to report how much you earn, what kinds of savings and investments you have, and whether you have any other sources of income. A lender may also want to know about your reliability. In other words, they will want to know your occupation, how long you have been with your present employer, how long you have lived at the same address, and whether you own or rent your home.

**Actions to Establish Credit**

**What are the three Cs of credit?**

- **Character**: Your creditworthiness is based on your past behavior. Employers and lenders look for a history of timely payments and负责任 behavior.
- **Capacity**: This refers to your ability to pay. Lenders want to know that you have the means to pay back the loan.
- **Collateral**: This is something of value that you can use to secure the loan. It provides a backup in case you default on payments.

Having a good employment and educational record also helps to start a favorable credit record. Having a good credit history is crucial for obtaining loans, mortgages, and other financial transactions.
CREDIT BUREAU

In addition to checking with your credit references, a lender will usually check with a credit bureau. A credit bureau, or credit reporting agency, is a company that gathers information on credit users. It sells that information to businesses offering credit. Banks, finance companies, and retail stores are among the customers of credit bureaus.

Credit bureaus keep debt records of consumers. They can record only information that is officially reported to them. The information shows if payments are up to date or overdue and if any action has been taken to collect overdue bills. Other credit bureau information may be added to create a month-by-month credit history for the consumer accounts.

Credit bureaus cooperate with each other. They provide information to other credit bureaus. If you are new to an area, the local credit bureau can obtain information from the bureau in your previous community.

Credit Report

A credit bureau uses your record to grade you as a credit risk. Your credit report shows the debts you owe, how often you use credit, and whether you pay your debts on time. Figure 18-5 shows a credit report that a credit bureau may issue. Credit bureaus do not make value judgments about any

Credit Report

FOR
FIRST NATIONAL BANK
Arborville, MT 83206

REPORT ON: LAST NAME: SOCOLO
SOCIAL SECURITY NUMBER: 123-45-6789
ADDRESS: 5421 MAPLE AVENUE CITY: ARBORVILLE
MT ZIP CODE: 83206

PRESENT EMPLOYER: THE ARTIST'S LOFT, INC.
POSITION HELD: ARTIST, MGR.
SINCE: 10/90
GROSS DIAMETER: 5,000

CREDIT HISTORY (Complete this section for all reports)

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<th>FIRST NAME</th>
<th>INITIAL</th>
<th>SOCIAL SECURITY NUMBER</th>
<th>SPONSOR'S NAME</th>
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Credit Report

FYI

The three major companies that store data on consumers and provide information to lenders are Experian, Equifax, and Trans Union. Equifax maintains over 190 million credit files on U.S. consumers.

Figure 18-5

What kind of information would be on your credit report?
individual. The bureau simply gathers facts as reported to them.

Your credit record is confidential. That is, only you or those who have a legitimate reason for examining it can obtain it.

The top half contains background information about the individual. The bottom half lists information about the individual’s accounts and payment history. Note that at the bottom there is a reference to a public record. It shows a dispute between the consumer and a creditor that was settled in a small claims court. All of this information is of interest to credit grantors.

> WORK AS A GROUP

Create a contract that might be used in a consumer credit situation. What information should be included in the contract? How should the information be worded so consumers better understand what they are signing?

CREDIT DOCUMENTS

Credit is important in many ways. Millions of consumers and businesses enjoy this privilege. No matter what kind of credit is involved, both parties have legal responsibilities.

You can help maintain a good credit record by keeping track of your purchases and payments. When you buy on credit, you should keep a copy of the sales slip, credit card receipt, or other documents. As you make payments by check, keep track of the date and check number.

Credit Contracts

“KWYS” are four letters to keep in mind when signing any legal form.

These letters stand for “know what you’re signing.” This principle applies to all credit contracts. An installment contract is one of the most important forms you may sign. Before signing one, consider the following questions.

- How much are the finance charges? Are they clearly shown on the contract?
- Does the contract include the cost of services you may need, such as repairs to a television or a washing machine?
- Does the contract have an add-on feature so that you can later buy other items?
- If you pay the contract in full before the ending date, will the finance charge be reduced?
- Is the contract completely filled in before you sign? Be sure to draw a line through any blank space before signing.
- Will you be given a copy of the contract?
• Under what conditions can the seller repossess the merchandise if you do not pay on time?

**Statement of Account**

As a credit card or charge account customer, you will receive a monthly summary of your account. The **statement of account**, or simply the **statement**, is a record of the transactions completed during the billing period. Most statements report the following information.

• The balance that was due when the last statement was mailed

**Did Glen Bower make a payment on this account during the previous month? Why?**

**Figure 18-6**

---

**Monthly Credit Statement**

**WEST SIDE DEPARTMENT STORE**

P. O. BOX 34577
JACKSONVILLE, MO 40232

0140472

Mr. Glen Bower
98176 Cooper Rd.
Pontiac, MO 05015-8857

5080615965818

**MAIL ANY BILLING ERROR NOTICE TO: WestSide Department Store at address shown below**

P. O. BOX 34577  JACKSONVILLE  MO 40232  406-555-1356  MON-FRI  9-5

---

**FINANCE CHARGE**

**MONTHLY PERIODIC RATES**

**ANNUAL PERCENTAGE RATE(S)**

<table>
<thead>
<tr>
<th>FINANCE CHARGE RATE(S)</th>
<th>MONTHLY PERIODIC RATE(S)</th>
<th>ANNUAL PERCENTAGE RATE(S)</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ .01 TO $28.50</td>
<td>1.75%</td>
<td>21%</td>
</tr>
<tr>
<td>$28.51 AND ABOVE</td>
<td>52%</td>
<td></td>
</tr>
</tbody>
</table>

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**Notice:**

To avoid a FINANCE CHARGE next month, pay the NEW BALANCE shown above within 30 days (28 days for February statements) from BILLING DATE. If you prefer to pay in installments, pay the MINIMUM PAYMENT shown above, or more, within 30 days (28 days for February statements) from BILLING DATE. If you pay by mail, payments received prior to 1 p.m. on a banking day will be credited as of the date received. Payments received after 1 p.m. will be credited the following banking day. The sooner you pay and the more you pay, the smaller your FINANCE CHARGE.

---

**ATTENTION: SEE REVERSE SIDE FOR IMPORTANT INFORMATION.**

---

**Figure 18-6**

---

**Did Glen Bower make a payment on this account during the previous month? Why?**

---

**Figure 18-6**

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**Did Glen Bower make a payment on this account during the previous month? Why?**

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**Figure 18-6**

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**Did Glen Bower make a payment on this account during the previous month? Why?**

---

**Figure 18-6**

---

**Did Glen Bower make a payment on this account during the previous month? Why?**

---

**Figure 18-6**
Accuracy of Records
Keeping accurate records will help you avoid credit record problems. Accurate record keeping is a good personal business practice.

Many errors are simply honest mistakes. Businesses are as eager to correct them as you are. Your creditworthiness may be at stake. Bad publicity may also hurt the reputation of the business if errors are not corrected.

Avoiding Fraud
The Federal Trade Commission reports that credit card fraud is a major problem. To avoid loss due to fraud, you should check your credit card account statements very carefully for errors.

Each month, you should check the accuracy of your statement by comparing it with your copies of sales slips. Verify payments and other credits, such as amounts subtracted when merchandise is returned. If you discover an error on a statement, you should notify the business at once.

What safety precautions are in place on the Internet to prevent credit card fraud?

CHECKPOINT
What are the main items reported on a statement of account?

18-3 Assessment

Key Concepts
Determine the best answer.

1. A reputation for paying bills on time relates to a person’s
   a. capacity  b. collateral  c. character  d. capital

2. The main activity of a credit bureau is to
   a. calculate the cost of credit for lenders and borrowers
   b. determine when a person is overusing credit
   c. contact a government agency when lenders overcharge for credit
   d. report information on the use of credit by consumers

Make Academic Connections

3. Business Math Don Ghonski received his credit card statement. This report showed $45 in new purchases, a current balance of $178, a payment of $70, and finance charges of $2. What was the amount of Don’s beginning balance from the previous month?

4. Technology Go to the web site of one of the major credit reporting agencies. What services does the agency provide for businesses? What information is available to assist consumers?
Protection of Credit Rights

Goals

> Identify credit application regulations.
> Explain credit use regulations.
> Discuss credit problems and available assistance.

Key Terms

credit counselor
bankruptcy

Focus on Real Life

Ben Khan mistakenly leaves a credit card lying on a counter at a store. After asking at the store and waiting a few weeks, he realizes the card will not be returned. On his next statement, more than $200 worth of merchandise was charged.

Julie Roma checks her charge account statement and finds several errors on it. One charge is for a purchase she did not make, and this is the third month in a row that this charge has shown up on the statement.

Your friends, Monique and Gary Buckman, had their loan application turned down. The loan officer explained that their credit bureau report was not good. Monique and Gary were shocked. They always pay their bills on time, with only a few minor exceptions. They need this loan for home improvements.

These credit problems can happen to anyone. If consumers know about credit laws and regulations, they can take actions to avoid and correct problems.

CREDIT APPLICATION REGULATIONS

Most businesses are honest in their business dealings. Unfortunately, some are not. Because of this, it became necessary for federal and state governments to pass laws to protect credit consumers.

Truth-in-Lending Law

The Truth-in-Lending Law of 1968 was the first of a series of credit protection laws. Truth-in-Lending requires that you be told the cost of credit before signing an agreement. The law requires that the lender must clearly state the annual percentage rate (APR) and total finance charge.

The Truth-in-Lending Law also protects consumers against unauthorized use of credit cards. The law limits your liability to $50 for unauthorized credit card purchases made prior to notifying the card issuer. You are not liable for any fraudulent charges made after you have notified the credit card company. You can notify the company by telephone, but you should also put your notification in writing.

What are some reasons that a loan application would be turned down?

> Identify credit application regulations.
Equal Credit Opportunity Act

The Equal Credit Opportunity Act prohibits creditors from denying a person credit because of age, race, sex, or marital status. Young people who may have just entered the labor market cannot be denied credit based only on age. Older, possibly retired, people also have special protection under this act.

Married women who previously found it difficult to establish credit in their own names now have a legal right to do so. Under this law, a woman has a right to her own credit if she proves to be creditworthy.

Unless your state still requires a person to be at least 21 to enter into a contract, a creditor cannot deny you credit based on your age alone. A creditor must look into your creditworthiness. Upon request, a creditor must give any person who is denied credit a written statement of the reasons for denial.

Credit Use Regulations

Several laws have been created to protect your rights when using credit.

Fair Credit Billing Act

The Fair Credit Billing Act requires prompt correction of billing mistakes. To get a correction of an error, you must notify the creditor in writing within 60 days after your statement was mailed. A good rule is to report errors as soon as you discover them. After you report an error, remember the following points.

- While waiting for an answer, you are not required to pay any amount in question.
- The creditor must acknowledge your complaint within 30 days unless your statement is corrected before that time.
- You do not pay finance charges on any amount in error.
- If no error is found, the creditor must bill you again. The bill may include finance charges that have
accumulated plus any minimum payments that were missed while the statement was being questioned.

The Fair Credit Billing Act also provides that you may withhold payment of any balance due on defective merchandise or services purchased with a credit card. Your first step should be to contact the business and try to resolve the problem. You can correct many situations if your complaint is made in a courteous but firm manner. The law protects you if you have made this “good faith” effort to work with the business.

**Fair Credit Reporting Act**
The *Fair Credit Reporting Act* is the law that gives consumers the right to know what information credit bureaus are giving to potential creditors, employers, and insurers. This law provides that if credit is denied based on information in a credit report, the applicant must be given the name, address, and phone number of the credit bureau that provided the information. In addition, credit records for both a husband and wife are kept if both are responsible for the debt. This allows a credit history to be developed for each spouse.

Prior to the passage of this law, many consumers were unaware that potential lenders had access to reports on their bill-paying habits. This act makes those reports available to the consumer. It provides ways in which consumers can access and correct information.

The Fair Credit Reporting Act also requires that credit bureaus must delete any information dealing with a personal bankruptcy that is more than ten years old. The credit bureau must also delete any other adverse information if it is more than seven years old.

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**A Question of Ethics**

**Pawnshops, Payday Loans, and Credit Repair**

Consumer credit is an area where unfair and deceitful business credit practices thrive. Pawnshops lend money based on the value of property, such as jewelry. These small loans are usually repaid in a month or two, but typically at a high interest rate. Some states allow pawnshops to charge 3 percent a month—that's 36 percent a year.

People in need of a small amount of money for a short time may use a payday loan. Nearly 10,000 of these companies now operate in the U.S. The interest rate for this cash advance can be over 600 percent. With a payday loan, a consumer may write a personal check for $230 to borrow $200 for 14 days. The lender agrees to hold the check until the next payday. This $30 finance charge for the 14 days translates into an APR of nearly 400 percent. Often, a customer continues to borrow without paying anything back. Within a few weeks, the finance charge can exceed the amount borrowed.

“Credit Repair—Are you in trouble with past due payments? Is your credit record being ruined? We can fix all problems quickly—come in today.” Every day, credit repair companies offer to help consumers with poor credit histories. They promise to improve your credit rating, for a fee. Too often, after paying hundreds of dollars, consumers get nothing. Companies disappear with your money. To protect consumers, the Credit Repair Organizations Act requires that credit repair companies cannot collect their fee until completing the promised services.

**Think Critically**

1. Why are people attracted to these credit situations?
2. Conduct research to obtain additional information about pawnshops, payday loans, and credit repair companies.
Consumer Credit Reporting Reform Act

An unfavorable credit report can force you to pay a higher interest rate on a loan or you might be denied a loan. The Consumer Credit Reporting Reform Act places the burden of proof for accurate credit information on the credit reporting agency rather than on you. Under this law, the creditor must certify that disputed data is accurate. If a creditor or the credit bureau verifies incorrect data, you can sue for damages. The federal government and state attorneys general can also sue creditors for civil damages.

Fair Debt Collections Act

A debt collection agency attempts to obtain money that is past due. The agency may contact people who are overdue with credit payments.

To prevent threats and other inappropriate actions, the Fair Debt Collection Practices Act requires that debt collectors treat you fairly. It bans various debt collection actions. This law does not take away the debts that are owed.

A debt collector may contact you in person, by mail, telephone, telegram, or fax. A debt collector may not contact you at inconvenient times or places, such as before 8 a.m. or after 9 p.m. They also may not contact you at work if your employer prohibits such contact.

CREDIT PROBLEMS AND ASSISTANCE

A person who cannot pay his or her bills when they are due might take these four steps.

1. Contact creditors and explain the situation.
2. Make a realistic proposal for when and what you can pay. Don’t just say, “I can’t pay.”
4. Make a written copy of your agreement to avoid disagreements later.

What can a credit counselor do for people with credit problems?
You may be able to work out a debt repayment plan. A creditor and a debtor develop this agreement to reduce payments to a more manageable level and still pay off the debt. This plan is good for both the creditor and the debtor.

One thing to avoid is being misled by advertisements that tell you, “Erase bad credit! 100% guaranteed.” Claims such as these are fraudulent. No one can unconditionally correct a bad credit record—it does not work that way. If you need help with a credit problem, contact a reputable credit counseling organization.

**Credit Counseling**

Different kinds of help are available to people with credit problems. A credit counselor discusses and suggests actions to take to reduce spending and eliminate credit difficulties.

Various nonprofit counseling services are available around the country. The National Foundation of Consumer Credit and the Consumer Credit Counseling Service (CCCS) can direct you to a local credit assistance program. This nonprofit organization has hundreds of affiliate offices around the country. Consumers are warned to be cautious of for-profit credit counseling services.

**Bankruptcy**

Consumers may take one additional step when facing credit problems. They should use this final option only for extreme situations. Bankruptcy is the legal process of reducing or eliminating an amount owed. This process is costly and requires legal assistance. Consumers can usually avoid bankruptcy by using credit wisely and practicing sensible money management.

---

**18-4 Assessment**

**Key Concepts**

Determine the best answer.

1. A person may be denied credit on the basis of his or her
   - a. sex
   - b. age
   - c. income
   - d. type of job

2. The federal law that provides protection when an error occurs on a monthly statement is the
   - a. Truth-in-Lending Law
   - b. Fair Credit Reporting Act
   - c. Fair Credit Billing Act
   - d. Equal Credit Opportunity Act

**Make Academic Connections**

3. **Statistics** Obtain current data about the number of people who have declared personal bankruptcy in recent years. Prepare a chart to show the trend of these data. Give an explanation as to why the trend occurred. What are the costs of bankruptcy to a society?

4. **Communication** Create a role-playing situation in which you are denied credit. Have one person explain how he or she encountered credit problems. Have the other person suggest actions to eliminate the credit problems.
>> Business Notes

18-1  Credit Fundamentals
1. Credit is the privilege of using someone else’s money with the obligation to repay it at a future time. The major types of consumer credit are charge accounts, credit cards, installment credit, and consumer loans.

2. Credit used wisely makes some buying more convenient, gives the purchaser immediate possession rather than waiting until later, allows buyers to take advantage of special sales, and establishes a person’s credit rating.

3. Credit is misused if it results in overbuying, careless buying, paying higher prices in stores that grant credit, or incurring excessive debt.

18-2  Cost of Credit
4. The amount of interest is calculated by multiplying the interest rate times the principal times the number of days or months.

5. The annual percentage rate (APR) states the percentage cost of credit on a yearly basis. Costs of credit in addition to interest include service fees, the cost of collecting bad debts, and credit insurance. The finance charge is the total dollar cost of credit including interest and all other charges.

6. The cost of credit varies among lenders. You can save money by shopping around to compare the APR, amount of monthly payments, and total finance charge.

18-3  Credit Application and Documents
7. A credit application is a document on which you provide information needed by a lender. A business considers a person’s character (honesty and willingness to pay debts), capacity (the ability to pay debts), and capital (the value of the person’s possessions) in reviewing an applicant for credit.

8. A credit bureau gathers information on credit users. A credit record documents your credit history. You can maintain a good credit history by paying your bills on time.

9. Two commonly used credit documents are the installment contract and the statement of account. Before signing an installment contract, consider the finance charges and other features of the loan. Credit statements should be checked carefully and errors reported as soon as they are discovered.

18-4  Protection of Credit Rights
10. The Truth-in-Lending Law and the Equal Credit Opportunity Act provide information and protection when applying for credit.

11. The Fair Credit Billing Act, the Fair Credit Reporting Act, the Consumer Credit Reporting Act, and the Fair Debt Collections Act protect consumers when using credit.

12. Assistance with credit problems is available from counselors, debt consolidation, and, as a last option, bankruptcy.

>> Communicate Business Concepts

1. Edward Adiska buys everything he possibly can on credit. If he does not have enough money to cover his monthly payments when they are due, he borrows money to pay them. His sister, Debbie, likes to buy things only after she has saved enough money to pay cash for them.
   a. Whose plan do you think is better? Why?
   b. What suggestions about the use of credit might you make to Edward and Debbie?

2. Gerry Shadle owns and operates a flower shop. She is considering expanding her shop to include home decorating items. At present, Gerry sells for cash only. How might extending credit help or hurt her business?

3. Read the following statements and explain why you agree or disagree.
   a. “A bank card is nice to have. If I’m out of cash, I can still buy what I want.”
b. “I don’t believe in using credit for most purchases. I pay cash for everyday items and use credit only for expensive items, such as a new refrigerator.”

c. “If I can’t pay cash, I can’t afford it. I won’t buy anything unless I can pay cash.”

d. “I often don’t pay the full amount of my charge account when it is due; the finance charges are quite reasonable.”

4. Les Heddle needed to borrow $15,000 to do some remodeling in his store and has three options:

   OPTION 1: The Thrifty Loan Company offered him an APR of 16% for a three-year loan. Monthly payments, including finance charges, would be $555.

   OPTION 2: The Green-back Bank offered him a five-year loan at 15% APR with a total monthly payment of $375.

   OPTION 3: The Silk Purse Finance Lending Shop did not quote an APR figure but said, “We have a ‘no frills’ loan policy, and you can have a four-year loan with monthly payments at the amazingly low figure of $496 per month.”

   Construct a loan comparison chart showing the lender, APR, loan length, monthly payment, total payment, and cost of credit. Then decide which loan would be the best for Les Heddle. Give reasons for your decision.

5. Suzanne Winters does not believe in buying anything on credit. She says too many people get into trouble with credit and many errors are made in credit transactions. Explain to Suzanne ways in which laws protect consumers who engage in credit transactions and tell her about some of the help that is available for consumers who have credit problems.

---

**Develop Your Business Language**

Match the terms listed with the definitions.

6. Your reputation for paying your bills on time.

7. Someone who becomes responsible for payment of a note if you do not pay as promised.

8. The privilege of using someone else’s money for a period of time.

9. A loan in which you agree to make monthly payments in specific amounts over a period of time.

10. The legal process of reducing or eliminating an amount owed.

11. A person who suggests actions to reduce and eliminate credit difficulties.

12. A payment of part of the purchase price that is made as part of a credit agreement.

13. A written promise to repay based on the debtor’s excellent credit rating.

14. Property that is offered as security for some loan agreements.

15. The total dollar cost of credit, including interest and all other charges.

16. The percentage cost of credit on a yearly basis.

17. A company that gathers information on credit users and sells that information in the form of credit reports to credit grantors.

18. A record of the transactions that you have completed with a business during a billing period.

19. A form in which you provide information needed by a lender to make a decision about granting credit.

20. The cost of using someone else’s money.

**Key Terms**

a. annual percentage rate (APR)
b. bankruptcy
c. collateral
d. cosigner
e. credit
f. credit application
g. credit bureau
h. credit counselor
i. credit rating
j. down payment
k. finance charge
l. installment loan
m. interest
n. promissory note
o. statement of account
Decision-Making Strategies

Samantha Mae has been out of school for three years and has held four different jobs with different employers. She has been on her present job for two months. Her monthly take-home pay is $1,362. She shares an apartment with two friends to keep expenses down, but she is always in debt. Each month, she is short of the money she needs to pay all of her charge accounts. Her checking account is frequently overdrawn. Samantha has decided it would be better to live by herself. She blames her roommates for her credit spending sprees. She has come to you for a loan of $2,000. Her new apartment will cost $400 a month, and she wants to pay off some of her bills that are past due. She assures you that she will pay you at least $50 each month.

21. What are some criteria you would use to determine whether a personal loan for Samantha would be a good idea? What additional information might you want?

22. Would you loan the money to Samantha? Why or why not?

Make Academic Connections

23. HISTORY Research the use of credit throughout history. When was credit first used in various civilizations? How has credit been used to influence the development of retailing and other business activities in the United States?

24. CULTURE People in different countries have different attitudes toward credit. Based on library research, a Web search, and talking with people who know about other countries, prepare a summary of how credit is used around the world.

25. RESEARCH Collect credit applications, advertisements, and online offers. Compare the different APRs reported in the various credit information sources.

26. COMMUNICATION Prepare a one-minute oral summary of the activities of a credit bureau. Explain how credit bureaus serve both consumers and businesses.

27. MATH Find the date of maturity for each of these loans:

<table>
<thead>
<tr>
<th>Date of Loan</th>
<th>Time of Loan</th>
</tr>
</thead>
<tbody>
<tr>
<td>March 15</td>
<td>4 months</td>
</tr>
<tr>
<td>May 26</td>
<td>3 months</td>
</tr>
<tr>
<td>July 31</td>
<td>5 months</td>
</tr>
<tr>
<td>April 30</td>
<td>30 days</td>
</tr>
<tr>
<td>October 5</td>
<td>45 days</td>
</tr>
</tbody>
</table>

28. RESEARCH Some credit contracts include the “Rule of 78.” This condition results in a “prepayment penalty” if a loan is paid off early. Conduct library or web research to obtain a basic understanding of the Rule of 78.

29. TECHNOLOGY Conduct a web search to locate a sample of a credit contract. What features of the contract provide consumers with clear information about the cost of credit and other terms of the loan agreement?

30. LAW Several federal agencies, including the Federal Trade Commission and the Federal Reserve Board, administer consumer credit protection laws. Conduct research on the laws discussed in the chapter. Prepare a table with a summary of which agency to contact when your rights are violated.

31. MATH Before borrowing $200, Laura Demetry visited a small loan company and the loan department of a bank. At the loan company, she found that she could borrow the $200 if she signed a note agreeing to repay the balance in six equal monthly installments of $36.50. At the bank, she could borrow the money by signing a promissory note for $215 and repaying the balance in six equal monthly payments.

a. What would be the cost of the loan at the small loan company?

b. What would be the cost of the loan at the bank?
> > Linking School and Home

Obtain information on the responsibilities involved with cosigning a loan. Talk to family members and others. What do they know about being a cosigner?

What precautions should be taken when cosigning?
Talk with a credit counselor to obtain information about problems associated with cosigning a loan.

> > Portfolio Activity

To provide tangible evidence of your learning about consumer credit, do the following:

**COLLECT** an article, photos, and other visuals that represent the three Cs of credit (character, capacity, and capital). Also, prepare a list of actions to take when using credit wisely.

**CREATE** a visual presentation (on a poster or with presentation software) to give an overview of the three Cs of credit. Explain how taking various actions would reduce the possibility of encountering credit problems.

**CONNECT** your visual to other items already in your class portfolio, or relate the flowchart to an important concept you learned in another class. Explain how consumer credit is related to other topics from this course. Describe how using credit wisely links to a topic you have studied in another class.

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**Impromptu Speaking Event**

Leaders have the special skill to express their thoughts without prior preparation. Poise, self-confidence, and organization of facts are three valuable skills that are beneficial for articulate leaders.

Participants will draw a current event and will be given 10 minutes to organize their speech. One 4” by 6” index card will be given to the participant and may be used during the preparation and performance of the impromptu speech. Information may be written on both sides of the note card. Your speech should be four minutes in length, and no reference materials may be brought to or used during the preparation or presentation. No microphone will be used for your speech. Participants will receive a five-point deduction for any time under 3:31 or over 4:29 minutes. Some impromptu topics:

- Importance of Credit
- Minding Your Cs of Credit
- Credit Protection and Rights
- Avoiding the Disasters of Credit

**Performance Indicators Evaluated**

- Understand the three Cs of credit.
- Differentiate the pros and cons of credit.
- Define the role of credit in the market economy.
- Explain credit concepts in a clear, concise manner.

For *more detailed information about performance indicators, go to the FBLA web site.*

**Think Critically**

1. List two advantages and two disadvantages of credit.
2. What are the three Cs of credit? How can individuals protect their credit?
3. Do you believe that consumers are addicted to credit in a negative way? Explain your answer.

http://www.fbla-pbl.org/
Chapter 19

Savings and Investment Strategies

19-1 Saving and Investment Planning
19-2 Stock Investments
19-3 Bonds and Mutual Funds
19-4 Real Estate Investments
19-5 Other Investments
Planning a Career in...
Investments

People save and invest money in many ways. A need exists for workers to guide investors in choosing just the right plan for their individual financial situation. Work in the investment field may be with individuals or with institutional investors, such as banks and pension funds.

New and different investment products continue to be created. These investment alternatives result in employment opportunities for those interested in helping others plan their financial futures.

Employment Outlook

- As more people seek investment opportunities, the demand for securities sales workers will increase.
- Clerical and research workers with computer skills and finance knowledge will have average growth.
- Nationally, demand for real estate sales workers will grow more slowly than average, with some regions of the country having greater job opportunities than others.

Job Titles

- Brokerage Account Executive
- Brokerage Clerk
- Economist
- Financial Analyst
- Securities Analyst
- Financial Services Sales Agent
- Real Estate Appraiser
- Real Estate Agent, Broker
- Securities Research Analyst
- Securities and Commodities Sales Agent
- Stockbroker

Needed Skills

- Understanding economic conditions and global business trends is fundamental.
- Knowledge of investment terms and the legal aspects of investing is necessary.
- Workers who serve as stockbrokers must be licensed to sell securities and need to possess strong sales skills and communication ability.
- Real estate agents and brokers must pass a state test for their licenses and need to be knowledgeable about the housing market in their community.

What’s it like to work as ... 
an Investment Broker

“Do you think I should sell my health care stocks? Or will they continue to be a good investment for my future? How will changing interest rates affect my investment holdings? What will be the charges to sell my stocks?”

These questions are commonly asked of Roberto Jimenez, an investment broker. He has found that an understanding of economic conditions and business trends is the foundation of success in this field.

Each day, financial markets around the world process millions of actions to buy and sell investments. Stocks, bonds, mutual funds, real estate, currencies, commodities, gold, and silver are bought and sold by investors. The people who research, sell, and record these transactions are employed by a variety of investment companies and related businesses.

What about you? How could economic conditions affect the demand for investment jobs? What training and knowledge would be important for success in investment careers?
SAVING AND INVESTMENT BASICS

Creating a personal saving and investing strategy is vital for every financial plan. Putting money aside in a systematic way is the basis for achieving financial goals.

When savings are invested and used, the economy benefits. Individuals, businesses, and governments borrow money from financial institutions. People commonly borrow the savings of others to pay for homes, motor vehicles, and college. When this money is spent, demand for goods and services increases. This results in more jobs and creates more spending by workers.

Businesses borrow funds to operate or expand their operations. Building a new factory, replacing old equipment, or selling a new product are common reasons for business borrowing. These actions create jobs and expand economic activity.

Governments may borrow for highways, schools, or other public services. An economy would be significantly weakened without savings and investments.

Focus on Real Life

“I’d sure like to buy that MP3 player,” said Mel. “It has all the features I want. But it costs over $200! I can’t afford it.”

“Try saving your money,” Hank said in an encouraging voice. “Maybe if you cut back on some of your other spending, you could save enough money to buy it.”

“That would take forever,” sighed Mel.

“It’s easier than you think,” responded Hank. “If you put aside just 60 cents a day, within a year you’d have over $200. If you save even more each day, you could buy the player fairly soon.”

“You’re kidding!” exclaimed Mel.

“Really,” said Hank. “Most people don’t realize that saving small amounts of money on a regular basis can result in large amounts in the future, and that doesn’t even include the interest you can earn.”
After building up some savings, most people want to earn more. **Investing** means using your savings to earn more money. While a savings plan is a simple type of investing, many other investment choices are available.

**Determine Investment Goals**

Every saver and investor has one of two major financial goals: income and growth. People who want income for current living expenses desire **current income**. People select various types of savings plans and investments to provide current income.

In contrast, **long-term growth** is the other main investment goal. This is for people who desire financial security in the future. Investors who desire long-term growth choose investments that they hope will increase in value over time.

**The Growth of Savings**

In addition to putting money aside as savings, you should have those savings working for you. **Interest** is money you receive for letting others use your money.

If you save $50 a month, in a year, the savings will amount to $600. Suppose you deposit this money in a savings program that earns 6% simple interest, paid quarterly. You will earn $9 every three months. You will earn $36 each year. The interest is not added to your account, but rather is paid directly to you. At the end of 10 years, you will still have $600 in the account but will have earned $360 in interest.

**Compound Interest**

Earning interest on previously earned interest results in faster growth of savings. **Compound interest** is computed on the amount saved plus the interest previously earned. For example, simple annual interest of 10% on $1,000 is $100.

If the interest is compounded, then the interest computed at the end of the next year is based on $1,100 ($1,000 + $100 first-year interest). The 10% interest earned in the second year is $110. Interest the third year is based on $1,210 ($1,100 + $110 second-year interest) and is $121. The more frequent the compounding, the greater the growth in your savings. Figure 19-1 shows how quickly monthly savings of different amounts increase when interest is compounded quarterly at 6%.

**Checkpoint**

How does saving influence economic activity?

<table>
<thead>
<tr>
<th>Monthly Savings</th>
<th>End of First Year</th>
<th>End of Second Year</th>
<th>End of Third Year</th>
<th>End of Fourth Year</th>
<th>End of Fifth Year</th>
<th>End of Tenth Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>$5.00</td>
<td>$61.98</td>
<td>$127.76</td>
<td>$197.76</td>
<td>$271.68</td>
<td>$350.32</td>
<td>$822.16</td>
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<td>$10.00</td>
<td>123.95</td>
<td>255.52</td>
<td>395.15</td>
<td>543.35</td>
<td>700.47</td>
<td>1,644.32</td>
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<tr>
<td>$25.00</td>
<td>309.89</td>
<td>638.79</td>
<td>987.87</td>
<td>1,358.38</td>
<td>1,751.62</td>
<td>4,110.79</td>
</tr>
<tr>
<td>$30.00</td>
<td>371.86</td>
<td>766.55</td>
<td>1,185.45</td>
<td>1,630.05</td>
<td>2,101.94</td>
<td>4,932.95</td>
</tr>
<tr>
<td>$35.00</td>
<td>433.84</td>
<td>894.30</td>
<td>1,383.02</td>
<td>1,901.73</td>
<td>2,452.26</td>
<td>5,755.11</td>
</tr>
<tr>
<td>$50.00</td>
<td>619.77</td>
<td>1,277.58</td>
<td>1,975.74</td>
<td>2,716.75</td>
<td>3,503.24</td>
<td>8,221.59</td>
</tr>
</tbody>
</table>
SAVING AND INVESTMENT CHOICES

Many choices are available for your saving and investing dollars. These start with very safe savings accounts and range to rather risky investments.

Savings Plans
Banks, credit unions, and other financial institutions offer a choice of savings plans. Regular savings accounts, certificates of deposit, and money market accounts all provide a safe location for storage of your money.

**Savings Account** A savings plan with a low or zero minimum balance is a regular savings account. Usually, you may deposit and withdraw money as needed. These accounts pay interest while keeping money safe.

**Certificate of Deposit** A certificate of deposit allows you to earn a higher interest rate than a regular savings account. It requires a minimum deposit of $100 to $1,000 or more. You must leave the money on deposit for a specified period, from a few days to several years. Penalties, such as loss of interest, may be assessed if the money is withdrawn early.

**Money Market Account** A money market account pays a variable interest rate based on various government and corporate securities. Interest paid on money market accounts reflects the current rates of interest being paid in the money markets.

In general, money market accounts do not require long-term deposits. They may have a large minimum balance requirement. The earnings on money market accounts are higher than regular savings but slightly less than long-term certificates of deposit.

Securities
Investments in securities include stocks, bonds, and mutual funds. Corporations and governments sell these securities to raise money.

**Stock Investments** When you buy a share of stock, you become part owner of a company. A stock purchase, made directly or indirectly through mutual funds, is a very common way of investing. If a stock increases in value and is then sold for more than its original cost, a capital gain results. When an investment is sold for less than its original cost, a capital loss is the result.

**Bond Investments** Lending money for use by businesses and
governments is another common investment. **Bonds** represent debt. When you purchase a bond, you are lending funds to a company or government agency to use for their business activities.

**Mutual Funds** Instead of buying individual stocks and bonds, people can buy shares in a mutual fund managed by an investment company. Money from many investors is used to invest in a variety of companies. Mutual funds allow investors to spread out their risk among many investments.

**Alternative Investments**
Other investment choices include real estate, commodities, and collectibles. These choices often carry greater risk than savings or securities choices. As with all investments, you should carefully review your information and options before investing in these areas.

**Real Estate** People invest in real estate for numerous reasons. Many people purchase their own home for the sense of security and stability. Some purchase property for rental income. Others buy vacant property in hopes that its value will increase. Housing, farmland, apartment buildings, and shopping malls are some examples of real estate investments.

**Commodities** Grain, livestock, precious metals, currency, and financial instruments are all commodities. Investors purchase commodity contracts in anticipation of higher market prices for the commodity in the near future. Commodity investing is considered very risky.

**Collectibles** Ancient coins, works of art, and other rare items are often bought with the hopes that their value will increase.

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**EVALUATING SAVINGS AND INVESTMENTS**
As you decide which investments are best for you, four main factors should be considered: safety, return, liquidity, and taxes.

**Safety and Risk**
Today, savings accounts at most financial institutions are insured up to $100,000 by the federal government. This insurance is a promise that your money will be available when you need it. **Safety** is assurance that the money you have invested will be returned to you.

Suppose you lend $100 to someone who promises to pay it back with 10% interest at the end of one year. If the loan is paid back, you will receive $110 ($100 + $10 interest). If the borrower has no money at the end of the year, you may get nothing back. You may lose both the $100 you loaned and the $10 interest you should have earned.

Not all investors require the same degree of safety. Someone may have enough money to make 20 different investments. If one of them is lost, the investor still has the other 19. Another person may only have a small amount of money and can make only one investment. One loss would be serious. Most people want to make investments that are as safe as possible.

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**FYI**
To determine how many years it will take your savings to double, use the “Rule of 72.” To use this rule, divide 72 by the interest rate on your investment. If your investment is earning a 10 percent interest rate, 72 divided by 10 = 7.2. At a 10 percent interest rate, your money will double every 7.2 years.

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**CHECKPOINT**
What are the nine main categories of saving and investment alternatives?
Potential Return
A good savings plan or investment should earn a reasonable return. The yield is the percentage of money earned on your savings or investment over a year. Other common names for yield are the rate of return or the annual yield. Figure 19-2 shows the value of an investment of $100 after 20 years at several different yields.

Usually, higher yields and greater risk of loss go together. Investments you make with the federal government are the safest. When you invest money with individuals or businesses, it usually earns higher interest than that paid by the government because there is less safety. For example, the government may pay 3 percent interest on an investment. At the same time, one business may pay 5 percent and a business with even greater risk may have to pay 10 percent.

Investors will not accept higher risks unless the yields are greater. However, a low rate of return on an investment does not guarantee safety. Similarly, high rates of interest do not mean that a loss will surely occur. Higher yields mean that investors believe the situation involves a higher risk. Figure 19-3 shows the risk level for various investments.

The Truth in Savings (TIS) law requires that financial institutions give consumers information to compare savings accounts. The TIS law defines the annual percentage yield (APY) as the percentage rate equal to the total amount of interest that a $100 deposit would earn.
based on a 365-day period. APY helps eliminate confusion caused by different interest calculation methods. Some financial institutions used 360- or 366-day years to calculate interest.

**Liquidity**

Sometimes cash is needed quickly to pay unexpected bills. Investments that can be turned into money quickly are called liquid. **Liquidity** is the ease with which an investment can be changed into cash without losing its value.

Suppose you have $5,000 on deposit in a bank. If you need money right away, you usually can go to your bank and withdraw it. On the other hand, suppose you own a piece of land that you bought for $5,000. The land may be a safe investment. However, if you need money immediately, you may find it difficult to sell the land right away. You might even have to sell it for less than $5,000 if you cannot wait for a buyer who is willing to pay your price.

If you have several investments, not all of them need high liquidity. The amount of liquid investments you need will depend upon your expected financial needs.

**Taxes**

Earnings from certain types of savings and investments are taxed. Taxes reduce your rate of return. For example, if you earn $100 in interest but 20% is taken in taxes, you have only earned $80, $100 − ($100 × 0.20). Some investments have tax-exempt earnings, meaning you don’t have to pay taxes on that income. These investments are attractive because the tax-free yield may actually be higher than a comparable taxable investment.

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**Assessment**

1. **Key Concepts**
   Determine the best answer.
   
   1. Which of the following is investing for current income?
      a. retired person who needs to pay living expenses
      b. business manager planning for retirement
      c. student putting away money for college
      d. family that wants to buy a vacation home

   2. The most liquid investment listed here is
      a. rare coins
      b. real estate
      c. a savings account
      d. a house

   3. A person who desires high income from an investment would be most concerned with
      a. safety
      b. return
      c. liquidity
      d. risk

2. **Make Academic Connections**

   4. **Math** To determine the annual yield (rate of return) on an investment, divide the income from the investment for the year by the original amount invested. Look at the example. Then, calculate the annual yield for the other investments.

<table>
<thead>
<tr>
<th>Investment</th>
<th>Annual Income</th>
<th>Amount Invested</th>
<th>Annual Yield</th>
</tr>
</thead>
<tbody>
<tr>
<td>Example</td>
<td>$80</td>
<td>$800</td>
<td>10%</td>
</tr>
<tr>
<td>Savings account</td>
<td>$4</td>
<td>$200</td>
<td></td>
</tr>
<tr>
<td>Bond</td>
<td>$85</td>
<td>$1,000</td>
<td></td>
</tr>
<tr>
<td>Real estate</td>
<td>$6,400</td>
<td>$40,000</td>
<td></td>
</tr>
</tbody>
</table>

   5. **Economics** Prepare a list of benefits of saving and investing for (a) consumers, (b) business, and (c) government.
Types of Stock

When you buy shares in a corporation, you become a stockholder. A printed form known as a stock certificate shows ownership. If a business is profitable, it may pay out part of the profits in cash to the stockholders. These payments are dividends. The opportunity to earn a high rate of return attracts people to invest in stocks. Keep in mind that the risk of losing money on a stock investment also exists.

Before it can pay any dividends to stockholders, a corporation must pay bondholders the rate of interest promised to them. Sometimes there is not enough money left to pay dividends. If the corporation decides to put the money it earns toward business expansion, stockholders receive no dividends. If a corporation goes out of business, a stockholder may get little or nothing back from the investment.

Preferred Stock

The two main classes of stock issued by corporations are preferred stock and common stock. Preferred stock has priority over common stock in the payment of dividends. The dividends paid to preferred stockholders are usually limited to a set rate. Investing in preferred stock is less risky than common stock, but preferred stockholders generally have no voting rights within the corporation.

Common Stock

The second main class of stock is common stock. Common stock represents general ownership in a corporation and a right to share in its profits. Common stock has no stated dividend rate. As part owners of the corporation, common stockholders are invited to the annual meeting of the corporation. They are entitled to one vote per share of common stock owned.
Common stockholders receive dividends only after preferred stockholders are paid their dividends. Yet, if the profits of a company are large, the common stockholders may receive more dividends than preferred stockholders. For example, suppose that a company has issued $100,000 worth of common stock and $100,000 worth of preferred stock with a dividend rate of 6 percent. The company earns a profit of $20,000 and pays all the profit out as dividends. Preferred stockholders would be paid $6,000 in dividends, $100,000 \times 0.06$. The remainder, or $14,000, $20,000 - $6,000$, would be available to pay dividends to the common stockholders. The common stockholders would earn a return of 14 percent.

**STOCK TRANSACTIONS**

Each day, people buy and sell hundreds of millions of shares of stock. Buying a stock that is right for you is an important decision.

**Using a Stockbroker**

A licensed specialist in the buying and selling of stocks and bonds is a stockbroker. Through brokers, stockholders state the price at which they are willing to sell their shares. Interested buyers tell brokers what they would be willing to pay for those shares. The brokers then work out a price that is acceptable to both buyers and sellers. For their services, brokers charge a fee called a commission.

Two types of brokers are common. A full-service broker provides information about securities you may want to buy. Full-service brokers work for brokerage houses with large research staffs.

In contrast, a discount broker just places orders and offers limited research and other services. They charge lower commissions than full-service brokers. Investors who do their own research can save money by using a discount broker.

**Online Investing**

Numerous brokers operate online services. These services allow investors to access account information as well as buy and sell securities. By investing online, you are essentially your own financial planner.

These transactions are usually less expensive and more convenient than using a financial planner or broker. There are also disadvantages to investing online. Inexperience in making investment trading decisions can result in a large financial loss. Many online investors buy or sell stocks too quickly because making trades is only a click away.

**Stock Exchanges**

Brokers work through a stock exchange, which is a business organization that accommodates the buying and selling of securities. The best-known stock exchange is the New York Stock Exchange in New York City. The American Stock Exchange is also in New York City. Regional stock exchanges...
exchanges operate in Boston, Chicago, Philadelphia, and San Francisco. More than 170 stock exchanges are in operation around the world.

Usually, stocks of smaller companies are not traded on a stock exchange. The over-the-counter (OTC) market is a network where securities transactions occur using telephones and computers rather than on an exchange. The OTC market in the U.S. is the NASDAQ, which stands for the National Association of Security Dealers Automated Quotations. Today, the NASDAQ includes many large companies.

**Changing Stock Values**

The *market value* of a stock is the price at which a share of stock can be bought and sold in the stock market. The market value indicates the current value of a share of stock.

The prices at which stocks are being bought and sold are available through stock market listings in newspapers and from online sources. Figure 19-4 shows a stock market listing.

The market value can change rapidly. If the business is doing well, the market value is likely to go up. If the business has a poor record, the market value usually goes down. The market value also may be affected by current economic conditions as well as national and global politics.

Another measurement of investment values is a *stock index*. These indicators of stock values are commonly reported on television, radio, and in newspapers. The Dow Jones Industrial Average (DJIA) includes 30 of the largest U.S. companies. Another commonly reported stock index is the Standard & Poor's (S&P) 500, which is based on stock values of 500 major companies.

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**Figure 19-4**

How is a stock's yield different from a bond's yield?

<table>
<thead>
<tr>
<th>Stock Market Quotations</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1</strong></td>
</tr>
<tr>
<td>52-Week Hi</td>
</tr>
<tr>
<td>74.93</td>
</tr>
<tr>
<td>1 – Highest price paid for stock during past 52 weeks</td>
</tr>
<tr>
<td>2 – Lowest price paid for stock during the past 52 weeks</td>
</tr>
<tr>
<td>3 – Abbreviated company name</td>
</tr>
<tr>
<td>4 – Symbol used to report company</td>
</tr>
<tr>
<td>5 – Current dividend per share (in dollars)</td>
</tr>
<tr>
<td>6 – Dividend yield based on current selling price</td>
</tr>
<tr>
<td>7 – Price-earning ratio</td>
</tr>
<tr>
<td>8 – Number of shares traded, expressed in hundreds, on the trading day</td>
</tr>
<tr>
<td>9 – Highest price for a share on the trading day</td>
</tr>
<tr>
<td>10 – Lowest price for a share on the trading day</td>
</tr>
<tr>
<td>11 – Closing price for the day</td>
</tr>
<tr>
<td>12 – Change in closing price compared to previous trading day</td>
</tr>
</tbody>
</table>
STOCK SELECTION

Buying stocks follows a process similar to the one shown in Figure 19-5. By viewing various economic and social trends in the U.S. and around the world, you will determine what types of companies would benefit from those trends. For example, as people live longer, they require increased health care. Companies involved in health care products may be a wise investment.

Stock Information Sources

When choosing stocks, you should learn about the company. Several sources are available to assist you. These include Moody’s Handbook of Common Stocks, Value Line, and Standard and Poor’s Encyclopedia of Stocks. Publications like these provide data about net worth, debt, sales revenue, profits, dividend history, and the future prospects of companies. Many web sites are also available to provide valuable information on companies.

Work as a Group

Discuss various business and economic trends. Prepare a list of stocks that your group believes would be good investments. Explain what factors influenced the selection of these companies.

The U.S. Securities and Exchange Commission oversees the financial markets. It requires all companies that issue publicly traded securities to electronically file detailed reports. You can access those reports online.

Economic Factors

Many economic conditions affect stock prices. Awareness of these factors will help you make better choices about stock investments. You should consider the following economic factors.

- **Inflation** Higher prices can result in lower spending by consumers, reducing company profits.

Can you name a company or industry that has profited from a trend in recent months?

Figure 19-5

Four-Step Process for Deciding Stock Purchases

1. Observe and analyze economic and social trends.
2. Determine industries that will be affected.
3. Identify companies in those industries.
4. Decide whether to buy, sell, or hold the stock of those companies.
• **Interest rates**  As the cost of money changes, company profits can increase or decline.

• **Consumer spending**  Profits of companies that sell products and services to households are directly affected by buying habits.

• **Employment**  As people obtain or lose jobs, the amount of money they have for spending will affect company profits.

**Company Factors**

If you are considering investing in a company, ask the following questions.

• Has the company been profitable over a period of years?

• Have the company’s managers made good business decisions?

• Does the company have growth potential in coming years?

• Does the company have an unusually large amount of debt?

• How does the company compare with others in its industry?

Other information about a company should also be considered. The **yield** of a stock is important if your goal is to earn a good return from your investment.

Suppose a company is paying a quarterly dividend of $0.60 a share. The total dividend for the year would be $2.40. If the stock were selling for $40 a share, the current yield (return) would be calculated as

\[
\text{Dividend per share} = \text{Dividend Yield} = \frac{\text{Dividend per share}}{\text{Market price per share}}
\]

\[
\text{Dividend per share} = \frac{2.40}{40} = 0.06 \text{ or } 6\%
\]

The price of a stock should also be considered. Many investors look at the stock’s **price-earnings (P/E) ratio**, which is the relationship between a stock’s selling price and its earnings per share. The P/E ratio gives you an indication of whether the stock is priced high or low in relation to its earnings per share.

**CHECKPOINT**

How do various economic factors affect stock prices?

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**19-2 Assessment**

**Key Concepts**

Determine the best answer.

1. Which of these statements best describes preferred stock?
   a. vote at the annual meeting of the company
   b. first priority for receiving dividends
   c. low priority for receiving dividends
   d. no stated dividend rate

2. Higher spending for recreation in the economy would most benefit the stock prices for companies in the ___?___ industry.
   a. electronics
   b. health care
   c. office equipment
   d. automobile

**Make Academic Connections**

3. **Math**  Based on Figure 19-4, answer the following:
   a. What number of shares was traded for Deere on this day?
   b. What is the highest price of a share of Kellogg’s during the past year?
   c. What was the closing price of Mattel on the previous trading day?

4. **Communication**  Conduct a survey of people about what they believe are the most important factors to consider when selecting a stock. Prepare a summary data table and written analysis of your findings.
GOVERNMENT BONDS
To raise money for current operations or future expansion, most governments and corporations sell bonds. A bond is a certificate representing a promise to pay a definite amount of money at a stated interest rate on a specified due date. The due date is also called the maturity date. Bonds are similar to promissory notes issued by individual borrowers. When you buy a bond, you are lending money to the organization selling the bond. You become a creditor of the organization. Governments issue bonds to raise money for funding public services. The federal, state, and local governments issue a variety of bonds.

Municipal Bonds
A city may want to build a new park or new school. A state may need funds to build or repair highways and bridges. Bonds issued by local and state governments are called municipal bonds, or munis.

Municipal bonds have an advantage over bonds issued by companies. Usually, interest earned on municipal bonds are exempt from federal income tax. Municipal bonds have an advantage over bonds issued by companies. Usually, interest earned on municipal bonds are exempt from federal income tax.

Focus on Real Life
Barbara Malcolm has decided to invest in bonds. She believes that bonds provide greater security for her investment funds. However, after looking into buying bonds, the process seemed very complicated.

“I’m not sure what to do,” Barbara commented to her friend. “I’d like to invest in bonds, but you have to be an expert to pick the right ones.”

“Instead, how about investing in a mutual fund?” responded Barbara’s friend Mandy.

“What’s a mutual fund?” asked Barbara.

Mandy explained, “A mutual fund takes money from many people and buys several investments. This action allows an expert to manage your investment funds.”

“That sounds like something I should consider,” said Barbara. “Tell me more.”
bonds is exempt from federal and most state income taxes. In order to avoid taxes, people buy municipal bonds even though the interest rates usually are not as high as the rates offered on corporate bonds. In general, municipal bonds are considered safer investments than corporate bonds.

**U.S. Savings Bonds**

For people with small amounts of money to invest, U.S. government savings bonds are one of the safest investments. Series EE savings bonds come in denominations ranging from $50 to $10,000. They pay interest through a process called *discounting*.

A Series EE bond is bought at half its face value. A $50 bond costs $25. At the end of its full term, it pays at least $50. The difference between the purchase price and the redemption value is the interest earned. The length of time the bond is held determines the interest earned. The time it takes for a savings bond to mature will vary depending on the current interest rate being paid.

The U.S. government also sells Series HH savings bonds. These bonds are available to investors in face values from $500 to $10,000. They are not discounted and pay a fixed rate of interest through a check mailed to the investor.

Interest payments for Series HH bonds are different from EE bonds. With EE bonds, interest is only paid when the bond is cashed. With HH bonds, bondholders receive interest payments twice a year. Many investors favor this semiannual income.

One other type of savings bond is the *I bond*. These investments pay an interest rate that is lower than the rate of other savings bonds, but it is a variable rate that increases with inflation.

**Other Federal Securities**

The federal government also borrows using Treasury bills and notes. The difference between these debt securities is the length of time to maturity. Treasury bills, or *T-bills*, involve short-term borrowing with maturities from 91 days to one year. Treasury notes, or *T-notes*, have maturities from 1 to 10 years.

Before 2001, the U.S. government also used treasury bonds, called *T-bonds*. These involved long-term borrowing, with maturities ranging from 10 to 30 years.

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**CHECKPOINT**

List the types of bonds issued by the federal government of the United States.
CORPORATE BONDS
Investing in bonds for a company is quite different from investing in stock. When you invest in stock, you become an owner. When you buy a bond, you are lending money to the company. Bonds issued by corporations are corporate bonds.

Bond Components
Each bond has a face value, also called the maturity value. This is the amount being borrowed by the corporation issuing the bond. Most corporate bonds are issued for $1,000.

Interest is paid to the investor periodically (usually twice a year) based on the face value and the stated interest rate. On the bond’s maturity date, the face value is repaid to the investor.

Bond Values
Bonds are bought and sold in the bond market. The market value of a bond varies based on changing interest rates and the credit rating of the borrowing organization.

Bond values are reported similarly to the way stocks are reported. Corporate bond prices are stated in 100s, but the bonds are sold in $1,000 denominations (10 times the listed amount). For example, a bond reported at 100 is selling at its face value—$1,000. A bond selling at 105 has a market value of $1,050.

The price investors are willing to pay for a bond depends upon the stated interest rate. If the bond’s stated rate is lower than interest rates on similar bonds, investors will want to buy the bond for less than its face value. If the bond’s stated interest rate is higher than interest rates on similar bonds, the seller of the bond will want to receive more than its face value.

MUTUAL FUNDS
You may not have the time needed to study stocks and bonds so that you can make wise investment decisions. An investment type exists that allows you to join with others in investing and benefit from their research and knowledge. A mutual fund is an investment fund set up and managed by companies that receive money from many investors. Then, the company buys and sells a wide variety of stocks or bonds.

Types of Mutual Funds
Over 15,000 different mutual funds are available to investors. These funds have many different objectives. For instance, some emphasize investing in growth stocks, some emphasize stocks that pay high dividends, and some emphasize international stocks. Following are some of the main types of mutual funds.

CHECKPOINT
What affects the value of a bond?

Make a list of long-term investment options. Can you think of the pros and cons for each type?
Work as a Group

Review the list of types of mutual funds. Describe situations in which each type might be appropriate for a particular individual or family. Explain how this type of mutual fund could meet various investment goals.

- Aggressive-growth stock funds seek quick growth, but also have higher risk.
- Income funds specialize in stocks that pay regular dividends.
- International funds invest in stock of companies from around the world.
- Sector funds buy stocks of companies in the same industry such as health care, energy, or telecommunications.
- Bond funds specialize in corporate bonds.
- Balanced funds invest in both stock and bonds.

When selecting a mutual fund in which to invest, match your personal investment goals to the type of mutual fund.

Mutual Fund Values

Mutual fund investors own shares of the mutual fund. The value of each share is based on the total value of all investments made by the mutual fund company. For example, if the investments were worth $400,000 and 80,000 shares existed, each share would be worth $5, $400,000 ÷ 80,000 = $5. This amount is called the net asset value (NAV) of a mutual fund.

A part of the dividends and interest received from the fund’s investments is used to pay operating expenses of the fund. The major portion of earnings is distributed to the mutual fund shareholders or reinvested in the fund.

>> CHECKPOINT

What are the main types of mutual funds?

19-3

Assessment

>> Key Concepts

Determine the best answer.

1. Municipal bonds are issued by
   a. corporations
   b. the federal government
   c. international companies
   d. state and local governments

2. The price of a mutual fund share is most affected by
   a. current tax rates
   b. the value of investments
   c. current foreign rates
   d. the value of housing

3. True or False. A bondholder is part owner of a company.

4. True or False. Interest rates in an economy affect the value of a bond.

>> Make Academic Connections

5. Technology Go to the web site for U.S. savings bonds (www.savingsbonds.gov) to obtain information about how to buy savings bonds online. What features are available online to calculate the current value of savings bonds?

6. Research With thousands of mutual funds available to investors, how could a person evaluate them? Locate library and online information that could provide assistance when deciding in which mutual funds to invest.
SELECTING HOUSING

Real estate—land and anything that is attached to it—is one investment that many people eventually acquire. Getting started with real estate usually means finding a place in which to live.

Renting Your Residence

Most people start by renting an apartment. As renters, you are freed from much of the work and expense of property maintenance. Renting also makes it easier for you to move when needed. As a tenant, you must take care of the rented property, but you are not able to call the apartment your own.

Many people want to own a house and yard that they can maintain and fix up just the way they want. To realize this goal, they must save money for a down payment on a house.

Focus on Real Life

Driving home from their honeymoon, Joshua Moskowitz turned to his bride Carrie. “You know, we have some money that we received as wedding gifts,” said Joshua. “We should buy some stocks for our long-term financial future. I have heard of a lot of people who made fortunes with stocks.”

“What do you know about stocks? Are you sure we won’t lose our money?” asked Carrie.

“Well, it’s true, I don’t know much about stocks,” responded Joshua. “But I do know baseball cards! Let’s invest our money in baseball cards.”

“That’s kind of risky, isn’t it?” was Carrie’s next question.

“OK . . . OK. Then let’s buy gold bars. Gold can be a solid investment,” replied Joshua. “You can’t go wrong with gold.”

“Hold on. We both want what’s best for our future, but don’t you think that first we’d better find a place to live?” responded Carrie.
Owning a Mobile Home

Some people find houses too expensive. They might consider a mobile home in a good location that they can afford. A mobile home can be a first step toward becoming a real estate owner.

An advantage of owning a mobile home is having a place to call your own. As time passes, a family may need more space and look to purchase a house.

Buying a Home

Unless you have thousands of dollars available, you will need to borrow to buy a house. A **mortgage** is a legal document giving the lender a claim against the property if the principal, interest, or both are not paid as agreed.

Mortgages are usually long-term loans—for 15, 20, or 30 years—that require monthly payments. These payments are usually higher than rent. They often include property taxes and insurance in addition to a percentage of the principal and interest charges. Money used for a down payment reduces the amount of loan needed with the mortgage.

Interest rates on mortgages may be set for the term of the loan. This type of mortgage is called a **fixed-rate mortgage**. Market interest rates generally increase or decrease during the life of a mortgage depending on economic conditions. Therefore, lenders also offer an **adjustable-rate mortgage (ARM)**. The interest rate of an ARM is raised or lowered from time to time depending upon the current interest rate being charged by lenders. Monthly payments for ARMs often are lower, especially in the early years of the mortgage, compared with fixed-rate mortgages.

Services of Real Estate Agents

Buying a house is not a simple matter. Most homebuyers use a real estate agent. This person is trained and licensed to help with the buying and selling of real estate. Someone who wants to buy a house contacts a real estate agent. The agent helps the person decide what they want in a house. The agent will also arrange for the prospective buyer to view homes offered for sale.
Sellers of real estate may also use the services of a real estate agent. Someone who wants to sell a house contacts an agent. The real estate professional helps to set the selling price and promotes that the house is for sale.

**Other Real Estate Professionals**

Legal matters are also a part of the real estate purchase process. A lawyer, working with the real estate agent, will help you with the transaction. A lawyer assures that your property has no claims against it, such as back taxes. Having a lawyer represent you in the transaction can help to avoid future legal problems.

When buying a house, an appraiser’s report on the home’s value is also important. An appraiser is someone trained to estimate the value of property and who can give an official report on the value. Factors such as the quality of construction, the location, and the price of similar houses are considered when doing the appraisal.

**Buying a Condominium**

In some areas, condominiums, or condos, are popular. This is an individually owned housing unit in an apartment-like complex. The maintenance and yard work are normally taken care of with a service fee paid by condo owners.

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**CHECKPOINT**

What are four available housing alternatives?

---

**BENEFITS OF HOME OWNERSHIP**

The advantages of home ownership include tax benefits, increased equity, and pride of ownership.

**Tax Benefits**

Although you may pay both mortgage loan interest and property taxes on real estate you own, these costs can be used to your benefit. Reduced income taxes result when the interest paid on a mortgage is included as a deductible expense. Real estate property taxes are usually also deductible when computing your federal income taxes.

**Increased Equity**

From an investment standpoint, the potential increase in home value is an important aspect of ownership. Equity is the difference between the price at which you could currently sell your house and the amount owed on the mortgage. Equity builds up over the years. It increases rapidly in the last few years of a mortgage.

Because of appreciation, a general increase in the value of property that occurs over time, homes increase in value. Over the 10 years that one family had lived in their home, its market value had increased to $144,000 and their debt decreased to $65,000. Therefore, their equity was $79,000.
Many factors affect the value of a home. Most important is location. In addition, the quality of schools, maintenance of the property, and home features increase home values. Features that can add to the value of a home include an updated kitchen, remodeled bathrooms, a master bedroom suite, a finished basement, and a large garage.

**Pride of Ownership**

Property ownership is one of the basic rights in a democracy. A principal advantage of owning real estate is pride of ownership. Having a home to use and decorate as desired is a strong motivation for many homebuyers.

**COSTS OF HOME OWNERSHIP**

While there are important advantages to owning your own property, disadvantages also exist. Home ownership has costs such as property taxes, interest payments, property insurance, and maintenance.

**Property Taxes**

Property taxes vary greatly from state to state and community to community. Generally, real estate taxes range from 2 to 4 percent of the market value of the property. Taxes are based on the assessed value, which is the amount that your local government determines your property to be worth for tax purposes. Assessed values normally are lower than the market value, often being only about half.
A home with a market value of $180,000 may be assessed at $90,000. If the tax rate is $60 per $1,000 of assessed value, the annual taxes are $5,400.

\[(\$90,000 \div \$1,000) \times \$60 = \$5,400\]

The tax rate is 6% of the assessed value, but only 3% of the market value.

**Interest Payments**

Interest payments add to the cost of the house. A 30-year mortgage for $100,000 at 8 percent interest would result in more than $164,000 in interest payments over the life of the loan.

**Property Insurance**

Property insurance is an essential home ownership cost. The value of the house, the construction material, the location in respect to other buildings, and the availability of fire protection are some factors that affect the cost of homeowners insurance. Typical annual home insurance costs are less than 1 percent of the market value of the house. Property insurance provides protection from fire, theft, accident, or other losses of your home or property.

**Maintenance**

The cost of upkeep—maintaining your property in good condition—is important in home ownership. Annual upkeep costs average about 2 percent of the property’s value. Postponing repairs or not taking good care of the house and yard through regular maintenance can be very costly in the long run.

**CHECKPOINT**

What are common costs of home ownership?

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**19-4 Assessment**

**Key Concepts**

Determine the best answer.

1. The person who reports on the value of a home is a(n)
   a. lawyer
   b. real estate agent
   c. appraiser
   d. mortgage broker

2. A common financial benefit of home ownership is
   a. low property insurance costs
   b. tax deduction for your down payment
   c. increased property value
   d. low maintenance costs

**Make Academic Connections**

3. **Finance** Obtaining a mortgage to buy a house is easier when a person has a large down payment. Prepare a list of sources of funds for a down payment that a person might consider.

4. **Math** A home worth $123,000 and a mortgage of $72,400 would have equity of $_. A home with an assessed value of $178,000 with a tax rate of $52 per $1,000 would have a property tax bill of $_.

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Known as Siam until 1939, Thailand is the only nation in southeast Asia that was never colonized. The country’s name means “land of the free.” Thailand is also known as the “Land of Smiles.” A sense of humor, laughter, and a pleasant attitude are highly regarded.

While Thailand guarantees freedom of religion with many religions represented, 95 percent of the population is Buddhist. Traditionally, all young men are expected to become monks for at least three months to study Buddhist principles.

Monks in Thailand are highly respected. The first rows of the theatre are reserved for them and for high-ranking officials. People are also expected to give up their seats on a bus or train to a monk who is standing.

Greetings in Thailand with a wai (pronounced why), in which you place the palms of your hands together at chest level, fingers extended, and bow slightly; women curtsy. A wai communicates respect.

The head is considered very sacred in Thailand. Never touch another person’s head or pass an object over it. In contrast, the bottoms of the feet are least sacred. Avoid pointing your feet toward others. Stamping your feet is considered very improper. Removing your shoes is customary when entering a Buddhist temple or private home.

A business lunch may last two hours, from 1 to 3 P.M. The time is used to develop relationships with business associates. You may discuss sports such as soccer, table tennis, badminton, volleyball, and basketball, which are popular in Thailand.

Dinner may extend from 7 to 10 P.M. with an eight- or nine-course meal. Rice is served with nearly every meal. In addition, you will likely have spicy dishes consisting of meat, vegetables, fish, eggs, and fruits.

English is the second most common language after Thai. Remember that speaking loudly or showing anger in public is offensive. During negotiations, Thais will never say “no.” Avoiding confrontation is a high priority.

**Think Critically**
1. What actions might be necessary when doing business in Thailand?
2. How might a person negotiate with business associates in Thailand?
3. Conduct library or Internet research to find additional information about business and economic activities in Thailand.
Other Investments

**Focus on Real Life**

“Take a look at this one! It must be over 100 years old,” said Colin. “Now that’s a great investment.”

“But how do we know these coins are genuine and whether they will increase in value?” asked Paul.

“Well, we could check on the Internet or get another opinion,” responded Colin.

“But that’s a lot of money to invest in something with that much risk,” cautioned Paul. “I’m not sure that’s how I want to invest my college savings.”

“Come on,” urged Colin. “You have to take a risk to make big bucks.”

“But I could also lose ‘big bucks!’” noted Paul.

“OK, that’s enough ‘buts.’ I guess you need to consider other types of investments that match your risk level and investment goals,” Colin said.

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**COMMODITIES AND FUTURES**

Another type of investment considered by experienced investors is commodities. Commodities include grain, livestock, and precious metals. Generally, commodity investing is considered to be speculative. A speculative investment is one with an unusually high risk.

Commodity investors buy and sell futures contracts. An agreement to buy or sell an amount of a commodity at a specified price in the future is a futures contract. Futures contracts also involve the buying and selling of currencies and financial instruments.

**Commodity Exchanges**

Commodities are bought and sold on exchanges similar to stock exchanges. Buyers and sellers are represented by traders on the exchanges.

One of the best known exchanges is the Chicago Board of Trade (CBOT). Established in 1848 to provide a market for agricultural products, CBOT helps to avoid the huge price variances for these products.

Other commodity exchanges around the world include the Chicago Mercantile Exchange, the Kansas City Board of Trade, Brazilian Futures Exchange, and the Russian Commodity and Raw Materials Exchange.

**Agricultural Commodities**

Agricultural products, such as corn, soybeans, and wheat, are some of the items traded on commodity exchanges. Agricultural producers sell their crops in advance of a harvest at what they believe is a good price. Farmers will then know in advance how much they will receive for a crop.
The futures contract buyers hope the price of the crop will go up when harvested so that they can earn a profit. Conditions that affect agricultural commodity prices include weather, international trade agreements, and worldwide demand and supply.

**Gold, Silver, and Precious Metals**

Precious metals have worldwide importance. Investors have traded gold and silver on commodity markets for centuries. Gold has the longest history as a monetary commodity, going back to gold coins that were circulated as early as 500 B.C. Gold is highly prized for both ornamental and industrial reasons. More recently, other metals, such as copper and platinum, have also become valuable commodities.

Prices of these metals are affected by economic conditions as well as supply and demand. For example, in 1879, gold sold for $18.79 per ounce. Since 1979, the price of an ounce of gold has ranged from over $800 to less than $300.

Precious metals are quoted as *spot prices* per one troy ounce. This is the current price quoted for precious metals in the world markets. You can find the spot price for gold in London and New York in newspapers and online.

Money invested in precious metals does not earn interest. If you hold gold, silver, or platinum, you might profit by selling them later at a price higher than what you paid. Gold and other precious metals have another advantage—many view them as protection against currency becoming worthless. Gold could be used for buying goods and services when paper money might not be accepted.

**Currency and Financial Instruments**

Currencies, such as the U.S. dollar, euro, and Japanese yen, and financial instruments, such as Treasury bills and notes, are traded on the futures markets. The price of currency and financial instruments is affected by a country’s economic outlook and current interest rates. Again, investors buy currency or financial instruments expecting the prices to increase in the future so that they can sell them to others at a profit.

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**FYI**

People often confuse the euro and a Eurodollar. The euro is the official currency of the European Union. A Eurodollar is a U.S. dollar deposited in a bank outside the United States. It was originally called the Eurodollar since most of those deposits occurred in Europe. Today, the U.S. dollar is used in all regions of the world.

**CHECKPOINT**

What types of commodities are commonly used with futures contracts?
COLLECTIBLES

Another form of investment that is popular with many people is collectibles. Collectibles are items of personal interest to collectors that can increase in value in the future.

An advantage of collectibles is the personal pleasure of buying, collecting, storing, arranging, and displaying what is collected. Often, collectors even form organizations. For example, stamp clubs around the country bring together stamp collectors who buy, sell, trade, display, and discuss their stamps. Baseball card trading takes place at scheduled events in huge arenas as well as over kitchen tables. Antique dealers and collectors gather for major events at which they buy and sell their items.

Types of Collectibles

A wide variety of collectible items may serve as investments. Commonly obtained items are stamps, coins, sport trading cards, and antiques. In addition, unusual items purchased as an investment include autographs and letters of famous people, Chinese ceramics, movie posters, glassware, rare books, and toys.

Collectible Values

The possibility of the average buyer of collectibles making a large profit is not great. Only rare stamps, coins, art, and antiques—which may cost hundreds or thousands of dollars—tend to be items on which the investor can make a considerable profit. The wise investor in collectibles studies the market, knows the product well, and analyzes the potential risk.

CHECKPOINT

What are common types of collectibles?

1. The spot price for gold or silver refers to the
   a. interest for borrowing to buy the precious metal.
   b. current market price of the precious metal.
   c. future market price of the precious metal.
   d. global price for the precious metal set by the World Bank.

2. The value of collectibles is most influenced by
   a. the current tax rate on investments.
   b. government regulations of the market.
   c. the futures market for commodities.
   d. interested buyers and potential sellers.

3. Research Go to the web site of the Chicago Board of Trade, the Chicago Mercantile Exchange, or another commodity exchange. Prepare a summary of the commodities and financial instruments traded on this exchange.

4. Art Identify paintings and other works of art that would be considered valuable investments.
**Business Notes**

**19-1 Saving and Investment Planning**

1. Savings plans help buy needed goods and services as well as prepare for future expenses and emergencies. Savings help the economy by making funds available to individuals, businesses, and governments for borrowing. The main investment goals are current income and long-term growth.

2. The major categories of savings and investments are savings accounts, certificates of deposit, money market accounts, stocks, bonds, mutual funds, real estate, commodities, and collectibles.

3. When evaluating savings and investments, consider safety, yield, liquidity, and taxes.

**19-2 Stock Investments**

4. Stock is equity and represents ownership. Preferred stock has priority over common stock in the payment of dividends. Preferred stockholders receive dividends paid at a set rate. Common stock represents general ownership in a corporation and a right to share in its profits. Common stockholders vote to elect the officers of the corporation.

5. Stockbrokers work through stock exchanges to buy and sell shares of stock for investors.

6. When selecting stock investments, consider a company’s profitability, debt, growth potential, yield, and price-earnings ratio (P/E). Also consider economic factors such as inflation, interest rates, consumer spending, and employment.

**19-3 Bonds and Mutual Funds**

7. A bond represents a debt owed by an organization. Government and companies sell bonds to raise funds to finance current operations or future expansion. Local and state governments sell municipal bonds. The federal government sells savings bonds, Treasury bills, and Treasury notes.

8. Companies issue corporate bonds to raise funds. Investors are paid interest for lending money to the company.

9. Mutual funds allow people to combine their funds to buy a variety of securities, which reduces risk and increases potential returns. Types of mutual funds include aggressive-growth stock funds, income funds, international funds, sector funds, bond funds, and balanced funds.

**19-4 Real Estate Investments**

10. A person can get started in real estate by renting a place to live or buying a mobile home. When buying a home, you may need to obtain a mortgage and use the services of a real estate agent and lawyer.

11. The advantages of home ownership are tax benefits, increased equity, and pride of ownership.

12. The major costs associated with owning a house include property taxes, interest payments, property insurance, and maintenance.

**19-5 Other Investments**

13. Commodities commonly used as investments include corn, soybeans, wheat, gold, silver, copper, platinum, foreign currencies, and Treasury debt instruments.

14. Collectibles can combine a hobby with an investment that may increase in value.

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**Communicate Business Concepts**

1. What actions could employers and government take to encourage saving in society?

2. How does inflation increase the risk of an investment?

3. Ella Chapman, a wealthy businessperson, invests $5,000 in a newly organized company. Frank Brokaw earns an average moderate salary and has $5,000 in a savings account. Because Ella has a reputation for being a good...
investor, Frank decides to also invest in that company. Does the fact that the investment may be a good one for Ella mean that it is also a good investment for Frank? Explain your answer.

4. What are some reasons people buy stocks even though they are not as safe as other types of investments?

5. Why do municipal bonds usually pay a lower rate of interest than corporate bonds?

6. Susan Haugen bought $5,000 of gold mining stocks a few years ago. Last week, she received a letter saying that the company went out of business. It could not operate profitably, so it closed down. How much of her investment might Susan lose?

7. People who buy and sell land and houses commonly say that the three most important factors to consider when buying real estate are “location, location, and location!” Why do you think this is their belief?

8. Blair Vazquez owns a house that has a value of $80,000. For the past three years, the upkeep has averaged less than $500 a year. Can Blair assume that his expenses will be only $500 in future years?

>> Develop Your Business Language

Match the terms listed with the definitions.

9. The amount that your local government determines your property to be worth for tax purposes.
10. Licensed specialist in the buying and selling of stocks and bonds.
11. Land and anything that is attached to it.
12. Represents general ownership in a corporation and a right to share in its profits.
13. Investments set up and managed by companies that receive money from many investors.
14. A legal document giving the lender a claim against real estate property.
15. Items of personal interest to collectors that can increase in value in the future.
16. Using your savings to earn more money.
17. The percentage of money earned on your savings or investment over a year, also called the rate of return.
18. Bonds issued by local and state governments.
19. Storage of money for future use.
20. The difference between the price at which you could currently sell your house and the amount owed on the mortgage.
21. Business organizations that accommodate the buying and selling of securities.
22. Bonds issued by corporations.
23. Agreements to buy or sell an amount of a commodity at a specified price in the future.
24. The price at which a share of stock can be bought and sold in the stock market.
25. Grain, livestock, and precious metals.
26. Stock that has first priority in the payment of dividends.
27. The ease with which an investment can be changed into cash without losing its value.

Key Terms

a. assessed value
b. collectibles
c. commodities
d. common stock
e. corporate bond
f. equity
g. futures contract
h. investing
i. liquidity
j. market value
k. mortgage
l. municipal bond
m. mutual fund
n. preferred stock
o. real estate
p. saving
q. stock exchange
r. stockbroker
s. yield
Decision-Making Strategies

Jennie Wolfe has inherited $18,000. She graduated from high school three years ago, has an accounting job, is renting a small apartment, and saves regularly.

Jennie understands the need to evaluate stock and bond investments based on safety, liquidity, and rate of return. In addition, she realizes that the investments she selects must be guided by her personal financial needs and goals. Jennie also believes that she will not need any large amounts of cash for the next several years.

28. Jennie wants to invest in stocks that will be very safe, highly liquid, and earn a high return. Is there anything wrong with this investment goal?

29. What advice would you give Jennie to help her study the companies from which she is considering buying bonds and stocks?

Make Academic Connections

30. LAW The Truth in Savings law was created to provide consumers with clear, accurate information on the earnings of savings accounts. Conduct an online search to obtain additional information about this law.

31. MATH Small amounts add up to large sums in a short time. How much will each person below save in one year (365 days) if he or she saves the following amounts without interest being added?
   a. Charles Jason: 20 cents a day
   b. Carla Spivak: 95 cents a week
   c. Alice Farney: $10 every two weeks
   d. Nolan Robinson: $20 a month

32. TECHNOLOGY Buying investments online can be convenient and reduce commission costs. Locate a web site that allows you to buy and sell stock and other investments online. What services are provided by this e-broker? What costs are involved?

33. MATH The price-earnings (P/E) ratio is calculated by dividing the price per share by the earnings per share. If a company has 100,000 shares of stock and earns a net profit of $150,000, (a) what is the earnings per share? (b) If the company’s stock is selling for $30 per share, what is the P/E?

34. GEOGRAPHY Research the location of stock exchanges around the world. Identify one in Europe, one in Asia, one in Africa, and one in Latin America. Prepare a map showing the locations of these stock exchanges.

35. VISUAL ART Select a company and research its stock price for one day a week for the past eight weeks. Prepare a table showing the changing market value of the stock. Describe situations that may have affected the market value of this stock.

36. COMMUNICATIONS Talk to a person who is a member of an investment club. What is the purpose of an investment club? How do these groups help investors earn money while learning about stocks and bonds?

37. ECONOMICS Locate current bond prices in the newspaper or online. Select a bond for a company. Identify the following: (a) company name, (b) stated rate of the bond, (c) bond maturity date, (d) current yield, and (e) current market value of the bond. What economic and company trends are likely affecting the current market value of the bond?

38. RESEARCH Junk bonds are investments with high risk but also potential for a high return. Conduct library or online research to obtain information about these risky bonds.

39. BUSINESS Commodity trading is governed by the Commodity Futures Trading Commission (CFTC) and the National Futures Association (NFA). Conduct library and online research to obtain additional information on these agencies.
> > **Linking School and Home**

Talk to people you know about their investments. What types of investments do they own? (Do not ask the value of the investments.) How did they decide to obtain these investments? What types of investments do they recommend for people of various ages? Prepare a one-paragraph summary of your findings.

> > **Portfolio Activity**

To provide tangible evidence of your learning about investments, do the following:

**COLLECT** examples of various types of investments. These examples may be photos, advertisements, graphs, data, online information, or other items. Obtain items that represent at least five different types of investments.

**CREATE** a visual presentation (poster, display, computer presentation, web page, or other format) to show how these types of investments vary with regard to risk. Put them in order from least risky to most risky.

**CONNECT** your presentation to other items already in your class portfolio, or relate the visuals to a concept you learned in another class. Prepare a two-paragraph summary explaining how various factors affect the risk and value of investments.

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**Presentation Management—Team Event**

This event will assess your use of current desktop technologies and software to prepare and deliver an effective multimedia presentation.

You will design a computer-generated multimedia presentation. You have 15 minutes for preparation and setup. The presentation will last a minimum of seven minutes and a maximum of 10 minutes. Up to five minutes will be allowed for questions from the judges. The contestants must make effective use of current multimedia technology in the presentation. In preparation for the presentation, contestants should use space, color, and text as design factors. No VCR or laserdisc may be used in the presentation. Charts and other graphics should be used in the presentation. The student is responsible for securing a release form from any individual whose name, photograph, and other information is included in the presentation.

**Topic:** You are an investment advisor who helps individuals decide where to invest money based upon the amount available to finance, risk factor, and rate of return. Your presentation must cover stocks, bonds, real estate, futures, commodities, and collectibles. You must discuss the safety, liquidity, and possible rate of return for each investment.

**Performance Indicators Evaluated**

- Demonstrate knowledge of multimedia software and components.
- Demonstrate effective oral communication skills.
- Apply technical skills to create a multimedia presentation that enhances the oral presentation.

You will be evaluated for your:

- Knowledge of the topic
- Organized presentation of the topic
- Confidence, quality of voice, and eye contact
- Relationship of the topic to business strategy

*For more detailed information about performance indicators, go to the BPA web site.*

**Think Critically**

1. What does liquidity of an investment mean?
2. Which investments involve greater risk?
3. What is the advantage of investing in real estate?
4. Why are futures markets and collectibles classified as riskier investments?

http://www.bpa.org/
Chapter 20

Insurance

20-1 Vehicle Insurance
20-2 Property Insurance
20-3 Life Insurance
20-4 Health Insurance
Planning a Career in...

Insurance

Over 1.5 million people work in the insurance industry. In addition to sales agents and brokers, many other insurance career options are available. These include claims examiner, actuarial clerk, and insurance investigator. The primary activities of these employees are to determine and satisfy the insurance needs of consumers and business organizations.

Employment Outlook

• There will be slower than average employment growth for insurance agents.
• Employment for support workers in the insurance industry will require strong technology competencies.
• As insurance agents offer additional financial planning services and investment products, expanded opportunities will be available.

Job Titles

• Insurance Sales Agent
• Actuary
• Insurance Broker
• Insurance Underwriter
• Claims Examiner
• Claims Clerk
• Auto Damage Insurance Appraiser
• Insurance Policy Processing Clerk
• Customer Service Representative
• Insurance Fraud Investigator

Needed Skills

• Employment with an insurance company usually requires a college degree with an emphasis in business, finance, or economics.
• Software skills and general ability with technology are important as most insurance activities are computerized.
• Sales ability and strong communication skills are vital for those involved in selling and customer service.
• Specialized insurance training may be obtained through courses offered by the Insurance Institute of America and other insurance organizations.

What's it like to work in ...

Insurance

“Now that we have your life, car, and home insured, how about considering a portfolio of mutual funds for your retirement plan?” asked Valerie Esposito.

“Wait a minute, I thought you were an insurance agent, not an investment broker,” responded Jane Conley.

“Well, we now do a lot more than just sell insurance,” responded Valerie. “My company offers all types of insurance for businesses and individuals. In addition, we can help you with various financial services and investment products. We also make car loans and mortgages, and we issue credit cards.”

“That’s nice to know,” commented Jane. “I’ll be able to get assistance from you about my insurance needs, but I will also be able to borrow and invest through your company. How convenient!”

What about you? What aspects of the insurance business might interest you for a future career?
Owning a vehicle puts you in a position of high economic risk. You might have an accident and injure yourself or other people. You might damage your vehicle or others’ property. Vandals might steal or damage your vehicle. Someone could sue you because of an accident involving your vehicle.

Treating injured people and repairing damaged property resulting from an automobile accident can take all of the assets of a person who does not have insurance. The amount of money paid to injured people and to owners of damaged property has increased dramatically. Vehicle insurance provides protection from the financial risks involved with owning and driving a car.

Sometimes you cannot avoid an accident. No one can be directly blamed for it. However, in most cases someone is at fault. The person who is legally at fault is liable for damages and financial losses that result from the accident. Although you may think you are faultless, you can be sued. If you are insured, your insurance company will provide legal defense for the suit. If the court decides that you are legally liable for injuries or damage to property, your insurance company will pay up to the limits stated in your insurance policy.

Individual states regulate laws related to vehicle insurance. Most of these laws benefit responsible drivers. Owners of vehicles should know about financial responsibility laws and compulsory insurance laws.
Financial Responsibility
All states have some type of financial responsibility law. These laws protect the public from financial loss caused by drivers. If you cause an accident and cannot pay for damages or injuries through insurance, the legal system may take other action. Your savings or property may be taken. Your driver’s license will also likely be suspended or taken away. Financial responsibility laws make you legally responsible for any injuries you cause to people. You are also responsible for damage to the property of others.

Compulsory Insurance
Most states require drivers to carry certain types of automobile insurance before they can get a license for their car. In those states, it is compulsory that an automobile owner have insurance for personal injury and property damage. Compulsory insurance laws may not allow a driver to register a car or get a driver’s license without proof of the required insurance coverage.

> CHECKPOINT
What are financial responsibility laws?

> Explain auto insurance coverage.

AUTOMOBILE INSURANCE COVERAGE
Insurance companies offer several types of auto insurance protection. The two main categories are personal injury coverage and property damage coverage. Figure 20-1 summarizes the types of automobile insurance coverage.

Personal Injury Coverage
Personal injury coverage includes bodily injury liability, medical payments, and uninsured motorist protection. These three types of coverage are the main source of money paid in claims by automobile insurance companies.

Bodily Injury Liability Protection
Insurance that protects a driver from claims resulting from injuries or deaths for which the insured is at fault is bodily injury liability coverage. This type of insurance covers people in other cars, passengers riding with the insured, and pedestrians. The insured and, in most cases, the insured’s immediate family are not covered.

Which type of coverage do you think is generally the most expensive?

Summary Chart of Automobile Insurance Coverage

<table>
<thead>
<tr>
<th>Types of Coverage</th>
<th>Coverage On</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>Policyholder</td>
</tr>
<tr>
<td>Personal Injury Coverage</td>
<td></td>
</tr>
<tr>
<td>Bodily injury liability</td>
<td>No</td>
</tr>
<tr>
<td>Medical payments</td>
<td>No</td>
</tr>
<tr>
<td>Uninsured motorist protection</td>
<td>No</td>
</tr>
<tr>
<td>Property Damage Coverage</td>
<td></td>
</tr>
<tr>
<td>Property damage liability</td>
<td>No</td>
</tr>
<tr>
<td>Collision insurance</td>
<td>Yes</td>
</tr>
<tr>
<td>Comprehensive physical damage</td>
<td>Yes</td>
</tr>
</tbody>
</table>
Dollar amounts of bodily injury coverage are generally expressed as two numbers, such as 100/300. The first number refers to the limit in thousands of dollars that the insurance company will pay for injuries to any one person in an accident. For example, with 100/300 bodily injury liability coverage, the insurance company would pay up to $100,000 for injuries to one person.

The second number, 300, is the maximum amount that the company would pay for injuries to multiple people because of the accident. If more than three people were injured, each person may not receive the full $100,000. The insurance company is only liable for $300,000 in this case. You may obtain larger amounts of bodily injury protection for a slight increase in your premium.

Medical Payments Protection
Policyholders and family members are covered if they are injured while riding in their car or another car through medical payments coverage. This protection may also cover them if they are walking and are hit by a car. In addition, the policy protects guests in the insured car.

Medical payments insurance covers the costs of medical, dental, ambulance, hospital, nursing, and funeral services. Payment, up to the limit stated in the policy, is made no matter who is at fault. Car owners usually purchase medical payments insurance along with bodily injury liability coverage.

Uninsured Motorist Protection
In some cases, injuries are caused by hit-and-run drivers or by drivers without insurance or money to pay claims. To protect against these drivers, insurance companies offer uninsured motorist coverage.

This coverage is available only to those people who carry bodily injury liability insurance. Uninsured motorist protection covers the policyholder and family members. It also covers guests in the policyholder’s car. Uninsured motorist protection covers the insured person only if the uninsured motorist is at fault. This is different from medical payments coverage, which pays regardless of who is at fault.

Insurance companies also offer underinsured motorist coverage. This insures you for losses caused by another driver whose coverage is insufficient.

Property Damage Coverage
Three types of automobile insurance protect you from economic loss as a result of property damage. The three types of coverage are property damage liability, collision, and comprehensive damage.

Property Damage Liability
Insurance that protects a driver against claims if the insured’s car damages someone else’s property and the insured is at fault is property damage liability coverage. The damaged property is often another car, but it may also be property such as telephone poles, fire hydrants, or buildings. Property damage liability insurance does not cover damage to the insured’s car.

Collision Insurance
Insurance that protects a car owner against financial loss resulting from a collision or rollover is collision coverage. This insurance does not cover injuries to people or damage to the property of others.

Collision coverage is usually written with a deductible clause. You must pay this amount before the insurance
company pays a claim. For example, suppose your car suffers $2,500 damage in an accident and your deductible amount is $500. You would pay $500 and the insurance company would pay $2,000, $2,500 damages — $500 deductible = $2,000 claim. Deductible amounts are often $200, $500, or more. Deductibles reduce the premium cost.

Collision coverage does not provide for payment of damages greater than the car’s value. Suppose the insured’s car incurs $6,500 in damages in a collision with another vehicle. If the car has a value of only $6,100, the collision coverage would pay only $6,100, not $6,500.

Collision coverage may not be worthwhile on a car that is of little value. In some situations, the cost of repairing the car may be more than the car is worth.

**Comprehensive Coverage** Your car can be damaged or destroyed in other ways. Common perils include theft or damage resulting from fire, tornado, flood, vandalism, or falling objects. Comprehensive coverage protects the insured against almost all damage losses except those caused from a collision or rollover.

If the insured’s car is stolen or destroyed, the amount paid by insurance is not necessarily equal to the amount paid for the car. Rather, it is equal to the car’s estimated value at the time of the loss. Suppose the insured’s car cost $15,000. It is stolen soon after it is purchased. The insurance company will probably pay almost as much as the car cost—perhaps $14,500. If the car is stolen two years after it is purchased, the insurance company may pay only $10,500. The car has grown older and has a decreased value.

**No-Fault Insurance Laws**

In an effort to reduce insurance costs and speed up claim settlements, no-fault insurance has been adopted by some states. Under this program, people injured in an automobile accident collect for their financial losses from their own insurance companies no matter who is at fault. These losses include their medical bills, loss of wages, and other related expenses.

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**CHECKPOINT**

What are the two main categories of automobile insurance coverage?
Automobile insurance is expensive. You should spend this money wisely and carefully. It is important to understand how to get the most protection for your insurance dollar.

**Insurance Rates**

Insurance companies use several factors to determine automobile insurance costs. Some of those factors include:

- Your age and other characteristics such as accident record, marital status, academic standing, and credit rating
- Purpose for which you use your car
- Number of miles you drive each year
- Value and type of your car
- Community in which you live
- Amount of coverage and deductibles

Since some drivers are more likely to have accidents than others, they pay higher premiums. To determine premium rates, drivers are classified according to age, marital status, driving record, and scholastic achievement.

The lowest rates are reserved for the best risks—those least likely to have an accident. When a driver in the family is under age 30, the cost of insurance is usually higher than if all drivers are over age 30.

The purpose for which a car is driven and the number of miles it is driven in a year also affect insurance rates. Cars used for business purposes are generally driven more miles in a year than are cars driven for pleasure. This increases the chances of an accident.

The value of your car has an important effect on the cost of insurance. Premiums for collision coverage and comprehensive physical damage coverage are higher for a car worth $18,000 than for a car worth only $11,000. The insurance company runs the risk of paying out much more to the insured if the $18,000 car is destroyed or stolen. The type of car also affects the rate. Drivers of a luxury car or a sports car will pay higher rates.

Rates for automobile insurance vary from state to state. They vary from city to city within a state. The population in a particular area and the number of accidents that occur in the area also affect insurance rates. Insurance companies gather statistics on the amount of claims paid for in an area. They base their rates on this information.

The cost of your automobile insurance will vary according to the coverage you have and the deductibles you choose. The more coverage you carry, the higher the cost.

**Reducing Auto Insurance Costs**

By planning your automobile insurance purchase carefully, you can save money. For example, insurance companies often decrease the extra amount charged for young drivers if they complete a driver education course. Companies in most states also offer young people a good student discount.
Selecting a Company
Automobile insurance premiums also vary from company to company. Be sure to compare rates. Companies may offer lower rates if the family insures more than one car or if the insured buys other types of insurance from the same company. Also, paying premiums on a monthly basis is usually more expensive than paying a premium for six months or one year.

Assigned-Risk Plans
Usually as a result of bad accident records, some drivers are unable to buy automobile insurance in the normal fashion. Because of this, every state has an assigned-risk plan. Every automobile insurance company in the state is assigned a certain number of high-risk drivers, based on the amount of insurance each company sells. Each company has to insure a fair proportion of high-risk drivers. Drivers in high-risk categories pay much higher premiums.

Insurance for Other Vehicles
Insurance on motorcycles, recreational vehicles, and snowmobiles is similar to automobile insurance. Bodily injury liability, property damage liability, collision, and comprehensive physical damage insurance are the most important types of coverage. The engine size and value of the vehicle are the key factors in determining the cost. Generally, the larger and more expensive the vehicle, the higher the insurance cost.

Assessment

Key Concepts
1. Health care costs for a person you hit while driving would be covered by
   a. collision
   b. medical payments
   c. bodily injury liability
   d. uninsured motorist
2. While driving, you damage a fence. The repair costs would be covered by
   a. collision liability
   b. property damage
   c. comprehensive
   d. no-fault insurance
3. You damage your car in an accident that is covered by your collision insurance, which has a $200 deductible. If the damage to your car costs $1,200, the insurance company would pay
   a. $200
   b. $1,000
   c. $1,200
   d. $1,400

Make Academic Connections
4. Math Joan Nordland is a college student who took a driver education course in high school. She has a B+ average in her college work. She qualifies for a driver education discount of 20 percent and a good student discount of 15 percent off the premium for her automobile insurance. If the standard premium for her policy is $850 per year, how much will Joan save?
5. Communication Research automobile accident rates for various age groups. Create a graph to communicate the data.
PROPERTY INSURANCE COVERAGE

Insurance that protects you from the financial loss you would incur if some of your property were lost or destroyed due to fire, theft, vandalism, flood, or other hazard is *property insurance*. Property owners also are at risk of being sued by other people who are injured on their property. Because the risks of loss in such situations are high, everyone should carry property insurance.

Home and property insurance protect you against three kinds of economic loss.

1. Damage to your home or property
2. Expenses you must pay to live somewhere else if your home is damaged and must be repaired or rebuilt
3. Liability losses related to your property

Damage to Home or Property

You should insure your home and other expensive property for damage from fire, vandalism, unavoidable accidents, and natural disasters such as lightning, wind, and hail. If your property is damaged and you are insured, the insurance company will pay all or a portion of the cost of repair or replacement.
Additional Living Expenses
If a fire or other disaster strikes your home, one of the first shocks you will experience is that you do not have a place to live. You may have to move into a hotel, motel, or furnished apartment while your home is being repaired.

Property insurance often includes coverage for additional living expenses. This feature helps to pay for the living costs you would incur if something happened to your home.

Liability Protection
The third kind of loss, liability loss, is protected by personal liability insurance. Personal liability coverage covers claims from injuries to people or damage to property caused by you, your family, or even your pets. Suppose a neighbor slips on your icy sidewalk and it is proven you are at fault. Personal liability coverage will pay for any medical and legal costs up to a stated limit. What if a child damages a car in an adjacent driveway with a tricycle? Claims will be paid through the policy of the child’s family. Specifically, the provisions that cover liability for physical damage to the property of others will be used to determine the claim amount.

These kinds of events may seem remote and rather petty. Yet court awards to those who suffer the damage or injury are often neither remote nor petty. In fact, these awards (and therefore premiums) are increasing so quickly that the insurance industry often refers to it as the insurance liability crisis. Awards to injured people for millions of dollars are not uncommon. Everyone should have some form of liability protection from economic loss.

PROPERTY INSURANCE POLICIES
When purchasing property insurance, you must first decide what you should insure. You must also decide the perils from which you should insure your property. Perils are the causes of loss such as fire, wind, or theft.

Property permanently attached to land, such as a house or garage, is real property. Property not attached to the land, such as furniture or clothing, is known as personal property. You may insure real and personal property with a homeowners policy.

Homeowners Policies
The most common form of home and property insurance policy sold today is a homeowners policy. This coverage provides a very convenient package-type insurance policy designed to insure homes and property. Homeowners policies come in several forms.

CHECKPOINT
What are the three main types of property insurance coverage?

What different kinds of perils should a home be insured against?
### Types of Perils

<table>
<thead>
<tr>
<th>Type</th>
<th>Perils</th>
</tr>
</thead>
</table>
| **Basic** | 1. Fire or lightning  
2. Volcanic eruption  
3. Windstorm or hail  
4. Explosion  
5. Vehicles  
6. Riot or civil commotion  
7. Aircraft  
8. Smoke  
9. Vandalism or malicious mischief  
10. Theft  
11. Breakage of glass constituting a part of building |
| **Broad** | 12. Falling objects  
13. Weight of ice, snow, sleet  
14. Collapse of buildings  
15. Sudden and accidental tearing apart, cracking, burning, or bulging of a steam or hot water heating system or of appliances for heating water, an air conditioning system, or automatic fire-protective sprinkler system  
16. Accidental discharge, leakage, or overflow of water or steam from within a plumbing, heating, or air-conditioning system or domestic appliance  
17. Freezing of plumbing, heating, and air-conditioning systems, automatic fire-protective sprinkler system, and domestic appliances  
18. Sudden and accidental injury from artificially generated currents to electrical appliances, devices, fixtures, and wiring (does not include loss to a tube, transistor, or similar electronic components) |
| **Special** | All perils EXCEPT earthquake, flood, war, nuclear accidents, and certain others (Check policy for details.) |

The **basic form** of a homeowners policy insures property against the first 11 perils listed in Figure 20-2. The **broad form** covers 18 different risks. The **special form** is even more comprehensive. It covers all perils shown in Figure 20-2 and many more. The special form is sometimes referred to as an **all-risk policy**. It costs from 10 to 15 percent more than the basic policy. Such a policy insures against all perils except those excluded by the policy.

Personal liability coverage is included with all forms of the homeowners policy. With a homeowners policy, you are as protected as you would be if you bought several separate policies.

### Renters Policies

Many people rent homes, condominiums, or apartments. Their dwellings are filled with personal property. Renters have many of the same property and liability insurance needs as homeowners. A **renters policy** is a property and liability policy suitable for renters.

This policy covers household goods and personal belongings. This coverage provides protection against the same kinds of perils covered by homeowners policies. A renters policy may include personal liability coverage, but it doesn’t protect the actual dwelling. The dwelling should be covered under the owner’s policy.
Special Coverage
You can purchase policies for damage caused by flood in a flood-prone area. You can also obtain insurance to protect against economic losses caused by earthquakes. Neither of these two perils is typically covered in other policies.

Making a Claim
If you have to make a claim for a property loss, you will want to be well prepared. You should keep a list, called an inventory, of personal property that you have insured. The list should include the following information.

1. The brand name and description of each item
2. The purchase price
3. The date and place of the purchase

In addition to an up-to-date personal property inventory, insurance agents suggest keeping receipts for purchases. Taking photographs or videos of your furniture and other property can also help to support claims.

Inventory records and photographs should be stored in a location that cannot be damaged by fire, water, or smoke. If the records are lost or damaged, it will be hard to provide the insurance company with the information it needs to make a payment for your claim. A safe deposit box in a bank or other safe location away from your home is a good storage area for property records.

The age of a personal property item is quite important. Most property becomes old, gradually wears out, and decreases in value. This decrease in value is depreciation. It may affect the amount an insurance company will pay if the property is destroyed.

For example, a sofa costing $700 that is expected to last 10 years would depreciate $70 each year ($700 cost ÷ 10 years = $70 depreciation per year). Its value after six years would be $280 (depreciation per year $70 × 6 years = total depreciation $420; original cost $700 – total depreciation $420 = $280).

In recent years, homeowners have begun to purchase replacement insurance. With this method, the insurance company actually replaces an item that has been destroyed. No depreciation is deducted. Instead, the item is actually replaced no matter what the current cost may be. A replacement cost policy would pay whatever it cost to replace your property.

While over nine of ten homeowners have property insurance, only about three of ten renters have coverage for property damage and personal liability risks.

FYI
What is the value of homes in your neighborhood? How does this affect insurance rates in your area?

CHECKPOINT
How does a renters policy differ from homeowners insurance?
PROPERTY INSURANCE COSTS

As with any insurance purchase, a wise consumer should seek the proper protection at the lowest cost. This process involves making sure that you insure the property for the correct amount. You should also carefully consider the factors affecting property insurance costs. The value of a home and furnishings represents the largest investment that many people make. The purchase of a carefully selected insurance plan to protect these items makes good sense.

Coverage Selection

Suppose a family had a house built in 2001 for $100,000. They insured it for that amount. If today’s cost of building a similar house is $135,000, the current replacement value of the house is $135,000. Yet if the house is destroyed by fire, the insurance company may pay the family only $100,000.

Some insurance companies provide for automatic increases in property coverage as the price level increases. Others will pay the current replacement value if the property is insured for at least 80 percent of that replacement value.

Building costs and property values increase almost every year. Property owners should review the value of their homes and insurance coverage on a regular basis. They should determine the cost of replacing their property. They must make sure that their insurance policies provide enough protection.

Special care should be taken to correctly estimate the value of personal property. Since personal property includes many items, some may be overlooked. Most homeowners policies provide personal property coverage at 50 to 70 percent of policy value. For example, if your home is insured for $100,000, your personal property is insured for 60 percent of this, or $60,000. The value of personal property that you obtain over the years is often high. In many cases, a homeowner’s personal property is worth a great deal more than the coverage provided. Additional coverage is available for a slightly higher premium.

Why is a detailed household inventory helpful if you need to submit an insurance claim?
Insurance Premiums
Premiums paid for homeowners insurance have grown each year. Several factors determine the price that you pay for insurance on a home and furnishings. The most important factor is the estimated danger of loss based on the insurance company’s past experiences. In addition to the loss experiences, an insurance company considers the following factors in determining homeowners’ insurance premiums.

- Value of the property insured
- Construction of the building: whether it is made of brick, wood, or concrete, and the construction of the roof
- Number of claims on the property
- Type of policy (basic, broad, or special)
- Distance to the nearest fire department and water supply
- Amount of deductible (the higher the deductible, the lower the premium)
- Credit rating of the insured

You should consider these items before purchasing or building a home. You should also keep them in mind when you are shopping for insurance on a home you already own. In addition, homeowners insurance discounts are often available for policyholders who are nonsmokers, for installing smoke detectors and burglar alarms, and for buying multiple policies, such as life and auto insurance, from the same company.

Work as a Group

When items are stolen or damaged, insurance companies require that you prove the value of the item. Prepare a list of possessions that are commonly found in a home. Describe actions that might be taken to prove the value of these items.

You should consider these items before purchasing or building a home. You should also keep them in mind when you are shopping for insurance on a home you already own. In addition, homeowners insurance discounts are often available for policyholders who are nonsmokers, for installing smoke detectors and burglar alarms, and for buying multiple policies, such as life and auto insurance, from the same company.

CHECKPOINT

What factors affect the cost of home insurance?

20-2  

Assessment

Key Concepts

Determine the best answer.

1. True or False. Most property insurance policies will pay for living somewhere else while a damaged home is being repaired.
2. True or False. A garage is an example of personal property.
3. The most coverage is provided by the ___?___ form of homeowners insurance.
   a. basic  
   b. special
   c. broad
   d. renters

Make Academic Connections

5. Visual Art Use photos, drawings, and other visual images to create a display that communicates the various perils covered by property insurance.
6. Research Contact a local insurance agent to obtain information on the costs of renters insurance in your community.
Sharpen Your Life Skills

Visual Presentation of Data

“Thirty-eight percent of our customers want improved service. Sixty-three percent believe we have the best brand.” Numbers are important to every organization. Data such as this can be communicated most effectively with visuals. An audience benefits from the visual presentation of data through improved clarity and stronger recall.

Commonly used visuals include slides, transparencies, posters, videos, models, photographs, flip charts, computer images, chalkboards, dry erase boards, maps, and demonstrations. To create effective visuals, be sure to use the following guidelines.

- Keep the design simple. Include only one major idea per visual.
- Make visuals large enough to be seen by the entire audience.
- Limit how many visuals you use.
- Be concise and accurate. Proofread visuals carefully.
- Position yourself so the audience can clearly see the visuals.

Charts and graphs can enhance a presentation. Color can make charts or graphs more appealing. Be careful not to use too much color. That could overwhelm and confuse your audience. Do not portray your information in a manner that might misrepresent the data. Commonly used charts and graphs include pie charts, organization charts, bar graphs, flow charts, line graphs, and pictographs.

Presentation software such as PowerPoint can enhance an oral report. Templates and designs should be selected carefully to create audience appeal and not be distracting. When creating a presentation using software, consider these guidelines.

- Limit the text quantity to six lines per slide, six words per line.
- The text and background colors should contrast for easy reading.
- Use a consistent font style with a size that can be read.
- Images (photos, maps, graphs) can emphasize key ideas.
- Avoid distracting transitions, animation, and sound effects.

When presenting, do not read from the screen or your notes. Talk to your audience with enthusiasm, expression, and voice projection.

Think Critically
1. How can visuals enhance the effectiveness of a presentation?
2. Create a visual that could be used with a presentation for a class or other situation.
Life Insurance

Goals
- Discuss the principles of life insurance.
- Explain the types of life insurance.
- Describe the process of buying life insurance.

Key Terms
- beneficiary
- term life insurance
- permanent life insurance

Focus on Real Life
“Last night I started thinking about college education for my two youngsters. I need to start planning for their future. It seems like I take care of their day-to-day needs, but I have forgotten about their future needs!”

“Rafael, have you considered borrowing on your life insurance policy when the time comes for the children to go to college?” asked Steve.

“You probably won’t believe this, Steve, but I don’t have any life insurance. I have other kinds of insurance, but I thought I was too young to worry about life insurance.”

“Everyone needs life insurance to protect their family against economic loss. And if you buy a permanent policy soon, you may be able to use it to your advantage when your children need cash for college.”

While developing a plan for the future welfare of his children, Rafael should certainly include the purchase of life insurance. He will need to decide what kind of life insurance to buy, how much to buy, and where to buy it.

LIFE INSURANCE PRINCIPLES
Life insurance protects survivors against financial loss associated with death. Specifically, it is designed to replace a loss of income for family members who are financially dependent upon another person. Life insurance can also be considered a means of saving or investing, but its primary purpose is always protection against financial loss.

The Life Insurance Policy
A life insurance policy is a contract between the insurance company and the person buying the insurance, called the insured. The following are the major elements of a life insurance policy.
- Name of the insured
- Amount of coverage, also called the face value or death benefit of the policy
- Cost of the insurance, called the premium amount
- Name of the beneficiary

Beneficiary Selection
When you buy life insurance, you must name a beneficiary. A beneficiary is the person named in the policy to receive the insurance benefits. The beneficiary is most often a spouse, children, or other dependents. You may insure not only your own life, but also the life of any person in whom you have an insurable interest. To have an insurable interest in the life of another person, you must receive some kind of financial benefit from that person’s continued life.
You have, for example, an insurable interest in the lives of your parents. You do not have an insurable interest in a stranger’s life. A partner in a business has an insurable interest in the lives of other partners.

**Checkpoint**

What is an insurable interest?

**Types of Life Insurance**

Insurance companies offer a variety of life insurance plans that meet different needs. The two basic types of life insurance policies are term life and permanent, or cash value, life.

**Term Life Insurance**

Insurance that provides financial protection from losses resulting from a death during a definite period, or term, is term life insurance. This coverage is the least expensive form of life insurance. Term insurance is also the only form of life insurance that is purely life insurance. All other forms of insurance also have savings or investment features.

Term policies may run for a period of 1 to 20 years or more. If the insured dies during the period for which the insurance was purchased, the amount of the policy is paid to the beneficiary. If the insured does not die during the period for which the policy was purchased, the insurance company is not required to pay anything. Protection ends when the term expires.

By paying a slightly higher premium, a person can buy renewable term insurance. This type of policy allows the policyholder to continue term insurance for one or more terms without taking another physical examination.

Term insurance policies may be level term or decreasing term. With level term insurance, the amount of protection and the premiums remain the same while the insurance is in effect. With decreasing term insurance, the amount of protection gradually becomes smaller, but premiums remain the same during the term. This is often appropriate because the need for insurance normally declines as children become independent and other savings and investments grow.

**Permanent Life Insurance**

The common characteristics of permanent life insurance are that it has cash value and an investment feature. Part of the premium you pay for permanent life insurance is used for insurance that provides protection. This feature is just like term insurance. The insurance company invests the remaining part of the premium that is not needed to pay for the coverage. It adds to the cash value of the insurance policy.
Cash value refers to the amount of money that the insurance company will pay if the policyholder decides the insurance is no longer needed. The cash value is much less than the death benefit that would be paid to beneficiaries. As long as permanent policies are kept in force, they accumulate cash value in addition to providing life insurance.

The longer you keep your permanent life insurance policy, the higher its cash value will be. If you give up or surrender your policy, you receive the amount of the cash value. If you need money but do not want to cancel your policy, you can borrow an amount up to the cash value from the insurance company. If you should die before the loan is repaid, the insurance company will withhold the unpaid amount from the face value of the policy when it pays your survivors. Face value is the amount of insurance coverage that was originally purchased and that will be paid upon the death of the insured.

The cash value of permanent life insurance can be seen as a savings plan. Usually, the return on your money in the cash value portion of permanent life insurance is not large. Nevertheless, permanent insurance plans have a built-in savings feature that encourages people to save for the future. Permanent life insurance comes in the form of whole life, variable life, and universal life policies. Each type builds up cash value.

Whole Life Insurance Permanent insurance that extends over the lifetime, or whole life, of the insured is whole life insurance. One type of whole life insurance is an ordinary life policy. Premiums for ordinary life insurance remain the same each year as long as the policyholder lives.

Some whole life insurance policies are meant to be paid in full in a certain number of years. Limited-payment policies may be designated by the number of years the policyholder agrees to pay on them, such as 20-payment life policies. They are like ordinary life policies except that premiums are paid for a limited number of years or until a person reaches a certain age. Limited-payment policies free the insured from paying premiums during retirement when income may be lower.

Variable Life Insurance An insurance plan that resembles an investment portfolio is variable life insurance. This plan lets the policyholder choose among a broad range of investments. These investments include stocks, bonds, and mutual funds. The death benefits and cash values of variable life policies vary according to the yield on the investments that the policyholder selects.

The insurance company first designates an amount of the variable life premiums to cover the cost of insurance. It places the remaining amount in an
insurance account. Both the death benefit and the cash value rise and fall with the success of the investment account.

A variable life policy might guarantee a minimum death benefit. There is no guaranteed cash value. The minimum death benefit, in relation to premiums paid, is well below other types of life insurance. On the positive side, a strong rate of return on the investment account can increase the cash value and the death benefit.

**Universal Life Insurance**

*Universal life insurance* provides both insurance protection and a substantial savings plan. The premium that you pay for universal life insurance is split in three ways. One portion of it pays for insurance protection. The insurance company takes a second portion for its expenses. The third portion goes into interest-earning investments for the policyholder.

The most important feature of universal life insurance is that the investment portion of the policy earns a variable rate of return. This rate is usually higher than is paid on other types of cash value life insurance. This yield on the investment portion tends to rise or fall based on changing economic conditions. Figure 20-3 compares the features of the different types of life insurance.

### Figure 20-3

<table>
<thead>
<tr>
<th>Types of Life Insurance Policies</th>
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<tbody>
<tr>
<td><strong>TERM INSURANCE</strong></td>
</tr>
<tr>
<td><strong>Whole Life</strong></td>
</tr>
<tr>
<td><strong>Ordinary Life</strong></td>
</tr>
<tr>
<td><strong>Limited Life</strong></td>
</tr>
<tr>
<td><strong>Premium</strong></td>
</tr>
<tr>
<td><strong>Payment Period</strong></td>
</tr>
<tr>
<td><strong>Cash Value</strong></td>
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<tr>
<td><strong>Death Benefit</strong></td>
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<tr>
<td><strong>Purposes</strong></td>
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**Which kind of insurance is least expensive for a given amount of death benefit?**

**Variable Life**

**Universal Life**

---

**Figure 20-3**

<table>
<thead>
<tr>
<th><strong>TERM INSURANCE</strong></th>
<th><strong>PERMANENT INSURANCE</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Whole Life</strong></td>
<td><strong>Variable Life</strong></td>
</tr>
<tr>
<td><strong>Ordinary Life</strong></td>
<td>Fixed</td>
</tr>
<tr>
<td><strong>Limited Life</strong></td>
<td>Higher than ordinary life insurance but constant</td>
</tr>
<tr>
<td><strong>Premium</strong></td>
<td>High, but usually stays constant</td>
</tr>
<tr>
<td><strong>Payment Period</strong></td>
<td>Life of the insured</td>
</tr>
<tr>
<td><strong>Cash Value</strong></td>
<td>Some cash value</td>
</tr>
<tr>
<td><strong>Death Benefit</strong></td>
<td>Fixed</td>
</tr>
<tr>
<td><strong>Purposes</strong></td>
<td>Protection for life, some cash value for policyholder</td>
</tr>
<tr>
<td></td>
<td>Protection for life, some cash value for policyholder</td>
</tr>
<tr>
<td></td>
<td>Protection for life, some cash value for policyholder</td>
</tr>
<tr>
<td></td>
<td>Life insurance plus an opportunity to select different cash value investment options</td>
</tr>
<tr>
<td></td>
<td>Life insurance with a fairly high rate of return on cash value</td>
</tr>
</tbody>
</table>
Group Life Insurance
Some individuals are fortunate to have an employer or some other group offer the opportunity to buy group life insurance. An insurance policy that covers a group of people is called group life insurance. The group acts as a single unit in buying the insurance.

The cost of group life insurance is less than the cost of a similar individual policy. This savings results from the insurance company covering many people in one policy.

Most group life insurance plans offer term rather than permanent insurance. The insurance company works with an employer or other organization, such as a union, to develop the insurance plan. Then, each employee or member of the organization may purchase individual life insurance coverage.

BUYING LIFE INSURANCE
Almost everyone needs life insurance at some time in their lives. Few people have the financial resources needed to pay the costs that can build up upon the death of someone close to them. For a life insurance program to be effective, it must fit your needs and those of your family.

Coverage Amount
Anyone with dependents needs life insurance. A dependent is a person who must rely on another for financial support. In the future, you will need to ask the question, “What would happen to the people who are financially dependent on me if I died tomorrow?” If they could not live financially in the way in which they lived before your death, you most likely need life insurance.

The following questions will help to determine the need for life insurance.

- How much money is required for your dependents’ financial stability if your income is lost?

Why do people working in dangerous occupations cost more to insure?
Work as a Group

Knowing how much life insurance to have can be a difficult decision. In your group, prepare a list of factors that a person might consider when determining the amount of life insurance to obtain.

- How much income will you need when you retire and what will be the sources of your income?
- What can you afford to pay for your life insurance needs?

Answers to these questions will help you purchase the best life insurance program for you.

Life Insurance Application

To buy individual life insurance coverage, you need to complete a life insurance application. You apply for this coverage through an insurance agent representing an insurance company.

You may be required to take a physical exam to assess your health. If you have no serious health problems, you then pay a premium and receive your life insurance policy.

If you are in poor health or work in a dangerous job, you may be considered a poor risk. Even so, you may still be able to get insurance. You will probably pay higher premiums than people who are in good health and are employed in less hazardous jobs.

Premium Payments

In addition to the health and occupation of the insured, the type of policy affects the cost of life insurance. The age of the person being insured also affects premiums. In purchasing a whole life policy, for example, the premiums for ordinary life insurance are higher than those for term insurance, but the annual premium stays the same throughout the insured’s life. The premiums on limited-payment life insurance are higher than those for ordinary life insurance, but they are payable for only a limited number of years.

20-3 Assessment

Key Concepts

Determine the best answer.

1. __?__ life insurance is considered temporary coverage.
   a. Whole    b. Universal
c. Term      d. Variable

2. The beneficiary of a life insurance policy
   a. is the cost of insurance
   b. makes the premium payments
   c. receives money when the insured dies
d. is the period for which the policy is in effect

Make Academic Connections

3. Technology Conduct a web search to locate additional information about applying for life insurance. What actions are necessary in this process?

4. Math The rate of return on the investment portion of a life insurance policy is 6.47 percent for a given year. If the investment portion (cash value) was $17,643 at the beginning of the year, what will it be worth at the end of the year? Round to the nearest cent.
HEALTH INSURANCE COVERAGE

Several types of health-related insurance are available to provide different kinds of coverage. One type of health insurance is medical insurance. It can be classified as (1) hospital insurance, (2) surgical insurance, (3) regular medical insurance, (4) major medical insurance, and (5) a comprehensive medical policy. Insurance companies also offer combination policies.

Hospital Insurance

An illness or injury may require you to be hospitalized. In this situation, hospital insurance usually pays most or all of the charges. These include expenses for your room, food, and medical items such as use of an operating room, anesthesia, X rays, laboratory tests, and medications. Because of the high cost of hospitalization, people purchase hospital insurance more than any other kind of health insurance.

You can buy hospital insurance from nonprofit corporations, such as Blue Cross, or from insurance companies. If expenses are more than the amount covered by the hospital insurance plan, the patient must pay the difference.

Surgical Insurance

Surgery is a major reason for hospitalization. It can be very expensive. Surgical insurance covers all or part of the surgeon’s fees for an operation. The typical surgical policy lists the types of operations that it covers and the amount allowed for each. Some policies allow larger amounts for operations than others. This, of course, requires that a higher premium be paid. Surgical insurance is often bought in combination with hospital insurance.

Focus on Real Life

“Carlotta! Welcome back to work! How is your back?”

“My back is doing great. I can’t believe I hurt it and had to have surgery. I am almost feeling normal again, and the insurance company paid all of my bills. You don’t realize how important health insurance is until you need it. If I didn’t have such great coverage, I would be out over $100,000.”

Almost no one has enough money to pay the medical bills associated with a serious illness. Health insurance provides protection against the economic risks associated with paying for medical care. It also provides protection from the loss of income that results when an injury or illness prevents you from working. Health insurance is similar to the other forms of insurance. You pay premiums for a policy that guarantees protection. When you are ill and need money to pay medical bills, the insurance company will pay the bills up to specified amounts.
Again, you can buy surgical insurance from insurance companies or from nonprofit organizations. Surgical plans cover mainly medical and surgical treatment rather than hospital care. These plans list the maximum amounts that they will pay for different types of surgery. They also cover the doctor’s charges for care in the hospital. Some plans pay the doctor’s charges for office or home care. The coverage generally does not provide for preexisting conditions or for illnesses or injuries that are covered by other insurance.

**Regular Medical Insurance**

Sometimes normal care provided by a physician can be quite expensive. **Regular medical insurance** covers fees for nonsurgical care given in the doctor’s office, the patient’s home, or a hospital. The policy states the amount payable for each visit or call. It also lists the maximum number of visits covered. Some plans provide payments for diagnostic and laboratory expenses.

Regular medical insurance is usually combined in one policy with hospital and surgical insurance. The protection provided by regular medical, hospital, and surgical insurance is often referred to as **basic health coverage**.

**Major Medical Insurance**

Long illnesses and serious injuries can be very expensive. Bills of $50,000 to $100,000 and higher are not unusual. **Major medical insurance** provides protection against the high costs of serious illnesses or injuries. This coverage complements the other forms of medical insurance.

Major medical insurance helps pay for most kinds of extended and specialized health care prescribed by a doctor. It covers the cost of treatment in and out of the hospital, special nursing care, X rays, psychiatric care, medicine, and many other health care needs. Maximum benefits may be limited, but usually extend to a high amount, such as $500,000 or $1,000,000.

All major medical policies have a **deductible** clause. The clause is similar to the one found in automobile collision insurance. With this clause, the policyholder agrees to pay the first part of the expense resulting from sickness or injury. The deductible may be $500 or more.

Major medical policies usually contain a **coinsurance** clause. **Coinsurance** is the sharing of expenses by the policyholder and the insurance company. The policyholder typically pays a deductible and then shares the remaining cost with the insurance company.

For example, the insurance company may pay 80 percent of the cost for medical treatment after the deductible is paid. The policyholder will then pay the remaining 20 percent. The policyholder’s share is limited to a specific dollar amount stated in the policy. Once the deductible and the coinsurance amounts are met, the insurance
company reimburses 100 percent of the cost up to the policy’s coverage limits.

The deductible clause discourages the filing of minor claims. The coinsurance clause encourages the policyholder to keep medical expenses as reasonable as possible. Thus, both clauses help to lower premiums because they help to reduce payments of insurance claims.

**Comprehensive Medical Policy**

Insurance providers have developed a comprehensive medical policy that combines the features of hospital, surgical, regular, and major medical insurance. This coverage retains the features of each separate coverage, such as amounts-payable limits. The policy has only one deductible. A combination of coverages will likely be less expensive than the total of the separate coverages.

**Dental Insurance**

As dental expenses have grown over the years, insurance companies now offer coverage to help pay for normal dental care. Dental insurance usually includes examinations, X rays, cleaning, and fillings. It may cover part or all of complicated dental work such as crowns or bridges. This policy also covers dental injuries resulting from accidents.

Most dental plans contain deductible and coinsurance provisions to reduce the cost of premiums. Dental insurance is offered mainly through group plans. It continues to grow in popularity.

**Vision Care Insurance**

In anticipation of eye care expenses, many consumers and groups purchase vision care insurance. These policies cover eye examinations, prescription lenses, frames, and contact lenses. New medical developments may result in additional vision care coverage. Some plans now cover the cost of laser eye surgery that eliminates the need for glasses.

**CHECKPOINT**

What four types of health insurance would be included in a comprehensive medical policy?
HEALTH INSURANCE PROVIDERS

Health insurance is available from several sources. These options include group health insurance, individual health insurance, health maintenance organizations, preferred provider organizations, and government programs.

Group Health Insurance

The most popular way to buy health insurance is through a group. As with group life insurance, employers, unions and other organizations offer group health insurance policies.

Companies that sponsor group policies often pay part or all of the premium costs for their employees. They provide this as an employment benefit. Employees can usually buy coverage for family members as well.

The cost of group health insurance is lower per insured than the cost of a comparable individual policy. The costs are lower because insurance companies can manage group plans more economically.

Individual Health Insurance

Some people are not eligible for group health insurance. They may be self-employed and have no employer to help buy health insurance. One alternative is to buy individual health insurance. These policies are available to individuals and are adapted to individual needs. Individual health insurance policies are usually rather expensive. They require a physical exam and have a waiting period before the policy takes effect.

Technology Topics

Geocaching: The Thrill of the Hunt

Why would a person spend days to locate a “treasure” worth less than a dollar? The answer is “geocaching.”

Geocaching is an adventure game using a global positioning system (GPS) to locate caches. These small storage containers are “treasures” that vary in size, location, and contents. The GPS unit can find an approximate location (within 6-20 feet) anywhere on earth. Once found, a cache provides visitors with various rewards. The visitor may be asked to take something from the cache, leave something, or write in a logbook.

People all around the world set up caches. More than 100,000 active caches exist in over 200 countries with location information on the Internet. A cache may be just a logbook with valuable or entertaining information. It may be a waterproof bucket placed within the local terrain with a logbook and valuable items—this makes geocaching a true treasure hunt! Food is never put in a cache since animals will find the cache first.

Most caches are in parks, forests, and other natural settings. Some can only be accessed by rock climbers or with scuba equipment. In cities, caches may be below ground or inside and outside buildings. The thrill of the search and excitement of the find keeps geocachers on the trail of their next adventure.

Think Critically

1. What do the “geo” and “caching” in geocaching refer to?
2. What are educational and economic benefits of geocaching?
3. Conduct an online search to obtain additional information about geocaching.
Managed Care Plans
Various alternative health insurance plans have grown in popularity. Known as managed health care or managed care, these programs cover more than two-thirds of Americans who have insurance through their employer. These plans often provide lower-cost, comprehensive health care through networks of medical professionals.

Managed care plans usually have higher monthly premiums. Yet the overall cost of health care may be lower for the consumer because of lower deductibles, low copayments, and little or no paperwork. A potential drawback is that patients have less control and limited choices of whom they see for health care. Managed care plans have various names, such as HMOs (health maintenance organizations) and PPOs (preferred provider organizations).

The growth of managed care has resulted from large companies trying to control the rising cost of providing health care coverage for employees. Today, many managed care plans are run by insurance companies.

Health Maintenance Organization (HMO) One managed care choice is a health maintenance organization. A health maintenance organization (HMO) commonly consists of a staffed medical clinic to serve members. You join an HMO for a fixed monthly fee. As a member, you are entitled to a wide range of prepaid health care services, including hospitalization. HMOs emphasize preventive health care. Early detection and treatment of illnesses help reduce hospital visits and keep costs down. Generally, HMOs do not cover treatment or care that is not authorized by a physician or procedures that are above the average cost for the area.

Preferred Provider Organization (PPO) A popular alternative is the preferred provider organization (PPO). This system involves several health care providers, such as a group of physicians, a clinic, or a hospital. These medical professionals contract with an insurance company to provide services to members. These providers agree to charge set fees for services.

Members are encouraged, but not required, to use the PPO services through financial incentives. Members are able to get medical treatment through the PPO at a significant discount. They may seek medical treatment elsewhere. However, expenses for treatment outside the PPO may be only partially reimbursed.

State Government Assistance
An important health insurance program by state governments is workers compensation. This insurance plan provides medical and survivor benefits for people injured, disabled, or killed on the job. Accidents can occur on almost any job. Employees may suffer injuries or develop some illness because of working conditions. Workers compensation laws provide medical benefits to employees who are injured on the job or become ill as a direct result of their working conditions. Under these laws, most employers are required to provide and pay for this insurance for their employees.

State governments also administer a form of medical aid to low-income families known as Medicaid. The federal government shares with states the cost of providing health benefits to financially needy families. The services

Work as a Group
Everyone is affected by rising health care costs. In your group, prepare a list of actions that might be taken by (a) individuals, (b) businesses, and (c) government to (1) improve the health of people in society and (2) reduce costs for medical services.
covered by Medicaid include hospital care, doctor services, X rays, lab tests, nursing home care, and home health care services. States may also offer a health insurance program for people who have trouble obtaining coverage. Past health conditions can result in a person being turned down by most health insurance providers.

**Federal Government Assistance**
The nation’s Social Security laws provide a national program of health insurance known as Medicare. This insurance is designed to help people aged 65 and older and some disabled people pay for health care. Medicare has two basic parts: hospital insurance and medical insurance.

The hospital insurance plan includes coverage for hospital care, service in an approved nursing home, and home health care up to a certain number of visits. No premium payments are required for the hospital insurance. Almost everyone 65 years old and older may qualify.

The medical insurance portion of Medicare is often called supplementary or voluntary medical insurance. The services covered under this plan include doctor services, medical services, supplies, and home health services. The medical insurance requires a monthly premium. The federal government pays an equal amount to help cover the cost of the medical insurance.

**Cost Containment**
The cost of health insurance is very high. In fact, health care costs consistently increase two to three times faster than the overall cost of living. The cost of health insurance is determined by four main factors: extent of the coverage, number of claims filed by policyholders, age of the policyholder, and number of dependents. You have little control over your age and the number of people dependent on you. You can make sure you buy only the kind and amount of insurance you need. You can also take good care of yourself and not use your medical benefits unnecessarily.

Insurance companies encourage policyholders to play an active role in cost containment, or keeping costs down. The most common methods are coinsurance and deductibles.

Some policyholders have coverage under both their employer’s and their spouse’s insurance. Insurance providers coordinate benefits to prevent two or more insurers from making payments on the same charges. The health insurance industry encourages second opinions to ensure the necessity of procedures.

Another cost-containment strategy is the use of outpatient services such as surgery. In the past, people undergoing some forms of surgery might have been admitted to the hospital for one or two days. Now, the person comes to the hospital or an outpatient center in the morning. After the surgery, the patient returns home the same day.
The need for health insurance goes beyond various medical expenses. Disability income and long-term care insurance programs protect people in other types of situations.

**Disability Income Insurance**

For most people, income from employment is their single most important economic resource. Protecting your income is very important. One form of health insurance provides periodic payments if the policyholder becomes disabled. **Disability income insurance** protects you against the loss of income caused by a long illness or an accident. The insured receives weekly or monthly payments until they are able to return to work.

Disability income policies often include a waiting period. This requires the policyholder to wait a specified time after the disability occurs before payment begins. Monthly payments under disability insurance plans are usually much smaller than the income people earn from their jobs. The amount may be 40–60 percent of the normal income, but many disability payments are not subject to income taxes.

**Long-Term Care Insurance**

With people living longer, **long-term care insurance** is the fastest-growing type of protection. This coverage provides **long-term care**, which is daily assistance needed because of a long-term illness or disability. This assistance may involve a stay in a nursing home. It may cover help that is provided at home for daily activities such as dressing, bathing, and doing household chores.

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**20-4**

**Assessment**

**>> Key Concepts**

Determine the best answer.

1. Health insurance coverage for a long illness is __?__ insurance.
   a. hospital
   b. surgical
   c. regular medical
   d. major medical

2. A state government health insurance plan for low-income workers is
   a. Medicare
   b. Medicaid
   c. workers compensation
   d. an HMO

**>> Make Academic Connections**

3. **Geography** Identify various health concerns in several regions of the world. Create a map to show the areas of these illnesses and other medical concerns.

4. **Visual Communication** Create a poster or video that communicates actions for wise health care behaviors.
20-1 Vehicle Insurance
1. Motor vehicle risks include having an accident, having your vehicle stolen, injuring yourself or another person, or damaging another’s property.
2. Personal injury insurance covers bodily injury liability, medical payments, and uninsured motorist protection. Property damage liability protects you against claims if you damage another person’s property.
3. Automobile insurance rates are affected by age, accidents, marital status, academics, credit rating, car use, number of miles driven a year, value of car, and where you live.

20-2 Property Insurance
4. Home and property insurance protect against three economic losses: (1) damage to home or property, (2) expenses to live somewhere else if your home is badly damaged, and (3) liability losses.
5. A homeowners insurance policy provides coverage for various perils. Renters insurance is available for those who rent.
6. Wise consumers select the most appropriate protection at the lowest cost.

20-3 Life Insurance
7. Life insurance protects survivors against the financial loss associated with dying. It replaces a loss of income for a family who is financially dependent upon another person.
8. Term life insurance provides financial protection from losses of life during a definite period. Permanent insurance has both cash value and an investment feature.
9. To buy individual life insurance coverage, a person applies to an insurance agent. A physical exam may be required to assess the person’s health. Life insurance premiums depend on the type of policy and the age and health of the person being insured.

20-4 Health Insurance
10. Five common types of medical insurance are hospital insurance, surgical insurance, regular medical insurance, major medical insurance, and a comprehensive policy. Dental and vision care insurance provide specific coverage for these medical needs.
11. Health insurance providers include group health insurance, individual health insurance, health maintenance organizations, preferred provider organizations, and government programs.
12. Disability income insurance protects against income loss due to illness or accident. The insured receives payments until able to return to work. Long-term care insurance provides daily assistance needed because of a long-term illness or disability.

Communicate Business Concepts
1. Which type of automobile insurance would cover the following situations?
   a. A pedestrian is injured by a driver.
   b. A family member is injured when you run into a parked car.
   c. You, in an attempt to avoid hitting a dog in the street, run into a parked car.
   d. Winds cause a tree branch to break your windshield and dent the hood.
2. A driver was at fault when three passengers were badly hurt. The court awarded two of the people $30,000 each and $45,000 to the third person. The driver had bodily injury liability coverage of 50/100. Was this enough coverage for financial loss? Why or why not?
3. Why is collision coverage on a 10-year-old car less important than on a three-year-old car? Why may a person still want to have collision coverage on a 10-year-old car?
4. What type of property insurance would cover these situations?
   a. Damage to furniture because of a fire
   b. The cost of staying at a hotel after your home was damaged by fire
   c. Injury to a repairperson on your property

5. Recently, homes in an Iowa valley were destroyed when heavy rains caused the Mississippi River to rise above flood level. Do you think those Iowa residents who had homeowners policies suffered any financial losses? Why or why not?

6. What type of life insurance policy would you recommend for these people?
   a. Carlos Medina, age 27, wants a policy with premiums as low as possible for the next 10 years.
   b. Julie Hovel, age 45, wants a policy with no premium payments after she retires.

7. Why is a physical examination not usually required when buying group life insurance coverage?

>> Develop Your Business Language

Match the terms listed with the definitions.

8. Health insurance that covers all or part of surgeon’s fees.
9. The person named in the life insurance policy to receive the benefits.
10. Covers claims for injuries or damage to property caused by you or your family.
11. The amount the insured pays before the insurance company pays a claim.
12. Coverage that provides protection against the high costs of serious illnesses or injuries.
13. Coverage for claims resulting from injuries or deaths for which the insured is at fault.
14. Health coverage for your room, food, and other hospital expenses.
15. The decrease in value of property.
16. Insurance coverage for medical expenses of a policyholder and family members if they are injured while riding in a car.
17. Coverage for injuries caused by hit-and-run drivers or by drivers without insurance.
18. Protection against the loss of income caused by a long illness or an accident.
19. Life insurance coverage with a cash value and an investment feature.
20. Coverage that protects a driver against claims if the insured’s car damages someone else’s property.
22. A package-type insurance policy designed to insure homes and property.
23. Auto coverage for a loss resulting from a collision with another car or object.
25. Auto coverage for almost all damage losses except those caused from a collision.
26. Life insurance that provides financial protection during a set period.
27. The sharing of expenses by the policyholder and the insurance company.

Key Terms

a. beneficiary
b. bodily injury liability
c. coinsurance
d. collision
e. comprehensive coverage
f. comprehensive medical policy
g. deductible
h. depreciation
i. disability income insurance
j. homeowners policy
k. hospital insurance
l. major medical insurance
m. medical payments
n. permanent life insurance
o. personal liability coverage
p. property damage liability
q. regular medical insurance
r. surgical insurance
s. term life insurance
t. uninsured motorist
Decision-Making Strategies

Jane is a rather careless driver. She is a 17-year-old with a late-model compact car that looks sporty and is equipped for speed. Jane loves to drive fast and has compiled a rather poor traffic record. In only one year, she has had two “fender bender” accidents and received two speeding tickets. Those who care about Jane have suggested that her reckless driving habits are putting her and others at risk.

28. What potential property and liability risks are associated with Jane’s driving habits?
29. How is Jane’s driving affecting her auto insurance premiums?
30. What suggestions do you have for Jane about her driving?

Make Academic Connections

31. **LAW** Obtain information on the financial responsibility and automobile insurance requirements in your state.
32. **RESEARCH** Contact a local insurance agent to obtain information on the costs of automobile insurance for young drivers.
33. **MATH** Orien Defoe was involved in an automobile accident. The total damage to both vehicles was $3,228. The state in which Orien lives assigns a percentage of fault to each driver involved in an accident. Each driver must pay the percentage of damages based on the percentage of fault assigned. If Orien was assigned 35% of the fault in the accident, how much of the damages will he be required to pay? How much must the other driver pay?
34. **LAW** Describe in writing or present in class various liability situations that would be covered by a person’s homeowners or renters insurance policy.
35. **ACCOUNTING** The value of personal property declines due to time and use. Using newspaper advertisements and other information sources, compare the value of various new and used items. What observations can you make about depreciation?
36. **MATH** If Ellen Williams owned a home worth $98,000 and wanted to be certain it was insured for at least 80 percent of its value, for how much should it be insured?
37. **COMMUNICATION** Write and present a short script that communicates the need for life insurance in various family situations.
38. **RESEARCH** Conduct library or online research about actions that might be taken to reduce the costs of health care.
39. **LANGUAGE ARTS** Create a poster or other visual media to educate and remind classmates about automobile safety. Include information on both safe driver and safe pedestrian habits. Display the posters in your school or obtain permission to hang them in your local government office.
40. **MATH** Fran Markowitz had her annual medical examination. According to her insurance plan, she paid a portion of the costs of the services. The total costs and her share of each were as shown in the table.

<table>
<thead>
<tr>
<th>Service</th>
<th>Total Cost</th>
<th>Patient Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Doctor visit</td>
<td>$80</td>
<td>$15 deductible</td>
</tr>
<tr>
<td>Lab work</td>
<td>$220</td>
<td>20% copay</td>
</tr>
<tr>
<td>Prescriptions</td>
<td>$120</td>
<td>$20 copay</td>
</tr>
<tr>
<td>Vision exam</td>
<td>$65</td>
<td>$10 deductible</td>
</tr>
<tr>
<td>New lenses</td>
<td>$180</td>
<td>5%</td>
</tr>
</tbody>
</table>

a. What was the total cost of the medical examination?
b. How much of the total cost did Fran pay?
c. What percent of the total cost did the insurance company pay?
**Linking School and Home**

Most people have several types of insurance. Talk to family members and friends. Ask them to name the types of insurance coverage they have. What coverage has been obtained through group policies and which are individual policies? What suggestions do they have for you when buying various types of insurance?

**Portfolio Activity**

To provide tangible evidence of your learning about insurance, do the following:

**COLLECT** examples of the main risks faced by most people. Obtain photos, graphics, and other visual images that communicate potential financial losses related to a person’s life, health, home, and motor vehicle.

**CREATE** a summary poster (or computer presentation) using these visuals. Show the relationship of the visuals to the types of insurance coverage available.

**CONNECT** your visual to other items already in your class portfolio. Why is insurance important to other business activities? Alternatively, relate your visual to an important concept you learned in another class. Make the connection by writing a one-paragraph summary of how insurance links to the topic.

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**Entrepreneurship Case Study**

This event is composed of two parts: a written objective test and a decision-making problem (case study). Teams consisting of three participants will present and defend their solution to a business challenge.

Once you receive your business topic, you have 30 minutes to prepare your presentation and argument. Each participant will be given two 4” by 6” index cards that may be used during the preparation and presentation to the judges/students. No reference materials or visual aids may be brought to or used during the preparation or performance.

Your team has 10 minutes to present the case. One member should introduce the team and describe or summarize the case study. All team members must participate in the presentation. Note cards may be used to explain decisions and rationales to the judges. After the presentation, five minutes are allowed for questions and answers.

Your case study involves the rising cost of insurance. Health insurance is an important fringe benefit that you provide your employees. The cost of health insurance is rising at a rapid rate, and now your company is faced with determining strategies to continue paying for employee health insurance. You must determine how you will pay for the increasing costs. What will you do to keep employees healthy? How will you shop around for insurance? What other expenses are you willing to cut in order to continue funding health insurance?

**Performance Indicators Evaluated**

- Understand the importance of health insurance for employees.
- Prepare a concise plan for funding the rising costs of health insurance.
- Explain the sacrifices that must be made to fund health insurance.
- Explain the importance of shopping around for health insurance.

*For more detailed information about performance indicators, go to the FBLA web site.*

**Think Critically**

1. Why is health insurance such an important fringe benefit?
2. What can a company do to encourage employees to follow healthy lifestyles?
3. What fringe benefits are you willing to cut in order to save health insurance?

Global Business Project

Manage International Business Operations

Goals
• Identify consumer buying habits in various cultures.
• Research common financial institutions in other countries.
• Explore cultural attitudes toward the use of credit.
• Analyze the investment environment of a foreign country.
• Create a global risk management plan and recommend insurance coverage.

Activities
Use your textbook, library materials, web sites, interviews with people, and other resources to complete the following:

1. Buying habits in other cultures can be different. Using the country in your portfolio (or select a country), research customs, traditions, and beliefs that affect buying behaviors or eating habits in that nation. Describe various goods and services that might need to be adapted when being sold in this country.

2. Banks and other financial institutions provide funds and transfer money for business transactions. Research the banking system and payment activities in the country from your portfolio (or another country). To what extent is electronic banking used in that country?

3. Attitudes toward credit vary around the world. Obtain information about the cultural feelings toward the use of credit in another country. How might this information affect a company’s international business activities?

4. Individuals and companies want to invest in countries with strong economic and business potential. Using the country you have studied (or another one), research expected economic conditions and business...
opportunities for this nation. What recommendations would you make to investors about this country?

5. Select a company involved in international business. Obtain recent financial statements for the company. Prepare a summary of its recent financial situation and the international operations of the company.

6. The use of insurance is a common part of a risk management plan. Describe the liability and property insurance a global company might need.

**Present**

Prepare a portfolio (folder, file, or notebook) to store the information and materials you created in the activities above.

1. Create a poster, slide presentation, web site, or video showing different buying behaviors in other countries. Describe how a product or service might need to be changed based on the culture and traditions in another country.

2. Develop a flowchart or graph that shows the banking system and payment activities in another country. Explain how various payment methods (the country’s currency, checks, credit cards, and electronic banking) are used by individuals and businesses.

3. Prepare a written report (with visuals) describing the investment potential of another country. Describe economic and business strengths of the country. Point out areas of concern about which investors should be aware. Use visuals (photos, tables, maps) to communicate the strengths and weaknesses of the country’s investment environment.

4. A common method for reducing global business risk is working with a partner in another country. Create an in-class presentation (or video) explaining a joint venture that might be established when doing business in another country.
KINDS OF CALCULATORS

Many different models of calculators, both desktop and hand held, are available. All calculators have their own features and particular placement of operation keys. Therefore, it is necessary to refer to the operator’s manual for specific instructions and locations of the operating keys for the calculator being used.

HAND-HELD CALCULATORS

There are many different kinds of hand-held or pocket calculators. They come in all shapes and sizes. They also come with a variety of keys and functions. All calculators have number keys (0 to 9), operation keys (+, −, ×, ÷), and clear keys (C or CE). Most calculators have a percent key (%). Some hand-held calculators come with a memory for storing numbers and calculation results. These are shown as M+, M−, and MR. Others, such as scientific calculators, have many more keys including \(x^2\), 1/x, and √.

For hand-held calculators, it is important to read the operator’s or owner’s manual to learn how to operate your particular calculator. Be sure to keep the manual in a safe place so you can refer to it for help in solving various mathematical problems.

DESKTOP CALCULATORS

Several operating switches on a desktop calculator must be engaged before the calculator will produce the desired results.

The decimal selector sets the appropriate decimal places necessary for numbers that will be entered. For example, if the decimal selector is set at 2, both the numbers entered and the answer will be displayed with two decimal places. If the decimal selector is set at F, the calculator automatically sets the needed decimal places. The F setting allows the answer to be unrounded and carried out to the maximum number of decimal places possible.

The decimal rounding selector rounds the answers. The down arrow position will drop any digits beyond the last digit desired. The up arrow position will drop any digits beyond the last digit desired and round the last digit up. In the 5/4 position, the calculator rounds the last desired digit.
up only when the following digit is 5 or greater. If the following digit is less than 5, the last desired digit remains unchanged.

The *GT* or *grand total switch* in the on position accumulates totals.

**Ten-Key Touch System**

Striking the numbers 0 to 9 on a desktop calculator or numeric keypad on a computer without looking at the keyboard is called the *touch system*. Using the touch system develops both speed and accuracy.

The 4, 5, and 6 keys are called the *home row*. If the right hand is used for the key-board, the index finger is placed on the 4 key, the middle finger on the 5 key, and the ring finger on the 6 key. If the left hand is used, the ring finger is placed on the 4 key, the middle finger on the 5 key, and the index finger on the 6 key.

Place the fingers on the home row keys. Curve the fingers and keep the wrist straight. These keys may feel slightly concave or the 5 key may have a raised dot or bar. The differences in the home row allow the operator to recognize the home row by touch rather than by sight.

Maintain the position of the fingers on the home row. The finger used to strike the 4 key will also strike the 7 key and the 1 key. Stretch the finger up to reach the 7 and stretch the finger down to reach the 1 key. Visualize the position of these keys.

Again, place the fingers on the home row. Stretch the finger that strikes the 5 key up to reach the 8 key and down to reach the 2 key. Likewise, stretch the finger that strikes the 6 key up to strike the 9 key and down to strike the 3 key. This same finger will stretch down again to hit the decimal point.

If the right hand is used, the thumb will be used to strike the 0 and 00 keys and the little finger to strike the addition key. If the left hand is used, the little finger will be used to strike the 0 and 00 keys and the thumb to strike the addition key.

**Performing Mathematical Operations on Desktop Calculators**

Mathematical operations can be performed on any calculator both quickly and efficiently. The basic operations of addition, subtraction, multiplication, and division are used frequently on a calculator. Here is how these operations are completed on a typical desktop calculator.

**Addition** Each number to be added is called an *addend*. The answer to an addition problem is called the *sum*.

Addition is performed by entering an addend and striking the addition key (+). All numbers are entered on a calculator in the exact order they are given. To enter the number 4,375.68, strike the 4, 3, 7, 5, decimal, 6, and 8 keys in that order, and then strike the addition key. Commas are not entered. Continue in this manner until all addends have been entered. To obtain the sum, strike the total key on the calculator.

**Subtraction** The top number or first number of a subtraction problem is called the
**minuend.** The number to be subtracted from the minuend is called the *subtrahend.* The answer to a subtraction problem is called the *difference.*

Subtraction is performed by first entering the minuend and striking the addition key (+). The subtrahend is then entered, followed by the minus key (−), followed by the total key.

**Multiplication** The numbers being multiplied together are called *factors.* The answer to a multiplication problem is called the *product.*

Multiplication is performed by entering one factor, striking the multiplication key (×), entering the other factor, and then striking the equals key (=). The calculator will automatically multiply and give the product.

**Division** The number to be divided is called the *dividend.* The number the dividend will be divided by is called the *divisor.* The answer to a division problem is called the *quotient.*

Division is performed by entering the dividend and striking the division key (÷). The divisor is then entered, followed by the equals key (=). The calculator will automatically divide and give the quotient.

**Correcting Errors** If an error is made while using a calculator, several methods of correction may be used. If an incorrect number has been entered and the addition key or equals key has not yet been struck, strike the clear entry (CE) key one time. This key will clear only the last number that was entered. However, if the clear entry key is depressed more than one time, the entire problem will be cleared on some calculators. If an incorrect number has been entered and the addition key has been struck, strike the minus key one time only. This will automatically subtract the last number added, thus removing it from the total.

The computer has a keypad on the right side of the keyboard called the *numeric keypad.* Even though there are several styles of computer keyboards, there are two basic layouts for the numeric keypad, as shown below.

Most computers have a small light that indicates when the Num Lock key (above the 7 key) is on. When the Num Lock key is turned on, numbers are entered when the keys on the keypad are pressed. When Num Lock is not on, the arrow, Home, Page Up, Page Down, End, Insert, and Delete keys can be used. Enhanced keyboards allow you to keep the Num Lock key activated at all times.

The asterisk (*) on the computer is used for multiplication. The slash key (/) is used for division.

**Performing Mathematical Operations On Computers**

Calculations with a computer keypad are performed in much the same way as on a desktop calculator. However, after the + key is depressed, the display usually shows the accumulated total. Therefore, the total key is not found on the computer keypad. Some computer programs will not calculate the total until the Enter key is pressed.

Subtraction is performed differently on many computer keypads. The minuend is entered, followed by the minus (−) key. Then the subtrahend is entered. Pressing either the + key, the = key, or the Enter key will display the difference.

Multiplication and division are performed the same way as on a desktop calculator. Keep in mind that computers used the * for multiplication and / for division.
This arithmetic review will help you solve many of the end-of-chapter problems in this text as well as common arithmetic problems you may encounter in business.

**ESTIMATING SUMS AND DIFFERENCES**

In some situations, an estimate may be useful. Sometimes an exact answer is not needed, so you can estimate. Other times, estimation can be used to check mathematical calculations, especially when using a calculator.

Most people estimate by rounding numbers. Rounded numbers are easier to work with. Rounded numbers usually contain one or two non-zero digits followed by all zeros.

**Examples**

The U. S. Bureau of the Census estimated the 1997 population of Texas at 19,385,699.

- Round 19,385,699 to the nearest ten million. 19,385,699 → 20,000,000
  9 is greater than or equal to 5, so round up to 20,000,000

- Round 19,385,699 to the nearest million. 19,385,699 → 19,000,000
  3 is less than 5, round down to 19,000,000.

One new car has a list price of $15,209.50.

- Round $15,209.50 to the nearest dollar. $15,209.50 → $15,210
  5 is greater than or equal to 5, round up to $15,210.

- Estimate the answer to 24,432 + 15,000.
  
  **Option 1:** Round to the nearest ten thousand.
  24,432
  +15,000
  39,432

  **Option 2:** Round to the nearest thousand.
  24,000
  +15,000
  39,000

- Estimate the answer to $32.23 − $17.54.
  
  **Option 1:** Round to the nearest ten dollars.
  $32.23
  −17.54
  $14.69

  **Option 2:** Round to the nearest dollar.
  $30.00
  −18.00
  $12.00

- Estimate how much change you should get if you give the clerk $20 to pay for a bill of $6.98.
  
  **Option 1:**
  $20.00
  −6.98
  $13.02

  **Option 2:**
  $20.00
  −7.00
  $13.00
MULTIPLYING NUMBERS ENDING IN ZEROS

When you multiply numbers that have final zeros, you can use this shortcut:

Multiply the numbers by using only the digits that are not zeros. Then write as many final zeros in the product as there are zeros in the numbers being multiplied.

**Examples**

\[
\begin{align*}
200 \times 7 &= 1,400 \\
2 \text{ zeros} & \quad 2 \times 7 = 14 \\
2 \text{ zeros} & \\
40 \times 5,000 &= 200,000 \\
1 \text{ zero} & \quad 3 \text{ zeros} \\
4 \times 5 &= 20 & 4 \text{ zeros} \\
\end{align*}
\]

When multiplying larger numbers, use an imaginary line to separate zeros from the rest of the digits.

\[
\begin{align*}
36 \times 2,500 &= \\
36 & \quad 2,500 \\
180 & \quad 00 \quad 2 \text{ zeros} \\
72 & \quad \\
900 & \quad 00 \quad 90,000 \quad \text{Answer} \\
3,600 \times 25,000 &= \\
36 & \quad 00 \quad 2 \text{ zeros} \\
\times 25 & \quad 000 \\
180 & \quad 2 + 3 = 5 \text{ zeros} \\
72 & \quad \\
900 & \quad 00000 \quad 5 \text{ zeros} \\
90,000,000 & \quad \text{Answer} \\
\end{align*}
\]

ESTIMATING PRODUCTS

There are various ways to estimate the answer to a multiplication problem.

- Option 1: Round both numbers up. Estimate will be greater than the actual product.
- Option 2: Round both numbers down. Estimate will be less than the actual product.
- Option 3: Round each number to the nearest unit with one non-zero digit. The estimate will be close to the actual product.

**Examples**

Estimate 82,543 \(\times\) 653.

- Option 1: 90,000 \(\times\) 700 = 63,000,000
- Option 2: 80,000 \(\times\) 600 = 48,000,000
- Option 3: 80,000 \(\times\) 700 = 56,000,000

DIVIDING WHOLE NUMBERS

Division is the opposite of multiplication. Division is shown in several ways. To show that 18 divided by 3 is 6, you may use any of these forms:

\[
\begin{align*}
18 \div 3 &= 6 & \frac{18}{3} &= 6 & 3\overline{)18} \\
\end{align*}
\]

In each case, 18 is the dividend, 3 is the divisor, and 6 is the quotient.

\[
\text{dividend} \div \text{divisor} = \text{quotient}
\]

\[
\text{quotient} = \frac{\text{dividend}}{\text{divisor}}
\]

DIVIDING NUMBERS ENDING IN ZEROS

When you divide multiples of 10, there are several shortcuts you can use. Try either of the shortcuts discussed below:

- Write the numbers as a fraction. Cross out the same number of zeros in both the numerator and denominator of the fraction.
- Move the decimal point in the dividend to the left the same number of places as there are zeros in the dividend.

**Examples**

- \(1,000,000,000 \div 10,000 = \frac{1,000,000,000}{10,000} = 100,000\)
- \(1,000,000,000 \div 10,000 = \frac{10,000,000,000}{1,000} = 100,000\)
**ESTIMATING QUOTIENTS**

One way to estimate the answer to a division problem is to start by rounding the divisor to a number with one non-zero number followed by all zeros. Then round the dividend to a multiple of that rounded divisor.

**Example**

- Estimate $609 \div 19$.
  - Round 19 to 20 and 609 to 600.
  - $600 \div 20 = 30$
- Estimate $19,876,548 \div 650$.
  - 650 rounds up to 700.
  - Multiples of 7 are 7, 14, 21, 28, 35, and so on. Use the closest multiple, 21.
  - $21,000,000 \div 700 = \frac{2100000}{700} = \frac{210000}{7} = 30,000$

**MULTIPLYING DECIMALS**

When multiplying decimals, align the numbers at the right. Multiply as if you are multiplying whole numbers. To locate the decimal point in the answer, count all digits to the right of the decimal point in each number being multiplied and place the decimal point so there are that many digits after the decimal point in the answer.

**Examples**

- Multiply 7.46 by 3.2.
  - $7.46 \times 3.2 = 24.672$ (2 decimal places)
  - $1492 \times 1 = 1492$ (1 decimal place)
  - $2238 \times 3 = 6714$ (3 decimal places)
- Multiply 0.193 by 0.2.
  - $0.193 \times 0.2 = 0.0386$ (3 decimal places)

If needed to get enough decimal places, add a zero before the numeric answer but after the decimal point. Remember that the zero before the decimal point shows that there are no ones in the product. The answer is less than one.

Estimate to check your answer.

- $0.2 \times 0.2 = 0.04$
- 0.04 is close to 0.0386, so the answer is reasonable.

**ADDING AND SUBTRACTING DECIMALS**

When adding and subtracting decimals, align the decimal points. Then add or subtract as for whole numbers. Place the decimal point in the answer directly below where it is located in the computation. A number like 532 can also be written as 532. or 532.0. When writing decimals less than one, a zero if placed before the decimal point to show that there are no ones.

**Examples**

- Find the sum of 33.67, 72.84, 0.75, and 43.34.
  - $33.67 + 72.84 + 0.75 + 43.34 = 150.60$
- Find the sum of 320.5471, 1.4, and 82.352.
  - $320.5471 + 1.4 + 82.352 = 404.2991$
MULTIPLYING
BY POWERS OF 10
Numbers like 100,000,000, 10,000, 100, 0.1, 0.01, and 0.00001 are powers of 10. To multiply by these, simply move the decimal point in the number being multiplied.

When multiplying by a power of 10 greater than one, move the decimal point to the right. The answer is larger than the number you started with.

When multiplying by a power of 10 less than one, move the decimal point to the left. The answer is smaller than the number you started with.

Examples
- Multiply 25,397 by ten thousand.
  25,397 × 10,000 = 253,970,000
  Think: 25397.0000.
- Multiply 0.078 by one hundred.
  0.078 × 100 = 7.8
  Think: 0.0078.
- Multiply 192,536 by one ten-thousandth.
  192,536 × 0.0001 = 19.2536
  Think: 19.2536.
- Multiply 0.293 by one hundredth.
  0.293 × 0.01 = 0.00293
  Think: 0.000293

SHORTCUTS WHEN MULTIPLYING WITH MONEY
Businesses price items at amounts such as 49¢, $5.98, or $99.95. A price of $99.95 seems less to the buyer than an even $100. When finding the cost of several of such items, you can use a mathematical shortcut.

Examples
- Find the cost of 27 items at 98¢ each.
  normal multiplication  27 × 98¢ = 686
  Think: 98¢ × 27 = $26.46
  Alternate Shortcut: 101 = 100 + 1
  (100 × 98¢) + (1 × 98¢) = $999 + $9.99 = $1,008.99

MULTIPLYING A WHOLE NUMBER BY A FRACTION
To multiply a whole number by a fraction, multiply the whole number by the numerator (top number) and then divide that answer by the denominator (bottom number).

Examples
- $180 × \frac{2}{3} = \frac{180 × 2}{3} = \frac{360}{3} = 120$
- $500 × \frac{3}{4} = \frac{500 × 3}{4} = \frac{1500}{4} = 375$
- $768 × \frac{1}{8} = \frac{768 × 1}{8} = \frac{768}{8} = 96$
- $90 × \frac{4}{5} = \frac{90 × 4}{5} = \frac{360}{5} = 72$

Simplifying Fractions
When working with fractions, you can simplify the fractions by dividing the numerator and the denominator by a common factor (a number that will divide into both numbers evenly). Division by such common factors is called canceling or cancellation.
Examples

- Simplify \( \frac{10}{12} \).  
  **Think:** 2 is a factor of both 10 and 12.

\[
\begin{align*}
\frac{10}{12} & = \frac{5}{6} \\
5 & \rightarrow 10 \div 2 = 5 \\
6 & \rightarrow 12 \div 2 = 6
\end{align*}
\]

- Simplify \( \frac{75}{100} \).  
  **Think:** Use 25 as a common factor.

\[
\begin{align*}
\frac{75}{100} & = \frac{3}{4} \\
75 & \div 25 = 3 \\
100 & \div 25 = 4
\end{align*}
\]

- Simplify \( \frac{280}{60} \).  
  **Think:** Use 20 as a common factor.

\[
\begin{align*}
\frac{280}{60} & = \frac{14}{3} \\
280 & \div 20 = 14 \\
60 & \div 20 = 3
\end{align*}
\]

Using Fractional Parts of $1.00 in Multiplying Mentally

While goods and services may be priced at any figure, prices are frequently expressed in fractional parts of $1, $10, or $100. For instance, 2 items for $1 is the same as \( \frac{1}{2} \) of 100¢, or 50¢ per item, and 3 items for $10 is the same as \( \frac{3}{10} \) of $10, or $3.33 \( \frac{1}{3} \) per item.

You can also use fractional parts of $1.00 to find the cost of multiple items mentally.

- 24 items selling for $1.00 would cost $24.00
- 24 items at 50¢ each = \( \frac{1}{2} \) of $24 or $12.00
- 24 items at 25¢ each = \( \frac{1}{4} \) of $24 or $6.00
- 24 items at 33 \( \frac{1}{3} \)¢ each = \( \frac{1}{3} \) of $24 or $8

Many similar calculations can be made mentally. While there are many fractional parts of $1.00, below is a chart of those most commonly used.

<table>
<thead>
<tr>
<th>Fraction</th>
<th>Part of $1.00</th>
</tr>
</thead>
<tbody>
<tr>
<td>( \frac{1}{8} )</td>
<td>$0.12 ( \frac{1}{2} )</td>
</tr>
<tr>
<td>( \frac{1}{6} )</td>
<td>$0.16 ( \frac{2}{3} )</td>
</tr>
<tr>
<td>( \frac{1}{5} )</td>
<td>$0.20</td>
</tr>
<tr>
<td>( \frac{1}{4} )</td>
<td>$0.25</td>
</tr>
<tr>
<td>( \frac{1}{3} )</td>
<td>$0.33 ( \frac{1}{3} )</td>
</tr>
<tr>
<td>( \frac{2}{8} )</td>
<td>$0.37 ( \frac{1}{2} )</td>
</tr>
<tr>
<td>( \frac{2}{5} )</td>
<td>$0.40</td>
</tr>
<tr>
<td>( \frac{3}{8} )</td>
<td>$0.50</td>
</tr>
<tr>
<td>( \frac{3}{10} )</td>
<td>$0.60</td>
</tr>
<tr>
<td>( \frac{5}{8} )</td>
<td>$0.62 ( \frac{1}{2} )</td>
</tr>
<tr>
<td>( \frac{2}{3} )</td>
<td>$0.66 ( \frac{2}{3} )</td>
</tr>
<tr>
<td>( \frac{3}{4} )</td>
<td>$0.75</td>
</tr>
<tr>
<td>( \frac{4}{5} )</td>
<td>$0.80</td>
</tr>
<tr>
<td>( \frac{5}{6} )</td>
<td>$0.83 ( \frac{1}{3} )</td>
</tr>
<tr>
<td>( \frac{7}{8} )</td>
<td>$0.87 ( \frac{1}{2} )</td>
</tr>
</tbody>
</table>

Examples

- Find the cost of 16 items at \( 12 \frac{1}{2} \)¢ each.  
  **Think:** \( 12 \frac{1}{2} \)¢ = \( \frac{1}{8} \) of $1

\[
16 \times \frac{1}{8} = 2
\]

16 items at \( 12 \frac{1}{2} \)¢ each will cost $2.

- Find the cost of 33 items at 25¢ each.  
  **Think:** 25¢ = \( \frac{1}{4} \) of $1

\[
33 \times \frac{1}{4} = \frac{33}{4}, \text{ or } 8 \frac{1}{4}
\]

33 items at 25¢ each will cost $8 \( \frac{1}{4} \), or $8.25.
Find the cost of 48 items at 75¢ each.

**Think:** 75¢ = \( \frac{3}{4} \) of $1

\[
48 \times \frac{3}{4} = \frac{48 \times 3}{4} = \frac{12 \times 3}{1} = 36 = 36
\]

48 items at 75¢ each is $36.

Find the cost of 34 items at 62\(\frac{1}{2}\)¢ each.

**Think:** 62\(\frac{1}{2}\)¢ = \(\frac{5}{8}\) of $1

\[
34 \times \frac{5}{8} = \frac{34 \times 5}{8} = \frac{17 \times 5}{4} = \frac{85}{4} = 21 \frac{1}{4}
\]

34 items at 62\(\frac{1}{2}\)¢ each is $21\frac{1}{4}$, or $21.25.

**Fractional Parts of Other Amounts**

You can use the table on this page to find fractional parts of multiples of 10.

**Examples**

- **Find** \(\frac{5}{6}\) **of** $1,000.

  \[
  \frac{5}{6} \text{ of } 1000 = 1000 \times \frac{5}{6} = 100 \times 0.83 \frac{1}{3} = 83 \frac{1}{3}
  \]

  So, \(\frac{5}{6}\) **of** $1,000 is $833.33.

  \(\frac{1}{3}\) dollar = $0.33\frac{1}{3}$, which is $0.33 when rounded to the nearest cent.

- **Find** \(\frac{3}{4}\) **of** $100.

  \[
  \frac{3}{4} \text{ of } 100 = 100 \times \frac{3}{4} = 100 \times 0.75 = 75
  \]

  So, \(\frac{3}{4}\) **of** $100 is $75.

- **Find** \(\frac{7}{8}\) **of** $10.

  \[
  \frac{7}{8} \text{ of } 10 = 10 \times \frac{7}{8} = 10 \times 0.875 = 8.75
  \]

  So, \(\frac{7}{8}\) **of** $10 is $8.75.

**Dividing Decimals**

Division involving decimals is completed like division of whole numbers, except for dealing with the decimal point.

When you divide a decimal by a whole number, you divide as for whole numbers and place the decimal point directly above the location of the decimal point in the dividend.

**Examples**

- **Divide** 12.944 by 8.

  \[
  \begin{align*}
  1.618 \div 8 &= 1.618 \times \frac{1}{8} \\
  &= 0.20225 \\
  &= 0.00375 \\
  \end{align*}
  \]

  \[
  \text{Check: } 0.20225 	imes 8 = 1.618 \checkmark
  \]

- **Divide** 37 by 4.

  \[
  \begin{align*}
  9.25 \div 4 &= 9.25 \times \frac{1}{4} \\
  &= 2.3125 \\
  &= 0.578125 \\
  \end{align*}
  \]

  \[
  \text{Check: } 2.3125 \times 4 = 9.25 \checkmark
  \]
To divide by a decimal, move the decimal point to the right the same number of places in both the divisor and the dividend so you are dividing by a whole number.

**Examples**

- Divide 12.944 by 0.8.

  \[ \begin{array}{c}
  \text{Think: } 0.8 \text{ has one decimal place, move the decimal points in the divisor and the dividend right one place.} \\
  12.944 \\
  0.8 \\
  \hline
  61.8 \\
  49 \\
  48 \\
  14 \\
  8 \\
  64 \\
  64 \\
  0
  \end{array} \]

- Divide 37 by 0.004.

  \[ \begin{array}{c}
  \text{Add zeros as needed.} \\
  37 \div 0.004 = 9250. \\
  9 \\
  8 \\
  20 \\
  20 \\
  0
  \end{array} \]

**Remember:** Estimation can be used to check that your answer is reasonable and that you have correctly located the decimal point in the answer.
Determining Percentages and Interest in Business

Finding percentages and calculating interest are frequent functions in business. Every career in business demands some knowledge of percentages and interest. The well-prepared business person is comfortable with percentages and interest.

**MEANING OF PERCENT**
Percent is derived from two Latin words, “per centum,” meaning “by the hundred.” You can express a percent as a common fraction or a decimal fraction. When the percent involves a fraction, like \( \frac{7}{4}\% \), change the mixed number to a decimal and move the decimal point two places to the left.

\[
7 \frac{1}{4}\% = 7.25\% = 0.725
\]

**Examples**
- Write 19\% as a fraction and a decimal.
  
  Percent means *per one hundred*, so write it as a fraction with a denominator of 100.
  
  \[
  19\% = \frac{19}{100} = 0.19
  \]
- Write 0.98 as a fraction and a percent.
  
  \[
  0.98 = \frac{98}{100} = 98\%
  \]

- Write \( \frac{3}{100} \) as a decimal and a percent.
  
  \[
  \frac{3}{100} = 0.03 = 3\%
  \]
- Write \( 8 \frac{1}{2}\% \) as a decimal and a fraction.
  
  \[
  8 \frac{1}{2}\% = 8.5\% = 0.085 = \frac{85}{1000}
  \]
  
  Notice that 0.085 is 85 *thousandths*, so the fraction has a denominator of 1000.

**FINDING A PERCENT OF A NUMBER**
To find the percent of a number, change the percent to a fraction or decimal and multiply. Using a calculator simplifies the process.

**Example**
- Find 18\% of 117,334.

  With fractions:
  
  \[
  117334 \times \frac{18}{100} = \frac{117334 \times 18}{100} = \frac{2112012}{100} = 21,120.12
  \]
Find 18% of 117,334.
With decimals:

\[
117,334 	imes 0.18 = 21,120.12
\]

Find 10% of 359.

\[
359 	imes 0.10 = 35.9
\]

CALCULATING SIMPLE INTEREST

Interest is money paid for the privilege of using someone else’s money. Interest is always expressed as a percent. The principal is the amount of money borrowed. Simple interest \((I)\) is calculated by multiplying the principal \((P)\) times the annual interest rate \((R)\) times the length of time in years \((T)\). The formula is written as:

\[
I = P \times R \times T
\]

Examples

- Find the amount of simple interest due on $400 borrowed for 2 years at 8%.
  \[
  I = 400 \times 0.08 \times 2 = 64
  \]

- Find the amount of simple interest due on $600 borrowed for 1 month at 18%.
  
  Think: 1 month is \(\frac{1}{12}\) of a year.

  \[
  I = 600 \times 0.18 \times \frac{1}{12} = 9
  \]

- Find the amount of simple interest due on $3,000 borrowed for 6 months at \(\frac{3}{4}\)%.
  \[
  I = 3,000 \times 0.0975 \times \frac{6}{12} = 146.25
  \]

COMPOUND INTEREST

With the advances in the use of computer, compound interest is more common than simple interest. For example, a credit card may say that it charges 1.5% interest per month. It then seems that you are paying \(12 \times 1.5\)% or 18% interest per year. However, in reality you are charged more than 18% interest per year because you are paying interest on interest.

Example

- Suppose that you owe $100 on your credit card and do not make any payments for one year. Assuming there are no late fees, your balance at the end of each month would look as shown in the table on page 625. When the interest is calculated, all amounts are rounded up to the next cent.

<table>
<thead>
<tr>
<th>Month</th>
<th>Beginning Balance</th>
<th>Interest (1.5% per month)</th>
<th>Ending Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan.</td>
<td>$100</td>
<td>$1.50</td>
<td>$101.50</td>
</tr>
<tr>
<td>Feb.</td>
<td>$101.50</td>
<td>$1.53</td>
<td>$103.03</td>
</tr>
<tr>
<td>Mar.</td>
<td>$103.03</td>
<td>$1.55</td>
<td>$104.58</td>
</tr>
<tr>
<td>Apr.</td>
<td>$104.58</td>
<td>$1.57</td>
<td>$106.15</td>
</tr>
<tr>
<td>May</td>
<td>$106.15</td>
<td>$1.60</td>
<td>$107.75</td>
</tr>
<tr>
<td>June</td>
<td>$107.75</td>
<td>$1.62</td>
<td>$109.37</td>
</tr>
<tr>
<td>July</td>
<td>$109.37</td>
<td>$1.65</td>
<td>$111.02</td>
</tr>
<tr>
<td>Aug.</td>
<td>$111.02</td>
<td>$1.67</td>
<td>$112.69</td>
</tr>
<tr>
<td>Sept.</td>
<td>$112.69</td>
<td>$1.70</td>
<td>$114.39</td>
</tr>
<tr>
<td>Oct.</td>
<td>$114.39</td>
<td>$1.72</td>
<td>$116.11</td>
</tr>
<tr>
<td>Nov.</td>
<td>$116.11</td>
<td>$1.75</td>
<td>$117.86</td>
</tr>
<tr>
<td>Dec.</td>
<td>$117.86</td>
<td>$1.77</td>
<td>$119.63</td>
</tr>
</tbody>
</table>

So in 12 months you have paid $19.63 in interest on $100, or 19.63%, not 18% interest.

FINDING WHAT PERCENT A NUMBER IS OF ANOTHER

To find what percent a number is of another, divide the one number (the part) by the other number (the whole). Then show the result as a percent.

Example

- 50 is what percent of 200?

\[
0.25 \div 200 = 0.00125 \times 100 = 12.5\%
\]

50 is 25% of 200.
Using Measurements in Business

The metric system of measurement is used in business by most nations in the world. Because of our great amount of trade with other countries, the United States has taken some steps toward conversion to the metric system. Some U.S. businesses and industries have already made the change, and you should become familiar with the metric system.

There are some things about the metric system that may already be familiar to you. For example, if you have been to a track meet or swimming meet or have seen one on television, you know that distances can be measured in meters, not just in feet, yards, or miles. Food is often labeled to show amounts in grams as well as pounds or ounces. Meters, kilometers, and grams are examples of metric units of measurement.

**BASIC METRIC UNITS**
The basic metric units are the meter (length), the liter (capacity), and the gram (mass or weight). All measurements can be expressed in terms of these three basic units. However, prefixes are used with the basic units to avoid dealing with very large and very small numbers. The most common prefixes used in the metric system are:

- **kilo-** one thousand times
- **centi-** one one-hundredth of
- **milli-** one one-thousandth of

Look at the charts below. The same prefixes are used for length, capacity, and mass or weight.

**Length**
- 1 kilometer = 1000 meters
- 1 meter = 100 centimeters
- 1 meter = 1000 millimeters
- 1 centimeter = 10 millimeters
- 1 centimeter = 0.01 meter
- 1 millimeter = 0.001 meter

**Capacity**
- 1 kiloliter = 1000 liters
- 1 liter = 100 centiliters
- 1 liter = 1000 milliliters
- 1 centiliter = 10 milliliters
- 1 centiliter = 0.01 liter
- 1 milliliter = 0.001 liter

**Mass (Weight)**
- 1 kilogram = 1000 grams
- 1 gram = 100 centigrams
- 1 gram = 1000 milligrams
- 1 centigram = 10 milligrams
- 1 centigram = 0.01 gram
- 1 milligram = 0.001 gram

The abbreviations, or symbols, for metric measurements are also uniform, changing only to show whether you are measuring length, capacity, or mass.
CONVERTING UNITS WITHIN THE METRIC SYSTEM

Using the tables above, you can see that one kilometer is 1000 times as long as a meter and that one millimeter is one-thousandth of a meter. Since the relationships between the prefixes are multiples of 10, you can change from one unit to another by multiplying by a power of ten, which can be done by moving the decimal point.

Examples

- Change 0.36 meters to centimeters.
  
  **Think:** 1 meter = 100 centimeters
  
  To get from 1 to 100, move the decimal point to the right 2 spaces.
  
  0.36
  
  So 0.36 meters = 36 centimeters

- Change 5000 grams to kilograms.
  
  **Think:** 1000 grams = 1 kilogram
  
  To get from 1000 to 1, move the decimal point to the left 3 spaces.
  
  5.000
  
  So 5000 grams = 5 kilograms

- Change 4.5 liters to milliliters.
  
  **Think:** 1 liter = 1000 milliliters
  
  To get from 1 to 1000, move the decimal point to the right 3 spaces.
  
  4.500
  
  Notice how zeros are added so the decimal can be moved the needed number of spaces to the right.
  
  So 4.5 liters = 4500 milliliters

CUSTOMARY MEASUREMENT

In the United States feet, pounds, and gallons are still common units of measure. Below is a list of common customary measurements and their equivalents.

<table>
<thead>
<tr>
<th>Length</th>
<th>Capacity</th>
<th>Mass (Weight)</th>
</tr>
</thead>
<tbody>
<tr>
<td>kilometer → km</td>
<td>kiloliter → kL</td>
<td>kilogram → kg</td>
</tr>
<tr>
<td>meter → m</td>
<td>liter → L</td>
<td>gram → g</td>
</tr>
<tr>
<td>centimeter → cm</td>
<td>centiliter → cL</td>
<td>centigram → cg</td>
</tr>
<tr>
<td>millimeter → mm</td>
<td>milliliter → mL</td>
<td>milligram → mg</td>
</tr>
</tbody>
</table>

MEASURING TEMPERATURE

Thermometers that measure temperature are marked in degrees Celsius (°C) or in degrees Fahrenheit (°F). The Celsius scale is a metric scale. The Fahrenheit scale is nonmetric.

<table>
<thead>
<tr>
<th>Metric</th>
<th>Event</th>
<th>Nonmetric</th>
</tr>
</thead>
<tbody>
<tr>
<td>100°C</td>
<td>Water boils</td>
<td>212°F</td>
</tr>
<tr>
<td>37°C</td>
<td>Normal body temperature</td>
<td>98.6°F</td>
</tr>
<tr>
<td>0°C</td>
<td>Water freezes</td>
<td>32°F</td>
</tr>
</tbody>
</table>
CONVERTING BETWEEN SYSTEMS

Once in a while it may be necessary to convert from the metric system to the customary system or vice versa. You can use these charts when you need to change metric measurements to customary or vice versa.

### Length/Distance

<table>
<thead>
<tr>
<th>When you know:</th>
<th>You can find:</th>
<th>If you multiply by:</th>
</tr>
</thead>
<tbody>
<tr>
<td>inches</td>
<td>millimeters</td>
<td>25.40</td>
</tr>
<tr>
<td>inches</td>
<td>centimeters</td>
<td>2.54</td>
</tr>
<tr>
<td>feet</td>
<td>meters</td>
<td>0.305</td>
</tr>
<tr>
<td>yards</td>
<td>meters</td>
<td>0.91</td>
</tr>
<tr>
<td>miles</td>
<td>kilometers</td>
<td>0.305</td>
</tr>
<tr>
<td>millimeters</td>
<td>inches</td>
<td>0.04</td>
</tr>
<tr>
<td>centimeters</td>
<td>inches</td>
<td>0.39</td>
</tr>
<tr>
<td>meters</td>
<td>inches</td>
<td>39.37</td>
</tr>
<tr>
<td>meters</td>
<td>feet</td>
<td>3.28</td>
</tr>
<tr>
<td>meters</td>
<td>yards</td>
<td>1.09</td>
</tr>
<tr>
<td>kilometers</td>
<td>miles</td>
<td>0.62</td>
</tr>
</tbody>
</table>

### Capacity/Volume

<table>
<thead>
<tr>
<th>When you know:</th>
<th>You can find:</th>
<th>If you multiply by:</th>
</tr>
</thead>
<tbody>
<tr>
<td>pints</td>
<td>liters</td>
<td>0.47</td>
</tr>
<tr>
<td>quarts</td>
<td>liters</td>
<td>0.95</td>
</tr>
<tr>
<td>gallons</td>
<td>liters</td>
<td>3.78</td>
</tr>
<tr>
<td>liters</td>
<td>pints</td>
<td>2.11</td>
</tr>
<tr>
<td>liters</td>
<td>quarts</td>
<td>1.06</td>
</tr>
<tr>
<td>liters</td>
<td>gallons</td>
<td>0.26</td>
</tr>
</tbody>
</table>

### Temperature

<table>
<thead>
<tr>
<th>When you know:</th>
<th>You can find</th>
</tr>
</thead>
<tbody>
<tr>
<td>°F (degrees Fahrenheit)</td>
<td>°C (degrees Celsius)</td>
</tr>
<tr>
<td>subtract 32, multiply by 5, then divide by 9.</td>
<td></td>
</tr>
<tr>
<td>°C (degrees Celsius)</td>
<td>°F (degrees Fahrenheit)</td>
</tr>
<tr>
<td>multiply by 9, divide by 5, then add 32.</td>
<td></td>
</tr>
</tbody>
</table>

### Examples

- **You are in a 440-yard race. How many meters long is the race?**
  
  To change from yards to meters, multiply by 0.91.
  
  \[440 \times 0.91 = 400.4\]
  
  The race is 400.4 meters long.

- **A store shelf has a weight limit of 250 kilograms. What is that limit in pounds?**
  
  To change kilograms to pounds, multiply by 2.20.
  
  \[250 \times 2.20 = 550\]
  
  The weight limit is 550 pounds.

- **It is 10°C outside. What is the temperature in degrees Fahrenheit?**
  
  To change from °C to °F, multiply by 9, divide by 5, then add 32.
  
  \[10 \times 9 = 90; 90 \div 5 = 18; 18 + 32 = 50\]
  
  The temperature is 50°F.

- **It is 95°F outside. What is the temperature in degrees Celsius?**
  
  To change from °F to °C, subtract 32, multiply by 5, then divide by 9.
  
  \[95 - 32 = 63; 63 \times 5 = 315; 315 \div 9 = 35\]
  
  The temperature is 35°C.
A

Ability the quality of being able to perform a mental or physical task.

Absolute advantage when a country can produce a good or service at a lower cost than other countries.

Accountability taking responsibility for the results achieved.

Accounts payable record a financial document that identifies the companies from which credit purchases were made and the amount purchased, paid, and owed.

Accounts receivable record a financial document that identifies customers that made purchases using credit and the status of each account.

Adjustable-rate mortgage (ARM) a mortgage in which the interest rate is raised or lowered from time to time depending on the current interest rate being charged by lenders.

Advertising any paid form of communication through mass media directed at identified consumers to provide information and influence their actions.

Agricultural products crops and animals grown by farmers.

AI. See Artificial intelligence

Allowance the amount of money you plan to use for a certain budget category.

All-risk policy. See Special form

Annual percentage rate (APR) the percentage rate equal to the total amount of interest that a $100 deposit would earn based on a 365-day period.

Annuity an amount of money an insurance company pays (usually monthly) to a person who has previously deposited money with the company.

Antitrust laws laws that prevent unfair business practices such as false advertising, deceptive pricing, and misleading labeling.

Application form a form asking for information related to employment. It gives the employer standard information about each job applicant.

Application software programs that perform specific tasks such as word processing, database management, or accounting.

Applied research marketing research that studies existing products to develop design improvements or new product uses.

Appraiser someone trained to estimate the value of property and who can give an official report on the value.

Appreciation a general increase in the value of property that occurs over time.

APR. See Annual percentage rate

Arbitration a third-party action resulting in a decision that is legally binding.

ARM. See Adjustable-rate mortgage

Articles of incorporation a written legal document that defines ownership and operating procedures and conditions for the business.

Artificial intelligence (AI) software that enables computers to reason, learn, and make decisions. It uses logical methods similar to the methods of human use.

Assessed value the amount that your local government determines your property to be worth for tax purposes.

Asset record a financial document used to name the buildings and equipment owned by the business, their original and current value, and the amount owed if money was borrowed to purchase the assets.

Assets what a company owns.

Assigned risk plan a plan in which every automobile insurance company in the state is assigned a certain number of high-risk drivers, based on the amount of insurance each company sells.

Audio output processing results involving music and broadcast clips as well as presentations for training seminars.
Authority the right to make decisions about how responsibilities should be accomplished.

Automatic bill payment requires a bank customer to authorize preset amounts of monthly expenses. The bank deducts the payment from your account and transfers them to the appropriate companies.

Balance of payments the difference between the amount of money that comes into a country and the amount that goes out of it.

Balance of trade the difference between a country’s total exports and total imports.

Balance sheet a report that lists a company’s assets, liabilities, owner’s equity, and net profit.

Bank money order a form sold by a bank stating that money is to be paid to a specific person or business.

Bank reconciliation the document created to show how the two balances (your own record of your checking account and the bank’s record of your account) were brought into agreement.

Bank statement a report on the status of a bank account.

Bankruptcy the legal process of reducing or eliminating an amount owed.

Base-plan incentive a compensation system which combines a wage or salary with an additional amount based on the employee’s performance.

Basic economic problem the mismatch of unlimited wants and needs and limited economic resources.

Basic form a form of a homeowners policy that insures property against the basic perils.

Basic health coverage protection provided by regular medical, hospital, and surgical insurance.

Basic product the simplest form of a product. It is not unique and is usually available from several companies.

Behavioral interviewing an interview that evaluates an applicant’s on-the-job potential. Questions typically begin with “describe” or “tell me about …”

Benchmark the best practices among all competitors.

Beneficiary the person named in the policy to receive the insurance benefits.

Benefits compensation in forms other than direct payment.

Blank endorsement an endorsement that consists of only the endorser’s name.

Blue-collar workers workers who are employed in factories, on construction sites, and on farms.

Board of directors the people who make the major policy and financial decisions for the business.

Bodily injury liability insurance that protects a driver from claims resulting from injuries or deaths for which the insured is at fault.

Bond a certificate representing a promise to pay a definite amount of money at a stated interest rate on a specified due date.

Brand a name given to a product or service to distinguish it from other similar and competitive items.

Brand name a unique identification for a company’s products.

Broad form a form of a homeowners policy that insures property against 18 different risks.

Budget detailed plans for the financial needs of individuals, families, and businesses.

Budget charge account a credit agreement that requires a customer to make payments of a fixed amount over several months.

Budget deficit occurs when a government spends more than it takes in.

Budget surplus occurs when a government spends less than it takes in.

Budget variance any difference between actual spending and budgeted amounts.

Business consumers persons, companies, and organizations that buy products for the operation of a business, for incorporation into other products and services, or for resale to their customers.

Business cycle a movement of the economy from one condition to another and back again. It has
four cycles including prosperity, recession, depression, and recovery.

**Business ethics** rules about how businesses and their employees ought to behave.

**Business interruption insurance** compensation for ongoing business expenses that occur if a business has a temporary shutdown due to a fire, flood, or other major problem.

**Business plan** a written description of the business idea and how it will be carried out, including all major business activities.

**Buying motives** the reasons consumers decide what products and services to purchase.

**C**

**Cafeteria plan** employee benefit program that allocates a certain amount of money to each employee that can be spent on benefits.

**CAI.** See **Computer-assisted instruction**

**Capacity** refers to a person’s ability to pay a debt when it is due.

**Capital** the value of the borrower’s possessions, including money and the property owned.

**Capital gain** the result of an investment that is sold for less than its original cost.

**Capital loss** the result of a stock increase in value and then being sold for more than its original cost.

**Capital projects** spending by businesses for items such as land, buildings, equipment, and new products.

**Capital resources** the products and money used to produce goods and services.

**Capitalism** the private ownership of resources by individuals, rather than by the government.

**Career** a goal for work that is fulfilled through an occupation or series of occupations.

**Career planning** the process of studying careers, assessing yourself in terms of careers, and making decisions about a future career.

**Career portfolio** tangible evidence of your ability and skills.

**Cash budget** an estimate of the actual money received and paid out for a specific period of time.

**Cash flow statement** a report of net wages and other income along with spending for a period, such as for a month.

**Cash inflow** the money you have available to spend as a result of working or from other income, such as interest earned on your savings.

**Cash machine** an automated teller machine (ATM) that allows many bank services.

**Cash outflow** amounts spent for food, clothing, transportation, and other living costs.

**Cash record** a financial document that lists all cash received and spent by the business.

**Cash value** the amount of money that the insurance company will pay if the policyholder decides the insurance is no longer needed.

**Cashier’s check** a check that a bank draws on its own funds. It costs the amount of the check plus a service fee.

**Central processing unit (CPU)** the control center of the computer.

**Certificate of deposit rate** the rate for six-month time deposits at savings institutions.

**Certified check** a personal check for which a bank has guaranteed payment.

**Channel members** the businesses that take part in a channel of distribution.

**Channel of distribution** the route a product follows and the businesses involved in moving a product from the producer to the final consumer.

**Character** refers to a person’s honesty and willingness to pay a debt when it is due.

**Check cards.** See **Debit cards**

**Check register** a separate book, usually the same size as the checkbook, for recording account activities.

**Check stub** a form attached to the check by a perforated line.

**Claim** a policyholder’s request for payment for a loss that the insurance policy covers.

**Class action suit** a legal action by one party on behalf of a group of people who all have the same grievance.
Clearance sale  sales used to clear merchandise that stores no longer wish to carry.

Clearing  refers to the paying of checks among different banks in different cities.

Co-branded accounts  company credit cards that are affiliated with bank card companies.

Code of ethics  a set of rules for guiding the action of employees or members of an organization.

Coinsurance clause  the sharing of expenses by the policyholder and the insurance company.

Collaboration software (groupware)  software that provides real-time communications capabilities by voice, text, and video. It also allows team members working at their own computers from anywhere in the world to view the same documents on their computer screens and work on them as a team.

Collateral  property that is used as security, giving the lender the right to sell this property to get back the amount of the loan if it is not repaid.

Collectibles  items of personal interest to collectors that can increase in value in the future.

Collective bargaining  formal negotiation between members of unions and management to resolve issues.

Collision coverage  insurance that protects a car owner against financial loss resulting from a collision or rollover.

Command economy  an economy in which resources are owned and controlled by the government.

Commercial bank  the most common way for a bank to be organized. They offer checking accounts, provide savings accounts, make loans to individual and to businesses, and offer other services.

Commercial property insurance  coverage of property losses resulting from fire, storms, accidents, theft, and vandalism.

Commission  the amount of money an employee is paid based on a percentage of sales for which he or she is responsible; the fee stockbrokers charge for their services.

Commodities  grain, livestock, and precious metals.

Common market (economic community)  a market in which members do away with duties and other trade barriers.

Common stock  stock that represents general ownership in a corporation and a right to share in its profits.

Communication channel  the way the information being communicated from a sender is being transmitted to the receiver.

Comparative advantage  a situation in which a country specializes in the production of a good or service at which it is relatively more efficient.

Compensation  the amount of money paid to an employee for work performed, including salary and wages.

Compensation and benefits  planning and managing payroll, personnel records, and benefits programs.

Competition  the rivalry among businesses to sell their goods and services.

Competitors  businesses offering very similar products to the same customers.

Compound interest  interest computed on the amount saved plus the interest previously earned.

Comprehensive coverage  insurance that protects the insured against almost all damage losses except those caused from a collision or rollover.

Comprehensive medical policy  a policy that combines the features of hospital, surgical, regular, and major medical insurance.

Computer language  a system of letters, words, numbers, and symbols used to communicate with a computer.

Computer literacy  the ability to use computers to process information or solve problems.

Computer network  a group of computers such as those in businesses and schools that are linked together so users can share hardware, software, and data.

Computer system  the configuration that includes all functional components of a computer, including an input device, processing unit, memory and storage, and an output device.
Computer virus  a program code hidden in a system that can later do damage to software or stored data.

Computer-aided design  the use of technology to create product styles and designs.

Computer-assisted instruction (CAI)  the use of computers to help people learn or improve skills at their own pace.

Conditions of work  clauses related to employee well-being while on the job that are often included in labor contracts and company policy manuals.

Condominium (condo)  an individually owned housing unit in an apartment-like complex.

Conflict of interest  occurs when an action by a company or individual results in an unfair benefit.

Conservation  saving scarce natural resources.

Consumer  a person who buys and uses goods and services.

Consumer Credit Reporting Act, The  a law that places the burden of proof for accurate credit information on the credit reporting agency rather than on the debtor.

Consumer decision-making  the specific sequence of steps consumers follow to make a purchase.

Consumer movement  to fight against unfair business practices, consumers united to demand fair treatment from businesses.

Contingent worker  one who has no explicit or implicit contract for long-term employment.

Continuous Process Improvement (CPI)  a way to make sure manufacturing processes are completed as effectively as possible. It increases the quality of work by reducing errors, inefficiencies, and waste. Rather than waiting for a problem to occur, processes are continuously reviewed with the goal of finding ways to improve them.

Continuous processing  changing the form of raw materials into a specific product useable for consumption or for further manufacturing by constantly moving the materials through specially designed equipment.

Contract  an agreement to exchange goods or services for something of value, usually money.

Controllable risk  a risk that you can reduce or eliminate by actions you take.

Controlling  determines to what extent the business is accomplishing the goals it set out to reach in the planning stage.

Convenience stores  small stores that emphasize the sale of food items, an accessible location, and long operating hours.

Cooperative  a business formed to market products produced by members or to purchase products needed by the members. It is owned by members, serves their needs, and is managed in their interest.

Copyright  protection of the creative work of authors, composers, and artists. Protection lasts for the life of the person receiving the copyright and extends for 50 years after the person’s death.

Core values  the important principles that guide decisions and actions in the company.

Corporate bond rate  the cost of borrowing for large U.S. corporations.

Corporate bonds  bonds issued by corporations.

Corporate bylaws  operating procedures for the corporation.

Corporation  a separate legal entity formed by documents filed with your state. It is owned by one or more shareholders and managed by a board of directors.

Cosigner  the party responsible for payment of a note if the borrower does not pay as promised.

Cost containment  keeping costs down.

Counterfeiting  illegal uses of intellectual property, patents, trademarks, and copyrights.

Cover letter  a letter expressing your interest in a specific job.

Credit  the privilege of using someone else’s money for a period of time.

Credit application  a form on which you provide information needed by a lender to make a decision about granting credit.

Credit bureau  a company that gathers information on credit users. It sells that information to businesses offering credit.
Credit counselor someone who is available to help people with credit problems.

Credit limit a maximum amount that may be owed at one time.

Credit rating a person’s reputation for paying bills on time.

Credit references businesses or individuals who are able and willing to provide information about your creditworthiness.

Credit report a document that shows the debts a person owes, how often credit is used, and whether he or she pays debts on time.

Credit union a user-owned, not-for-profit, cooperative financial institution.

Creditor one who sells on credit or makes a loan; the purchaser of a corporate or government bond.

Culture the accepted behaviors, customs, and values of a society.

Current assets cash and those items that can be readily converted to cash such as inventory and accounts receivable.

Current income income for current living expenses.

Current liabilities amounts owed by the business that will be paid within a year.

Current ratio current assets compared to the current liabilities.

Custom manufacturing building a specific and unique product to meet the needs of one customer.

Debt repayment plan an agreement between a creditor and a debtor to reduce payments to a more manageable level and still pay off the debt.

Debt to equity ratio the company’s liabilities divided by the owners’ equity.

Debtor anyone who buys on credit or receives a loan.

Decoding the interpretation of information.

Decreasing term insurance the amount of protection gradually becomes smaller, but premiums remain the same while the insurance is in effect.

Deductible clause a clause stating that the insured must pay a specified amount before the insurance company pays a claim.

Deductible clause (for major medical policies) the amount the policyholder agrees to pay—the first part of the expense resulting from the sickness or injury.

Deficit when actual spending is greater than planned spending.

Deflation a decrease in the general level of prices.

Demand the quantity of a good or service that consumers are willing and able to buy.

Demand curve the graphic view of the demand for a product or service. The demand curve for a product, for example, illustrates the relationship between the price of the product and the quantity demanded by consumers.

Department stores stores that have an extensive product line and emphasize service.

Dependent a person who must rely on another for financial support.

Depreciation the decrease in value of a property as it becomes old and gradually wears out.

Depreciation record a financial document used to identify the amount assets have decreased in value due to their age and use.

Depression the phase of the business cycle that is marked by a prolonged period of high unemployment, weak consumer sales, and business failures.

Desktop publishing graphics software to prepare charts, graphs, and other visual elements.
Direct channel of distribution a channel in which products move from the producer straight to the consumer with no other organizations participating.

Direct deposit funds are deposited electronically and available automatically for your use.

Disability income insurance insurance that replaces income that is lost when you cannot work because of an illness or injury.

Discharge a type of termination that ends employment due to inappropriate work behavior.

Discount broker a stockbroker who places orders and offers limited research and other services.

Discount rate the rate financial institutions are charged to borrow funds from the Federal Reserve banks.

Discount stores stores that emphasize lower prices on their products.

Discounting the process in which savings bonds pay interest.

Discrepancies differences between actual and budgeted performance.

Displaced workers workers who are unemployed because of changing job conditions.

Distribution determining the best ways for customers to locate, obtain, and use the products and services of an organization.

Diversity the comprehensive inclusion of people with differences in personal characteristics and attributes.

Dividends payments of profits in cash to stockholders.

Domestic business the making, buying, and selling of goods and services within a country.

Down payment a payment of part of the purchase price, usually made at the time of purchase.

Downsizing a planned reduction in the number of employees needed in a firm in order to reduce costs and make the business more efficient.

Drawee the bank or other financial institution that pays the check.

Drawer the owner of the account who signs the check.

Earnings report a report, usually included with the employee's paycheck, that includes information for the current pay period as well as the cumulative amounts for the year.

E-commerce conducting business transactions using the Internet or other technology.

Economic decision-making the process of choosing which wants, among several options, will be satisfied.

Economic resources the means through which goods and services are produced.

Economic risk a risk that can result in financial loss, including personal risk, property risk, and liability risk.

Economic system a nation's plan for answering the three economic questions.

Effective communication the exchange of information so there is common understanding by all participants.

EFT. See Electronic funds transfer

Electronic funds transfer (EFT) refers to the use of computers and other technology for banking activities, including the use of automated teller machines (ATM), point-of-sale transactions, direct deposit, and automatic bill payment.

Embargo an action imposed by the government to stop the export or import of a product completely.

E-money a medium of exchange for online transactions.

Emotional buying motives reasons consumers decide what products and services to purchase based on feelings, beliefs, and attitudes.

Employee relations responsible for maintaining a safe, healthy, and productive work environment for all employees.

Employment interview a two-way conversation in which the interviewer learns about you and you learn about the job and the company.

Encoding preparing the information to be communicated.

Endorsement written evidence that a person received payment or transferred the right to receive payment to someone else.
Entrepreneur someone who takes a risk in starting a business to earn a profit.

Entrepreneurship the process of starting, organizing, managing, and assuming the responsibility for a business.

Equal Opportunity Act a law that prohibits creditors from denying a person credit because of age, race, sex, or marital status.

Equity stock ownership; the difference between the price at which you could currently sell your house and the amount owed on the mortgage.

Estate planning a plan that involves the accumulation and management of property during one's lifetime and the distribution of one's property at death.

Ethical business practices practices that ensure the highest standards of conduct are observed in a company's relationships with everyone who is a part of the business or affected by the business' activities.

Ethics principles of morality or rules of conduct.

Exchange rate the value of a currency in one country compared with the value in another.

Executives top-level managers with responsibilities for the direction and success of the entire business.

Exit interview an interview in which your employer asks questions about your work upon leaving the company.

Expenses costs of operating a business.

Experienced-based resume a resume in which experiences are usually listed in order of work history.

Experiment a method of marketing research which presents two carefully controlled alternatives to subjects in order to determine which is preferred or has better results.

Expert influence influence that arises when group members recognize that the leader has special expertise in the area.

Expert systems computer programs that help people solve technical problems.

Exports goods and services sold to other countries.

Express money order a form issued by various organizations including traveler's check companies, travel agencies, and many supermarkets, pharmacies, and convenience stores.

Express warranty a warranty that is made orally or in writing and promises a specific quality of performance.

External communications communications that occur between those inside the organization and outsiders such as customers, suppliers, and other businesses.

External data sources input provided to the management information system from outside an organization, such as financial institutions, government agencies, and customers.

Extraction and cultivation a form of production in which products are obtained from nature or grown using natural resources.

Extractor a business that takes resources from nature for direct consumption or for use in developing other products.

Face value the amount of insurance coverage that was originally purchased and that will be paid upon the death of the insured.

Factors of production economic resources, including natural resources, human resources, and capital resources.

Fair Credit Reporting Act a law that requires prompt correction of billing mistakes.

Fair Debt Collection Practices Act a law requiring that debt collectors treat you fairly. It bans various debt collection actions.

Family leave a policy that allows employees to take a leave of absence for the birth or adoption of a child, to care for a sick family member, or for other personal emergencies.

Farmer people who cultivate land and use other natural resources to grow crops and livestock for consumption.

Federal Deposit Insurance Corporation (FDIC) the federal agency that helps to regulate banks and other financial institutions.

Federal Reserve System (Fed) a system set up by the federal government to supervise and regulate
member banks and to help banks serve the public efficiently. All national banks are required to join the Federal Reserve System, and state banks may join.

**Feedback**
a response to the sender from the receiver.

**Final consumers** persons who buy products and services mostly for their own use.

**Finance charge** the total dollar cost of credit including interest and all other charges.

**Financial performance ratios** comparisons of a company's financial elements that indicate how well the business is performing.

**Financial plan** a report that summarizes your current financial condition, acknowledges your financial needs, and sets a direction for your future financial activities.

**Financial records** financial documents that are used to record and analyze the financial performance of a business.

**Financial responsibility law** a law that protects the public from financial loss caused by drivers.

**Financial statements** reports that sum up the financial performance of a business.

**Financing** budgeting for marketing activities, obtaining the necessary funds needed for operations, and providing financial assistance to customers so they can purchase the business' products and services.

**Fixed expenses** costs that occur on a regular basis and are for the same amount each time.

**Full endorsement (special endorsement)** an endorsement that allows you to transfer a check to another person.

**Full-service broker** a broker who provides information about securities you may want to buy. They work for brokerage houses with large research staffs.

**Full-time employee** one who regularly works a schedule of 30 hours or more a week.

**Future contract** contract involving the buying and selling of currencies and financial instruments.

**GDP per capita** the output per person, calculated by dividing gross domestic product (GDP) by the total production.

**GDP.** See **Gross domestic product**

**Generic products** unbranded items at reduced prices because they do not require advertising and fancy packaging.
Glass ceiling an artificial limit placed on minority groups moving into positions of authority and decision-making.

Global strategy a strategy that uses the same product and marketing strategy worldwide.

Goal a precise statement of results the business expects to achieve.

Goods things you can see and touch; they are products you can purchase to meet your wants and needs.

Goods-producing industries businesses that produce or manufacture products used by other businesses or purchased by final consumers.

Graphics output includes processing results such as company logos, photos, drawings, scrolling messages, and animated graphics.

Gross domestic product (GDP) the total dollar value of all final goods and services produced in a country during one year.

Gross margin the difference between the selling price and the product costs.

Group insurance health insurance coverage offered to a large number of employees and their family members.

Group life insurance an insurance policy that covers a group of people. The group acts as a single unit in buying the insurance.

Guarantee a promise by the manufacturer or dealer, usually in writing, that a product is of a certain quality.

Guarantee (warranty) an offering designed to build customer confidence in a company’s products.

Heterogeneous characterized by the differences in the type and quality of service provided.

HMO. See Health maintenance organization

Homeowners policy a very convenient package-type insurance policy designed to insure homes and property.

Horizontal communications communications that move across the organization at the same level—employee to employee or manager to manager.

Hospital insurance insurance that usually pays most or all hospital charges if an illness or injury requires the insured to be hospitalized.

Host country the country in which the multinational company (MNC) places business activities.

Human relations the way people get along with each other.

Human resources people producing goods and services.

I

I bond a bond that pays an interest rate that is lower than the rate of other savings bonds, but it is a variable rate that increases with inflation.

Identity influence influence that stems from the personal trust and respect members have for the leader.

Identity theft stealing information about a person from online sources to obtain money.

Implementing a manager’s effort to direct and lead people to accomplish the planned work of the organization.

Implication warranty a guarantee imposed by law and is understood to apply even though it has not been written or stated.

Imports items brought from other countries.

Improvement a designed change that increases the usefulness of a product, service, or process.

Impulse buying the opposite of spending time and effort is buying too quickly.

Incentive systems the amount of compensation connected to the quality or quantity of an employee’s performance.
Income statement  a report of revenue, expenses, and net income or loss from operations for a specific period.

Income tax  taxes levied on the income of individuals.

Indirect channel of distribution  a channel in which products move from the producer to the consumer through one or more other businesses.

Individual retirement account (IRA)  a tax-sheltered retirement plan in which people can annually invest earnings up to a certain amount.

Inflation  an increase in the general level of prices.

Influence  power enabling a person to affect the actions of others.

Informal communications  common but unofficial ways that information moves in an organization.

Informal influence  a leadership role that is not part of a formal structure.

Information management  using technology to access and exchange information to complete the work of an organization.

Informational interview  a planned discussion with a worker who is willing to help you find out about the work that a person does, the preparation needed for that career, and the person’s feelings about the career.

Infrastructure  a factor that supports international trade in industrialized countries, including a nation’s transportation, communication, and utility systems.

Innovation  an invention or creation that is brand new.

Inseparable  something that is consumed at the same time it is produced.

Installment loan  a loan in which you agree to make monthly payments in specific amounts over a period of time.

Installment sales credit  a type of credit contract issued by the seller that requires periodic payments at specified times. The seller adds finance charges to the cost of the items purchased.

Installments  a specified amount a borrower agrees to repay for a loan.

Insurable interest  a financial benefit from an insured person’s continued life.

Insurable risk  when a large number of people face a given risk and the cost of the possible losses can be predicted.

Insurance  a form of risk protection that exchanges the uncertainty of a possible large financial loss for a certain smaller payment.

Insurance agent  an agent who represents the insurance company and sells insurance policies to individuals and businesses.

Insurance policy  a policy stating the conditions to which the insurance company and the policyholder have agreed.

Insured  the person or business for which the insurer assumes the risk.

Insurer  a company that agrees to take on certain economic risks and to pay for losses if they occur.

Intangible  something that has no physical form.

Intellectual property  technical knowledge or creative work. It includes software, clothing designs, music, books, and movies.

Interest  the money you receive for letting others use your money.

Interest rates  the cost of using someone else’s money.

Interests  activities that give you satisfaction and that can provide a basis for your employment goals and possible career paths.

Intermediaries  businesses involved in selling the goods and services of producers to consumers and other businesses.

Intermittent processing  using short production runs to produce a precise amount of a variation of a product.

Internal communications  communications that occur between managers, employees, and work groups.

Internal data sources  input provided to the management information system from within the organization, such as accounting records, inventory information, and company sales figures.
International business  business activities needed for creating, shipping, and selling goods and services across national borders.

Internships  the involvement of work experience in organizations while learning about a career field.

Interstate commerce  business dealings involving companies in more than one state.

Intranet  a local computer network based on the same communication standards as the internet. It looks like and functions just like a typical web site, but it is private and only accessible to authorized users.

Intrastate commerce  business dealings involving companies that do business in only one state.

Inventory  a detailed account of a company’s materials, supplies, and finished products.

Inventory management  maintains the supply of all resources needed for production and the products produced.

Inventory records  a financial document used to identify the type and number of products on hand for sale.

Investing  using your savings to earn more money.

IRA. See Individual retirement account

Labor union  an organized group of employees who negotiate with employers about issues, such as wages and working conditions.

Layoff  a type of termination which is a temporary or permanent reduction in the number of employees due to changing business conditions.

Leadership  the ability to motivate individuals and groups to accomplish important goals.

Level term insurance  the amount of protection and the premiums remain the same while the insurance is in effect.

Liabilities  what a company owes.

Liability insurance  protection against losses from injury to people or property resulting from the products, services, or actions of a business.

Liability risk  a risk that relates to harm or injury to other people or their property because of your actions.

Licensing  selling the right to use some intangible property (production process, trademark, or brand name) for a fee or royalty.

Life cycle  when each stage of life is distinguished by unique characteristics, requirements, and expectations.

Life insurance  insurance that pays the amount of the insurance policy upon the death of the insured. The payment is made to people named in the policy known as beneficiaries.

Light pens  handheld input devices that detect the presence of light.

Limited liability company  provides liability protection for owners. it has a simpler set of organizing and operating requirements than a corporation. No articles of incorporation or bylaws are needed. A simple document much like a partnership agreement must be developed.

Limited liability partnership  a partnership that identifies some investors who cannot lose more than the amount of their investment, but they are not allowed to participate in the day-to-day management of the business.

Limited-payment policies  a whole life insurance policy that is designated by the number of years
the policyholder agrees to pay on it, such as a 20-payment life policy.

Liquidity  the ease with which an investment can be changed into cash without losing its value.

Loan credit  borrowed money for special use. It usually involves a written contract.

Locational unemployment  occurs when jobs are available in one place but go unfilled because those who are qualified to fill those jobs live elsewhere and are not willing to relocate.

Logistics  managing the acquisition, movement, and storage of supplies, materials, and finished products in a business.

Long-term assets (fixed assets)  the assets with a lifespan of more than a year, such as land, buildings, equipment, and expensive technology.

Long-term care insurance  insurance that provides long-term care including daily assistance needed because of a long-term illness or disability.

Long-term financing  the money needed for the main resources of a business (such as land, buildings, and equipment) that will last for many years.

Long-term liabilities  business debts that will continue for longer than a year.

They sell their products to consumers and other businesses.

Manufacturing  combining raw materials and processed goods into finished products.

Markdown  a reduction from the original selling price.

Market economy  an economy in which the resources are owned and controlled by the people of the country.

Market price  the point where supply and demand are equal.

Market value  the price at which a share of stock can be bought and sold in the stock market.

Marketing  the process of planning and executing the conception, pricing, promotion, and distribution of ideas, goods, and services to create exchanges that satisfy individual and organizational objectives.

Marketing mix  the blending of four marketing elements—products, distribution, price, and promotion.

Marketing orientation  an approach that considers the needs of customers when developing a marketing mix.

Marketing research  finding solutions to problems through carefully designed studies involving customers.

Marketing strategy  a company’s plan that identifies how it will use marketing to achieve its goals.

Marketing-information management  obtaining, managing, and using market information to improve business decision-making and the performance of marketing activities.

Markup  the amount added to the cost of a product to set the selling price.

Mass production  an assembly process that makes a large number of identical products using a continuous efficient procedure.

Mass promotion  communication to many people at the same time with a common message.

Materials processing  changing the form of raw materials so they can be consumed or used to make other products.
Maturity date the date on which a loan must be repaid.

Maturity value (face value) the amount being borrowed by the corporation issuing the bond.

Mediation involves the use of a third party who tries to resolve the complaint between the consumer and the business.

Medicaid a form of medical aid to low-income families administered by state governments. The federal government shares the cost of providing health benefits to financially needy families.

Medical payments insurance that covers policyholders and family members if they are injured while riding in their car or another car.

Memory a component of a computer system that stores a computer program.

Mentor an experienced employee or “career coach” who serves as counselor to a person with less experience.

Microphones and cameras input devices that allow input of audio and video.

Mid-managers specialists with responsibilities for specific parts of a company’s operations.

MIS. See Management information system

Mission statement a short, specific written statement of the reason a business exists and what it wants to achieve.

Mixed economy an economy that combines elements of the command and market economies.

Mixed management the combine use of tactical and strategic management styles.

MNC. See Multinational company

Mobility the willingness and ability of a person to move to where jobs are located.

Money management the day-to-day financial activities associated with using limited income to satisfy your unlimited needs and wants.

Money market account an account that pays a variable interest rate based on various government and corporate securities.

Money order a form of payment that orders the issuing agency to pay the amount printed on the form to another party.

Monopoly when a business has control of the market for a product or service.

Mortgage a legal document giving the lender a claim against the property if the principal, interest, or both are not paid as agreed.

Mortgage rate the amount individuals pay to borrow for the purchase of a new home.

Multinational company (MNC) an organization that does business in several countries. It usually consists of a home country and divisions or separate companies in one or more host countries.

Multinational strategy a strategy that treats each country market differently. Firms develop products and marketing strategies that adapt to the customs, tastes, and buying habits of a distinct national market.

Municipal bonds bonds issued by local and state governments.

Mutual fund an investment fund set up and managed by companies that receive money from many investors.

Mutual savings bank a savings bank that is owned by, and operated for the benefit of, its depositors.

N

National brands brands that are advertised all over the country.

National debt the total amount owed by the federal government.

Natural resources raw materials supplied by nature.

Needs things that are required in order to live.

Negative or unfavorable balance of payments the result of a country sending more money out than it brings in.

Net income occurs when revenue is greater than expenses.

Net income ratio the total sales compared to the net income for a period such as six months or a year.

Net loss occurs when expenses are greater than income.

Net worth the difference between a person’s assets and liabilities.
Networking the process of talking to other people about their jobs.

No-fault insurance insurance allowing people who are injured in an automobile accident to collect for their financial losses from their own insurance companies no matter who is at fault. Those losses include their medical bills, loss of wages, and other related expenses.

Non-depository intermediaries a category of financial institutions that does not take or help deposits. They earn their money selling specific services or policies.

Non-renewable resource a natural resource that cannot be replaced when used up.

Observations a marketing research study that collects information by recording the actions of consumers rather than asking them questions.

Occupation a task or series of tasks that is performed to provide a good or service. People are hired to fill occupations, and they are paid for the work they perform.

Operating budget describes the financial plan for ongoing operations of the business for a specific period of time.

Operating expenses all of the expenses of operating the business that are associated with the product.

Operating system software a computer program that translates commands and allows application programs to interact with the computer’s hardware.

Operational plan identifies how work will be done, who will do it, and what resources will be needed.

Opportunity cost the value of the next-best alternative that you did not choose.

Options choices of product features.

Oral communications communications that are word-of-mouth.

Ordinary life policy a type of whole life insurance in which premiums remain the same each year as long as the policyholder lives.

Organization chart a diagram that shows the structure of an organization, classifications of work and jobs, and the relationships among those classifications.

Organizational culture the environment in which people work, made up of the atmosphere, behaviors, beliefs, and relationships.

Organizing the function of a manager involving identifying and arranging the work and resources needed to achieve the goals that have been set.

Output a component of a computer system that presents data in a form that can be retrieved later or may be communicated immediately.

Outsourcing removing work from one company and sending it to another company that can complete it at a lower cost.

Outstanding checks checks that have not been deducted from the bank statement balance.

Over-the-counter (OTC) market a network where securities transactions occur using telephones and computers rather than on an exchange.

Owner’s equity the value of the business after liabilities are subtracted from assets; the value of the owners’ investment in the business.

Packaging protection and security for the product before it is used.

Partnership a business owned and controlled by two or more people who have entered into a written agreement.

Partnership agreement a written agreement among all owners detailing the rules and procedures that guide ownership and operations.

Part-time employee one who works a schedule with either fewer hours each day or fewer than 30 hours each week.

Patent the exclusive right of an inventor to make, sell, and use a product or process.

Payee the person to whom the check is written.

Payroll the financial record of employee compensation, deductions, and net pay.

Payroll record a financial document that contains information on all employees of the company, their compensation, and benefits.
**Payroll taxes** required federal and state payments for each employee, consisting of income taxes, Social Security, Medicare, and unemployment taxes.

**Pension** a series of regular payments made to a retired worker under an organized plan.

**Performance management** evaluating the work of employees and improving performance through training and development.

**Perils** the causes of loss, such as fire, wind, or theft.

**Perishable** the availability of a service to match the demand for that service at a specific time.

**Permanent employee** one to whom the company makes a long-term commitment. It is expected that the employee will work for the business as long as the business is profitable and the employee's performance is satisfactory.

**Permanent life insurance** life insurance that has cash value and an investment feature.

**Personal assets** items of value.

**Personal income** salaries and wages as well as investment income and government payments to individuals.

**Personal liability coverage** insurance that covers claims for injuries to people or damage to property caused by you or your family.

**Personal property** property not attached to the land, such as furniture or clothing.

**Personal risk** a risk that can result in personal losses such as health and personal well-being.

**Personal selling** direct, individualized communication with prospective customers to assess their needs and assist them in satisfying those needs with appropriate products and services.

**Personal time** a few hours each month that can be scheduled for non-job activities.

**Personalized promotion** communication directly with each customer using information tailored to that person.

**Piece rate** a pay-for-performance plan in which an employee receives a specific amount for each unit of work produced.

**Piracy** stealing or illegally copying software packages or information.

**Planning** the function of a manager involving analyzing information, setting goals, and making decisions about what needs to be done.

**Planning and staffing** activities directed at identifying and filling all of the jobs in the company with qualified people.

**Point-of-sale transaction** a transaction in which a merchant accepts debit cards to pay for purchases.

**Policies** guidelines used in making consistent decisions.

**Policyholder** the person or company buying the policy.

**Pollution** occurs when the environment is tainted with the by-products of human actions.

**Position influence** the ability to get others to accomplish tasks because of the position the leader holds.

**Positive or favorable balance of payments** occurs when a nation receives more money in a year than it pays out.

**Postal money order** a form purchased from the U.S. Post Office that can be sent safely through the mail.

**Postdated check** a check that is dated later than the date on which it is written.

**Preferred provider organization (PPO)** a managed care plan that involves several health care providers, such as a group of physicians, a clinic, or a hospital.

**Preferred stock** stock that has priority over common stock in the payment of dividends.

**Premium** the amount a policyholder must pay for insurance coverage.

**Presentation software** a program that allows a speaker to show text, data, photos, and other visuals. The images may be accompanied by sound effects, music, or other audio.

**Price index** a number that compares prices in one year with some earlier base year.

**Price-earnings (P/E) ratio** the relationship between a stock’s selling price and its earnings per share.

**Pricing** setting and communicating the value of products and services.
Primary research  studies carried out to gather new information specifically directed at a current problem.

Prime rate  the rate banks make available to their best business customers, such as large corporations.

Procedure  a list of steps to be followed for performing a particular work activity.

Processed goods  products that have been changed in form to increase their value and usefulness.

Processing  changing and improving the form of another product.

Producers  individuals and organizations that determine what products and services will be available for sale.

Product  everything a business offers to satisfy a customer’s needs.

Product costs  costs to the manufacturer of producing the product or the price paid by other businesses to buy the product.

Product features  additions and improvements to the basic product.

Product/service management  designing, developing, maintaining, improving, and acquiring products and services that meet consumer needs.

Production process  the activities, equipment, and resources needed to manufacture a product.

Productivity  the production output in relation to a unit of input, such as a worker.

Profit  the amount of money available to the business after all costs and expenses have been paid.

Program  a series of detailed, step-by-step instructions that tell the computer what functions to complete.

Promissory note  a written promise to repay based on a debtor’s excellent credit history.

Promotion  any form of communication used to inform, persuade, or remind; the advancement of an employee to a position with greater responsibility.

Promotional sales  sales used to promote the selling of regular merchandise with short-term price reductions.

Property damage liability  insurance that protects a driver against claims if the insured’s car damages someone else’s property and the insured is at fault.

Property insurance  insurance that protects you from the financial loss you would incur if some of your property were lost or destroyed due to fire, theft, vandalism, flood, or other hazard.

Property rights  the exclusive rights to possess and use property and its profits.

Property risk  a risk that can lead to loss of personal or business property including money, vehicles, and buildings.

Property tax  a major source of revenue for local governments based on the value of land and buildings.

Proprietorship  a business owned and run by just one person.

Prosperity  the peak of the business cycle, it is a period in which most people who want to work are working, businesses produce goods and services in record numbers, wages are good, and the rate of gross domestic product (GDP) growth increases.

Public relations  an ongoing program of non-paid and paid communications. It is planned to favorably influence public opinion about an organization, marketing effort, idea, or issue.

Public utility  an organization that supplies a service or product vital to all people including companies that provide local telephone service, water, and electricity.

Publicity  non-paid promotional communication presented by the media rather than by the business or organization that is being promoted.

Pure research  research done without a specific product in mind with the goal of discovering new solutions to problems.

Pure risk  a risk that presents the chance of loss but no opportunity for gain.

Qualifications-based resume  a resume in which your abilities and experiences related to the job for which you are applying are highlighted.
Quota a government set limit on the quantity of a product that may be imported or exported within a given period.

Rational buying motives reasons consumers decide what products and services to purchase based on facts and logic.

Real estate land and anything that is attached to it.

Real property property permanently attached to land, such as a house or garage.

Receiver a person or organization that is being communicated to by another person or organization.

Recession the phase of the business cycle in which demand begins to decrease, businesses lower production, unemployment begins to rise, and gross domestic product (GDP) growth slows for two or more quarters of the calendar year.

Records of account a financial document used to identify all purchases and sales made using credit.

Recovery the welcome phase in the business cycle in which unemployment begins to decrease, demand for goods and services increases, and gross domestic product (GDP) begins to rise again.

References a list of people who can give a report about your character, education, and work habits. These individuals may be teachers, previous employers, supervisors, or coworkers.

Regular medical insurance insurance that covers fees for nonsurgical care given in the doctor’s office, the patient’s home, or a hospital. The policy states the amount payable for each visit or call. It also lists the maximum number of visits covered.

Renewable term insurance an insurance policy that allows the policyholder to continue term insurance for one or more terms without taking another physical examination.

Renters policy a property and liability insurance policy suitable for renters. It covers household goods and personal belongings and protect against the same kinds of perils covered by homeowners policies.

Replacement insurance insurance in which the insurance company actually replaces an item that have been destroyed. No depreciation is deducted.

Responsibility the obligation to complete specific work.

Restrictive endorsement an endorsement that limits the use of the check to the purpose given in the endorsement.

Resume a tool that provides information about you to a potential employer.

Retail sales the sales of durable and nondurable goods bought by consumers.

Retailers the final business organization in an indirect channel of distribution for consumer products.

Return on equity ratio the net profit of the business compared to the amount of owners’ equity.

Revenue all income that a business receives over a period of time; government income.

Revolving account allows account holder to charge purchases at any time, but only part of the debt must be paid each month.

Reward influence the ability of a leader to give or withhold rewards.

Risk the possibility of incurring a loss.

Robotics mechanical devices programmed to do routine tasks, such as those in many factories.

Safe-deposit boxes well-guarded vaults for storage of valuables offered by banks.

Salary and wages direct payment of money to an employee for work completed.

Sales credit involves the use of charge accounts and credit cards by consumers purchasing goods and services.

Sales promotion activities and materials designed to reinforce a company’s brand and image. It is also a direct incentive to take an action likely to immediately increase sales of a product or service.

Sales tax a state or local tax on goods and services that is collected by the seller.

Saving the storage of money for future use.
SBA. See Small Business Administration

Scanners input devices that translate words and photos into computer-readable formats.

Scarcity not having enough resources to satisfy every need.

Schedule a time plan for completing activities. It matches people with resources to make sure activities are finished on time.

S-corporation a corporate form of business that offers the limited liability of a corporation.

Secondary research analyzing existing information gathered for another purpose but used to solve a current problem.

Secured loan a loan in which you must put up property or collateral as security for repayment.

Selling communicating directly with potential customers to determine and satisfy their needs.

Selling price the price paid by the customer for the product.

Sender a person or organization that has information to communicate to another person or organization.

Service business a business that carries out activities that are consumed by its customers.

Service charge the fee a bank charges for handling a checking account.

Service fee a charge involving the time and money it takes a creditor to investigate your credit history, process your loan or charge account application, and keep records of your payments and balances.

Service-producing industries businesses that perform services that satisfy the needs of other businesses and consumers.

Services activities that are consumed at the same time they are produced.

Share draft a checking account at a credit union.

Shareholders members of credit unions.

Short-term financing the money needed to pay for the current operating activities of a business.

Signature card a document used to verify your signature.

Simple interest the interest on single-payment loans.

Single-payment loan a loan in which you do not pay anything until the end of the loan period, possibly 60 or 90 days. At that time, you pay the full amount you borrowed plus the finance charge.

Small business an independent business with fewer than 500 employees.

Small Business Administration (SBA) a government agency that helps small business owners develop business plans and obtain financing and other support for their companies.

Small claims court a court system in every state that exists to resolve cases involving small amounts.

Smart cards plastic cards with silicon chips that are used to store information. The chip within the card stores such data as your current account balance and credit history or medical information.

Social responsibility the duty of a business to contribute to the well-being of a community.

Software the instructions that run the computer system.

Span of control the number of employees who are assigned to a particular work task and manager.

Special checking account checking accounts for people who only write a few checks each month. Banks charge customers about 10 to 20 cents for each check written.

Special form a form of a homeowners policy that insures property against all perils except earthquakes, flood, war, nuclear accidents, and certain others.

Specialty stores stores that have a special line of products for sale.

Specialty superstores stores that offer low prices and a wide variety of a limited product line.

Speculative risk the chance either to gain or to lose.

Spreadsheet software a program that formats data in columns and rows in order to do calculations.

Staffing the function of a manager including all of the activities involved in obtaining, preparing, and compensating the employees of a business.
Standard a specific measurement against which an activity or result is judged

Start-up budget plans income and expenses from the beginning of a new business or a major business expansion until it becomes profitable.

Start-up financing the amount of money needed to open the business.

Statement of account a record of the transactions completed during the billing period.

Stock ownership in a corporation.

Stock certificate a printed form showing ownership of shares in a corporation.

Stock exchange a business organization that accommodates the buying and selling of securities.

Stock index a measurement of investment values.

Stockbroker a licensed specialist in the buying and selling of stocks and bonds.

Stop payment order a written notice that tells the bank not to pay a certain check.

Store brands (private label brands) brands owned by stores. For example, Craftsman is one of the brand names on tools sold by Sears.

Straight salary a specific amount of money paid to an employee for each week or month worked.

Strategic management a style in which managers are less directive and involve employees in decision-making.

Substitution check a digital reproduction of the original paper check.

Supermarket in food retailing, it is the large, full-service store that carries name brands.

Superstores discount stores that have expanded to include a wide variety of food products. They may also include other retail services such as a bakery, restaurant, pharmacy, video rentals, and banking.

Supervisors the first level of management in a business, responsible for the work of a group of employees and some non-management duties.

Supply the quantity of a good or service that businesses are willing and able to provide.

Supply chain management an approach to managing operations as a collaborative network that enhances the flow of materials and information from suppliers to the final customer. It reduces the cost and time of the whole process, and improves the quality of products and services.

Supply chain management software software that allows cooperating companies to share ordering, production, and shipping information.

Supply chain management. See Logistics

Supply curve the graphic view of the supply for a product or service. The supply curve for a product, for example, illustrates the relationship between the price of the product and the quantity businesses will supply.

Surgical insurance insurance that covers all or part of the surgeon's fees for an operation.

Surplus when actual spending is less than the budgeted amount.

Surveys a marketing research study that gathers information from people using a carefully planned set of questions.

T

Tactical management a style in which the manager is directive and controlling.

Take-home pay the amount of a paycheck after taxes and other payroll deductions.

Talent a natural, inborn aptitude to do certain things.

Target market a specific group of customers that have similar wants and needs.

Targeted application letter a letter that provides a quick summary of your ability to meet the needs of an organization. It usually includes a list of major skills and competencies.

Tariff a tax that a government places on certain imported products.

Tax record a financial document that shows all taxes collected, owed, and paid.

Tax-deferred the investment earnings on the retirement plan will be taxed later, after retirement.

Tax-exempt earnings being exempt from paying taxes on investment income.

T-bill rate the yield on short-term (13-week) U.S. government debt obligations.

Technology the use of automated machines, electronic equipment, and integrated computer systems to help increase the efficiency of producing goods and services.

Telecommuting allows employees who primarily use personal computers and other technology to work from home. They communicate with
Managers, coworkers, and customers using the Internet, telephone, and fax machines.

**Temporary employee** one hired for a specific time or to complete a specific assignment.

**Tentative career decision** a decision that is subject to change as new information is received.

**Term life insurance** insurance that provides financial protection from losses resulting from a death during a definite period or term.

**Termination** the end of an employment relationship between a company and an employee.

**Text output** includes processing results displayed on a computer screen (monitor) or in a printed report.

**Time wage** a specific amount of money paid to an employee for each hour worked.

**Trade barriers** restrictions to free trade.

**Trade deficit** a situation in which a country imports (buys) more than it exports (sells).

**Trade surplus** a situation in which a country exports (sells) more than it imports (buys).

**Trademark** a distinctive name, symbol, word, picture, or combination of these that a company uses to identify products or services.

**Tradeoff** what you make when you give something up to have something else.

**Traditional economy** an economy in which goods and services are produced the way they have always been produced. It is used in countries that are less developed and are not yet participating in the global economy.

**Transfer** the assignment of an employee to another job in the company with a similar level of responsibility.

**Traveler’s checks** special forms designed for making payments when away from home.

**Treasury bills (T-bills)** bills that involve short-term borrowing with maturities from 91 days to one year.

**Treasury bond rate** the yield on long-term (20-year) U.S. government debt obligations.

**Treasury bonds (T-bonds)** bonds that involve long-term borrowing, with maturities ranging from 10 to 30 years.

**Treasury notes (T-notes)** note that involve borrowing with maturities from 1 to 10 years.

**Truth-in-Lending Law of 1968** the first in a series of credit protection laws, it requires that borrower’s be told the cost of credit before signing an agreement. It requires that the lender must clearly state the annual percentage rate (APR) and total finance charge. It also protects consumers against unauthorized use of credit cards.

**Truth-in-Savings law** a law requiring that financial institutions give consumers information to compare savings accounts.

**U**

**Uncontrollable risk** a risk that cannot be reduced by your actions.

**Unemployment insurance** insurance to reduce financial hardship of unemployment.

**Unemployment rate** the portion of people in the labor force who are not working.

**Uninsurable risk** when a risk is not common or if it is impossible to predict the amount of loss that could be suffered.

**Uninsured motorist** protection against hit-and-run drivers or drivers without insurance money to pay claims.

**Unit price** a price per unit of measure.

**Unity of command** a clear reporting relationship for all staff of a business.

**Universal life insurance** insurance that provides both insurance protection and a substantial savings plan.

**Upkeep** maintaining your property in good condition.

**V**

**Values** things that are important to you.

**Variable expenses** living costs that differ each time and may not be as easy to estimate.

**Variable life insurance** an insurance plan that resembles an investment portfolio. It lets the policyholder choose among a broad range of investments.
Vehicle insurance coverage of automobiles, trucks, and other business vehicles.

Vending machines non-store shopping where customers can shop for items by putting money into machines.

Venture capital money provided by large investors to finance new products and new businesses that have a good chance to be very profitable.

Vertical communications communications that move up or down in an organization between management and employees.

Video output processing results that may be in the form of a training film, television commercial, or news report.

Videoconferencing allows people in different geographic locations to meet “face-to-face” by satellite.

Voice-activated systems input devices that allow you to enter data or commands with a microphone, with the computer translating your words into instructions.

White-collar crime illegal acts carried out by office or professional workers while at work.

White-collar worker one whose work is more mental than physical and involves the handling and processing of information.

Whole life insurance permanent insurance that extends over the lifetime, or whole life, of the insured.

Work environment the physical conditions and the psychological atmosphere in which employees work.

Workers’ compensation an insurance plan that provides medical and survivor benefits for people injured, disabled, or killed on the job.

Workforce all of the people 16 years or older who are employed or who are looking for a job.

World trade. See International business.

Written communications communication that include notes, letters, reports, and e-mail messages.

Y

Yield the percentage of money earned on your savings or investment over a year.

W

Wants things that add comfort and pleasure to your life.

Warehouse club a no-frills outlet focusing on the sale of large quantities at reasonable prices.
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