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CRIB NOTES

A Cheat Sheet for Time-Pressed Readers Who Need Help Now

IF YOU'RE OVERWHELMED by the idea of diving into a whole book on personal finance, this chapter is for you. It cuts to the chase and sets you on the path to a solid financial life. No kidding around: Adopting even one or two of these strategies will put you ahead of the game and—I promise—make a big difference sooner than you think.

Of course, as someone's mother once said, cheaters only cheat themselves. And while this chapter is a good launching pad, ignoring the remaining nine chapters is a little like relying on the SparkNotes version of *Hamlet*: You'll get the basic plotline but never understand what all the fuss is about. That said, the following crib notes will give you the "need to know" basics. I've tried to list the advice in rough order of importance, but your priorities will depend on your own situation, of course.

1. Insure yourself against financial ruin.

You need health insurance. Period. As of this writing, the law requires that you have it. Even more important: It'll help protect you if you have an accident or illness, and guarantee that you don't bankrupt yourself—or your family—if you run into any serious

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medical problems. For these reasons, health insurance should be considered your number one financial priority.

If you work for a company that offers its employees health insurance, you're lucky; participating in a plan at work will almost always cost you much less than buying a policy on your own because your employer pays for part of it. Your company may offer more than one type of plan; make sure you consider not only the price but also the extent of the coverage. You'll want to find out exactly how much you'll be expected to pay out of pocket before insurance kicks in (this is known as the **deductible**), the rules for seeing specialists, and what happens if you want to visit a doctor who doesn't participate in the plan.

If your job doesn't offer coverage, you work for yourself, or you're looking for a job, you'll have to pay for it on your own. First, see if you can get coverage through a family member. Federal rules say you can be covered by your parents' insurance until you turn 26; some states will let you stay on even longer. If you're married and your spouse is insured through work, see about being added to that policy. Many companies also cover unmarried domestic partners.

If all else fails, you'll need to purchase a policy on your own. As of this writing, you can comparison shop at Healthcare.gov, sites like eHealth.com, or go directly to individual insurance companies.

For additional tips on the insurance that you need—and the kinds you should avoid—see Chapter 8.

2. Pay off your debt the smart way.

One of the smartest financial moves you can make is to take any savings you have (above and beyond money you need for essentials like rent, food, and health insurance) and pay off your high-rate loans. The reason is simple: You usually can "earn" more by paying off a loan than you can by saving and investing. That's because paying off a credit card or high-rate loan that has a 15% interest rate is equivalent to earning 15% on an investment, *guaranteed*—an extremely attractive rate of return. If you want a full explanation of this concept, turn to p. 31. Otherwise, take my word for it.

The first step in attacking high-rate debt is to try to reduce your interest rate. Start by simply calling your credit card company and asking for a lower rate. (Seriously, this often works.) Next, see if you can qualify for one of the lower-rate cards listed on sites like CreditCards.com and CardHub.com, and then transfer your remaining balance to it.

If you have several different types of debt—say, a balance on a credit card with a 15% interest rate, another credit card balance with a 12% rate, and a student loan with a 4% rate—pay off the loan with the highest interest rate first. One way to make this easier is to ask your federal student loan servicer to stretch out your payments for longer than the standard ten years by switching to a different repayment plan. This will reduce your monthly student loan payment, leaving you with extra cash, which you can use to pay off your credit card balances faster. Once you've gotten rid of your 15% card balance, increase the payments on your 12% balance. After you wipe out that one, increase your student loan payments to at least their initial levels.

The only time it doesn't make sense to kill your debt is when the interest rate you're being charged is *lower* than the rate you can receive on an investment. If, for example, you have a student loan with only a 3% rate and no other debt, you'd be better off maintaining your usual payment schedule on the loan and putting your cash into an investment that pays you an after-tax rate greater than 3%, assuming you can find it. One such place would be a 401(k) with matching contributions, which is coming up in the next point.

For detailed information on credit cards, auto loans, and student loans, see Chapter 3.

3. Start contributing to a tax-favored retirement savings plan.

This one might strike you as nuts at first. Why would you think about retirement now? But here's the reality: Saving money in a retirement plan is one of the smartest (and easiest) things you can do when you're young. If you're fortunate enough to work for a company that offers a retirement savings plan like a **401(k)**, you should take advantage of it. The big attraction here is that many

employers will match a portion of the amount you put into such a plan. That means the company contributes a set amount—say, 50 cents or a dollar—for every dollar you contribute, up to a specified percentage of your salary. That's free money, equivalent to an immediate 50% or 100% return. There's nowhere you can beat this! (In fact, if your company offers such a fabulous matching deal, you should probably contribute to the plan even before paying off your high-rate debt.) In addition, the federal government allows the money to grow tax-free. (See p. 135 for an explanation of how this saves you even more money.)

It may seem crazy to lock up your money in a retirement savings plan. Ignore that feeling. While it's true that you won't be able to withdraw your money from a 401(k) until you reach age 59½ without facing a penalty, the benefits of matching and tax-advantaged growth are so huge that this is still the best deal out there. If you switch jobs, you may be able to move your 401(k) money into your new employer's plan (or transfer it into something called an IRA; see below). Also, most plans allow employees to borrow against their retirement savings in an emergency. As of 2017, the maximum you can contribute annually is $18,000, which may be more than you can manage, but try to at least contribute the maximum amount for which you're eligible to receive matching funds.

If you don't work for an employer who offers a 401(k) or a similar retirement plan, you should start investing in an **individual retirement account (IRA)**. The most you can contribute to an IRA as of 2017 is $5,500 annually; if at all possible, contribute the maximum amount every year.

IRAs don't provide matching contributions, so putting money in one is somewhat less pressing than enrolling in a company-sponsored plan that offers a match. That said, certain IRAs known as Roth IRAs do offer one special benefit: There's no penalty for withdrawing the money you contribute to them at any time. You're not allowed to freely withdraw the interest you earned on the money you contributed until after you turn 59½. (Note that there's also something called a Roth 401(k); see p. 135.)

Bottom line: Max out your company's 401(k) up to the matching limit if you have one. If that's not an option, go with an IRA.

For all your questions on tax-favored retirement savings plans, see Chapter 6.

4. Build an emergency cushion using an automatic savings plan.

If you find it nearly impossible to save money, you're not alone. But once you've gotten rid of your high-rate debt, taken care of health insurance, and started saving for retirement, it's time to begin stashing away three to six months' worth of living expenses.

Your safest choice is to have money automatically withdrawn from each paycheck and funneled into an old-school savings account. That's a relatively painless way to force yourself to accumulate a cushion. The downside to all that safety? Interest rates on savings accounts are generally low, though Internet-only banks tend to offer slightly better rates.

At various times, a type of investment called a **money market fund**, aka a money fund, which is considered almost as safe as a traditional bank savings account, has tended to pay higher interest rates. To comparison shop for the best rates on money funds, check out iMoneyNet.com and Cranedata.com. You can set up an automatic transfer from your checking account once or twice a month so it's as easy as saving in a bank savings account. (For more on money market funds, see Chapter 5.)

No matter what type of automatic savings plan you choose, focus on your goal of accumulating that emergency cushion. To figure out how much you need to save, use the worksheet (Figure 2–2) on p. 16.

5. Consider investing in stock and bond funds.

Once you have your savings cushion in a low-risk bank account or money market fund, it's time to get more aggressive with your investments. The advantage of stocks and bonds is that they've tended to earn more for investors over long periods of time, yielding higher returns that stay ahead of inflation. (For a discussion of inflation and why you need to worry about it, see Chapter 5.)

The downside of stocks and bonds is that they're riskier than savings accounts or money market funds. Translation: You can lose

money by investing in them. So for money that you absolutely need to be there—say you've set it aside for a down payment on a home in a couple of years—don't invest it in stocks or bonds.

Only you can decide how much risk you're willing to accept, but there's an old rule of thumb that you subtract your age from 100, and that's the percentage of your investment money that should be in stocks; the rest should be in bonds and money market funds. Like any generalization, this one has to be tailored to your specific situation, but it can be a useful starting point.

If you do decide to put some of your money in stocks and bonds, invest it in **funds**, a type of investment that pools together the money of thousands of people. Here are some general rules: Avoid investing in funds with a **load**, which is the commission that some companies charge each time you put money into or take money out of a fund. They don't perform any better on average than no-load funds, so there's no point in paying extra for them. I also recommend that you consider only funds with low **expenses**, the annual fees charged by the fund that can take a huge bite out of your investment returns if you're not careful.

Although stock funds are considered somewhat riskier than bond funds (see below), they have also performed somewhat better over long periods of time. If you decide to invest in a stock fund, I like low-cost **stock index funds** and **exchange-traded funds (ETFs)**. (To find out exactly what these are, you'll need to read Chapter 5.)

Two companies that offer a large selection of low-cost index funds are Charles Schwab (Schwab.com) and Vanguard (Vanguard .com). You'll generally need to commit $1,000 to $3,000 to open an account if you want to invest in their stock index funds. If you don't have a lot of money, for about $100 you can start investing in a Vanguard ETF. (See p. 124 for more details.)

Holding bonds as well as stocks will help to diversify your investments, reducing your overall risk. Vanguard also offers low-cost bond funds. While there are several different types of bond funds, a reasonable approach would be to choose a **bond index fund** that invests in government securities or highly rated corporations.

To learn more about stocks, bonds, index funds, ETFs, and investing in general—you guessed it—you'll have to read Chapter 5.

6. Find out your credit score and improve it.

A **credit score** is the number that tells lenders whether or not you're a good risk. The score is based on information about you kept by the three major credit bureaus: Equifax, TransUnion, and Experian. These records, which include information received by the bureaus from your various lenders, are called your **credit reports**. You're legally entitled to one free report from each of the bureaus every year from AnnualCreditReport.com. It's smart to check your credit reports to make sure all the information included about you is accurate.

You can think of your credit score as the GPA of your financial abilities, a numerical representation of how appealing you are to lenders. Unlike your GPA, however, your credit score is being recalculated all the time. If you want to qualify for a low-rate credit card, car loan, or home loan; rent an apartment; or get insurance, your credit score will matter. You can get a free version of your credit score at CreditKarma.com, which also offers unlimited access to the information in your credit reports from Equifax and TransUnion. Before you apply for a loan, it may make sense to get your "official" credit scores from all three bureaus (they often vary) at myFICO.com for about $60. (See Chapter 3 for details.)

The better your credit score, the better the loan deals you'll get. For that reason, it's important to take steps to make sure your score is as good as it can be. The biggest component of your credit score is your track record for making on-time payments, followed by the amount of credit you're using and the length of your credit history. One of the easiest, most foolproof ways to keep your score in good shape is to pay all of your bills automatically online. That way, you'll be much less likely to miss a payment. For more on your credit—including how to fix and prevent identity theft—see p. 60.

7. Think hard before buying a house or apartment.

At some point in the next few years you may start to feel that it's time to purchase a home of your own. The decision about whether to switch from renter to owner involves more than simply comparing your monthly rent to the mortgage payments you'd make as an owner. A range of financial factors should enter into your decision, including the tax break you'll get from buying, the fees you'll pay when you buy, and how long you plan to live in the new home. For a discussion of how to analyze your own situation, see Chapter 7.

If you do decide that it's time to buy, you'll need to apply for a home loan, or a **mortgage**. One of the obstacles for first-time home buyers is coming up with the down payment required by the lender. You will likely need to have an amount equal to at least 10% (and ideally 20%) of the purchase price of the home. In addition, you will need a good credit score. You will also have to prove that your salary is high enough—and your other outstanding debts low enough—to make the monthly mortgage payments.

To shop for the best mortgage deal, you'll want to look at sites like HSH.com, Zillow.com, and Bankrate.com. It's also a smart idea to check with your local bank or credit union—sometimes the best home loan deals are right in your own backyard.

But what if you're eager to buy and can't come up with the full down payment or don't have great credit? All is not lost. For several alternative loan options—as well as caveats to make sure you don't get in over your head—see p. 172.

If you don't qualify for a mortgage (and still want to buy), don't give up. Make it your goal to spend the next one to two years improving your credit score (pay those bills on time!) and saving up for a down payment. You'll be surprised how quickly you can build your credit record (and increase your savings) if you follow the steps in this book.

For more housing-related tips for renters as well as buyers, see Chapter 7.

8. Get smart about income tax.

Nobody likes paying taxes. One way to decrease the portion of your paycheck that goes to Uncle Sam is to take as many tax **deductions** as you're eligible for. Deductions are specific expenses that the government allows you to subtract from your income before calculating the amount of tax you owe.

You can take deductions in either of two distinct ways. The easiest approach is to take the **standard deduction**, which is simply a fixed dollar amount ($6,350 for singles or $12,700 for couples in 2017) that you subtract from your income. Although all taxpayers are permitted to take the standard deduction, depending on your circumstances you may wind up owing even less if you **itemize** your deductions instead. Itemizing means listing separately the specific items that are deductible under the tax laws and then subtracting their total cost from your income.

If you do itemize, you'll file a tax form called a 1040 and list your deductions. (You can use a simpler form known as the 1040EZ if you don't itemize.) Among the expenses you may be allowed to deduct on the 1040 are state and local income taxes (or sales taxes) you've paid, charitable donations, housing costs like mortgage interest and property taxes, and some medical costs. (The list of deductions begins on p. 252.)

Say you earn very little, or have children or educational expenses. You may also qualify for valuable tax **credits**, which subtract money directly from the amount you owe the government. (For a list of tax credits to consider, including help with your health insurance premiums, see p. 260.) For other ways to cut your tax bill, see Chapter 9.

When the time comes to submit your tax return to the IRS, if you earn less than $64,000, you can use irs.gov/freefile to file online without any charge. Otherwise, try the tax prep software at TurboTax.com, HRBlock.com, or TaxAct.com, which may cost about $100 if you have a complicated return. Based on the answers to a few questions, this software will also help you determine whether you will save money by itemizing, as well as all the deductions and credits available to you.

If you've read this far—it wasn't that bad, was it?—you've already done yourself some good. But why stop now? The next eight chapters go more in-depth on all of the above topics, while Chapter 10 offers information tailored to military service members, veterans, and their families.